2017 AFP

Risk Survey

REPORT OF SURVEY RESULTS

AFP® ASSOCIATION FOR FINANCIAL PROFESSIONALS

Supported by

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2017 AFP

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January 2017

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ASSOCIATION FOR FINANCIAL PROFESSIONALS

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Marsh & McLennan Companies is proud to support the annual AFP Risk Survey, which provides a snapshot of the many challenges organizations face in the current risk environment. Since we began conducting the survey in 2011, financial professionals have consistently reported the steadily increasing challenge of risk forecasting; in 2016 that challenge was particularly pronounced.

No doubt many political pollsters and pundits would agree.

Results of recent referendums in the UK and Italy, and the presidential election in the US; uncertainty over upcoming elections in France and Germany; and rising electorate frustration towards the governments of South Korea and Brazil are just some examples of the shifting geopolitical environment in which corporations must attempt to manage. The uncertainty created by interconnected regulatory, credit, interest rate and market risks are continuing to grow.

Against this backdrop, this year's survey results, which include an in-depth look at geopolitical risks, are surprising.

Nearly 90 percent of respondents indicate that exposure to uncertainty in earnings is greater than or the same as it was three years ago. Yet, only just over half of the respondents — 52 percent—have considered the impact of a geopolitical change or event on their organization's growth.

Equally surprisingly, 39 percent of those surveyed indicate that their senior leaders showed no signs of unease regarding such risks; an additional 15 percent is unsure whether their C-Suite and Board felt any apprehension regarding geopolitical risks. This data stands in contrast to a recent survey of boards of directors by the National Association of Corporate Directors, which shows that global economic uncertainty and increasing regulations are top of mind for board members.[1]

Given the potential impact of geopolitical events on company strategy and operations, forward-thinking financial leaders, treasurers and risks managers can make a valuable contribution by helping their organizations understand the potential impact of emerging and uncertain events on their operations, supply chain and customers.

This survey data provides useful benchmarks against which to consider your own organization's approach to responding to global and emerging risks. I hope you find it useful and informative.

Alex Wittenberg
Executive Director, Marsh & McLennan Companies' Global Risk Center

[1]2016–2017 Public Company Governance Survey, NACD, 2016

Introduction

In the early months of 2016, strong job numbers, declining unemployment and a less severe winter compared to recent ones instilled some confidence among business leaders. In the months that followed, brutal terrorist attacks around the world, an unexpected outcome of the Brexit referendum, a continuing migrant crisis, and a very uncertain domestic political environment in the U.S. during a general election year painted a troubling economic picture. The global economy continued to face headwinds. Equity markets which swung wildly and volatility in currency and commodity markets contributed to a sluggish global economy. At the end of the first half of 2016, the overall momentum of economic recovery remained tepid and growth appeared to be muted.

An unexpected win by non-establishment candidate Donald Trump for president of the U.S. has also added to the existing uncertainty. While his campaign was centered on bringing manufacturing jobs back to the U.S, pushing for more stringent immigration reform, repealing the Affordable Care Act and changing current trade treaties, as of this writing the president-elect and his team have softened their positions on some of these issues. Still, we can certainly expect noticeable impacts on policies and the economy with a new administration.

Managing risk and forecasting earnings in an environment steeped in volatility and uncertainty is very challenging. Business leaders are well aware that their organizations may be vulnerable to geopolitical risks; they realize the importance of focusing on minimizing risk exposure in an extremely interconnected environment. In a landscape of global uncertainty, treasury and finance professionals need the tools and resources to be on the leading edge of effectively managing risk.

In September 2016, the Association for Financial Professionals® (AFP) conducted the *2017 AFP Risk Survey*, the sixth in the series of risk surveys. This year's survey provides insights on the current risk environment, levels of uncertainty among finance professionals, steps being taken by organizations to mitigate risks and the primary drivers of uncertainty. This year's report also includes a deeper dive into geopolitical risks as well as their impact, and finance professionals' concerns about those risks. Responses from 480 senior-level corporate practitioner members formed the basis of this report.

Survey results suggest that finance professionals anticipate that forecasting risk will continue to be challenging. Organizations are actively engaged in mitigating risk exposure using various mechanisms. Geopolitical risks are definitely creating concerns for senior business leaders who are taking steps to reduce the potential impact of such risks.

The AFP Risk Survey is once again supported by Marsh & McLennan Companies and its Global Risk Center. AFP thanks Marsh & McLennan Companies for its support of the survey, for help in crafting the survey questions and for sharing its insights into current risk issues. The Research Department of the Association of Financial Professionals® is solely responsible for the content of this report.

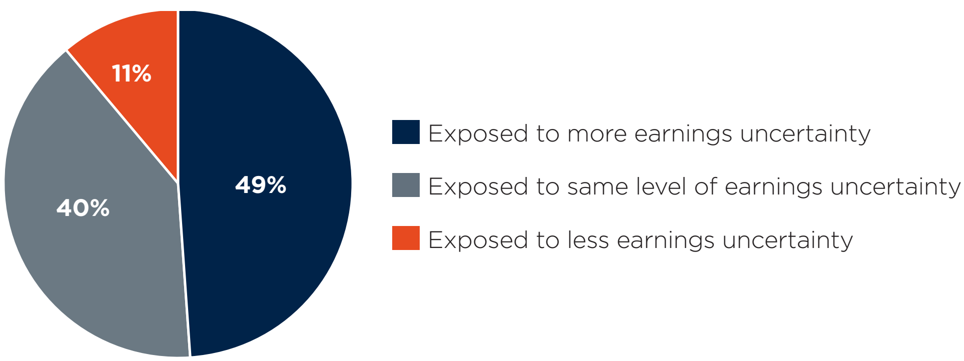
Uncertainty in Earnings Continues to Dominate

Businesses continue to be exposed to high levels of uncertainty surrounding their earnings. Forty-nine percent of finance professionals believe their organizations are exposed to greater earnings uncertainty today than three years ago. Another 40 percent indicate the level of uncertainty is unchanged and 11 percent report their organizations are exposed to less uncertainty. While still significant, the 49 percent share of respondents reporting increased exposure to earnings risk is slightly smaller than the 52 percent in the *2016 AFP Risk Survey* (reflecting data from 2015), but larger than the 43 percent in the *2015 AFP Risk Survey* (reflecting data from 2014).

Corporate practitioners from larger organizations with annual revenue of at least $1 billion (54 percent) and those that are publicly owned (56 percent) more frequently report that their companies are exposed to a greater amount of uncertainty than do their counterparts from other companies.

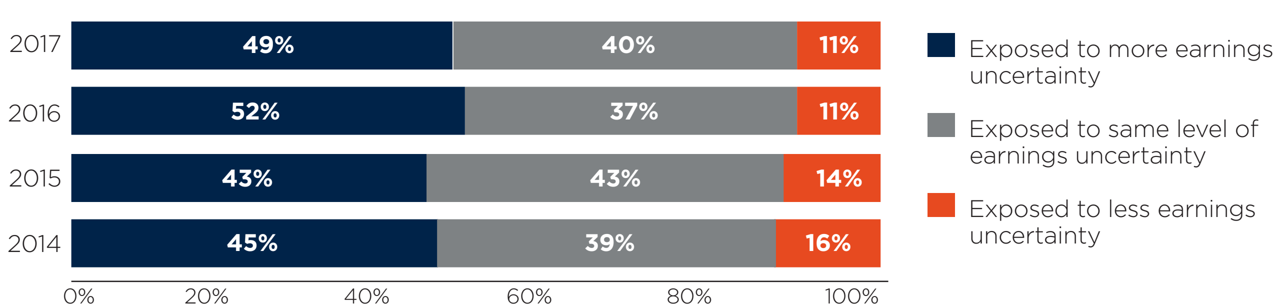
49% of survey respondents report increased exposure to earnings uncertainty in their organizations relative to three years ago

Change in Exposure to Uncertainty in Earnings Relative to Three Years Ago
(Percentage Distribution of Organizations)



The AFP Corporate Cash Indicators® released in October 2016 revealed that in the third quarter of 2016, U.S. businesses accumulated cash at a far more significant pace than ever before. This suggests that finance professionals are being extremely cautious with a continued focus on building cash reserves. Such behavior can only be expected as businesses take a "wait and see" approach, especially with regard to global issues and events. A large majority of corporate practitioners—89 percent—indicates that exposure to uncertainty in earnings is greater or the same as it was three years ago, a result similar to that reported in the 2016 survey.

Change in Exposure to Uncertainty in Earnings Relative to Three Years Ago
(Percentage Distribution of Organizations)

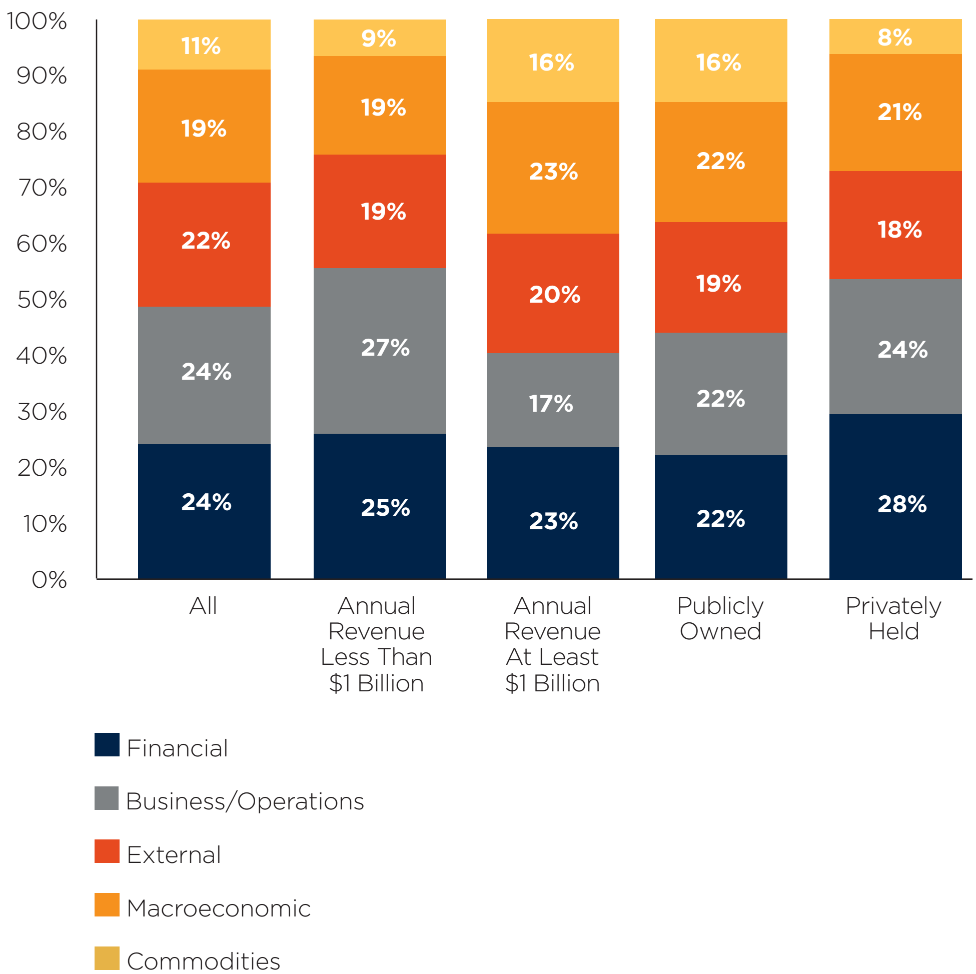


Financial Factors and Business/Operations a Top Reason for Earnings Uncertainty

Survey results show that the top two drivers of earnings uncertainty are (1) financial factors (e.g., credit, liquidity, interest rate, currency/FX) and (2) business/operations e.g. supply chain disruptions, production interruptions, litigation, labor, outsourcing, IT (each cited by 24 percent of survey respondents). External factors (country risk, regulatory, natural disaster) rank third (cited by 22 percent of respondents). These top three key factors are similar to those reported two years ago (for the *2015 AFP Risk Survey*) but differ from the top three cited in last year's survey. In the *2016 AFP Risk Survey* (reflecting data from 2015), financial factors, external factors, and commodities played key roles in earnings uncertainty—the latter not surprising as the commodities market experienced some extreme volatility in 2015. In the current survey, commodities is ranked fifth, cited by only 11 percent of finance professionals.

Financial factors and business/operations are the top two drivers of earnings uncertainty

Primary Drivers of Increase in Exposure to Earnings Uncertainty
(Percentage Distribution of Organizations that Have Experienced Greater Earnings Uncertainty)

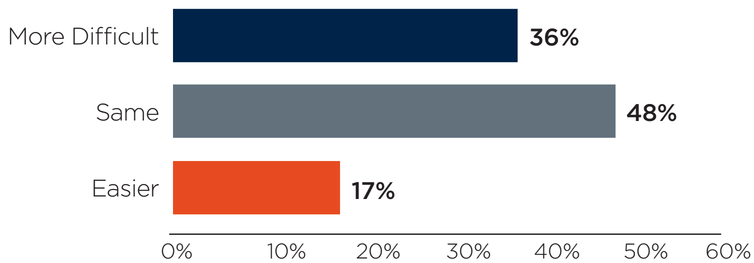


Actual and Anticipated Difficulty in Forecasting Risk

Forecasting risk continues to be a challenge for a majority of finance professionals. Eighty-four percent of them report that forecasting risk is either as difficult as or more difficult than it was three years ago. Thirty-six percent believe that forecasting is even more difficult than it was three years ago, slightly higher than the 34 percent who held this view in the previous survey, and five percentage points higher than the 31 percent reported for 2014 (in the 2015 survey). At the other end of the spectrum, only 17 percent of survey respondents indicate that forecasting risk is easier currently than it was three years ago, less than the 22 percent who held this view in last year's survey.

84% of finance professionals report that forecasting risk is as difficult or more difficult as it was three years ago

Difficulty of Forecasting Risk Today Versus Three Years Ago (2013)
(Percentage Distribution of Respondents)

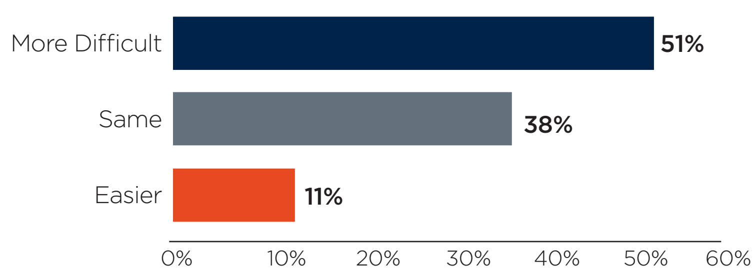


Over the six-year period AFP has been conducting these risk surveys, the share of respondents reporting that forecasting risk is a greater challenge compared to previous years has increased. There is also a consensus among finance professionals that forecasting will only become more difficult in the future. Fifty-one percent of survey respondents anticipate forecasting risk will be more difficult in three years; only 11 percent believe it will be easier. Given the current economic environment both in the U.S. and globally, most respondents expect earnings uncertainty will continue unchanged or increase in the next three years. In these circumstances, we can expect that forecasting will continue to be a challenge for finance professionals in the years to come.

One of the driving factors of the challenges of risk forecasting is highlighted by the annual *Global Risks Report* which notes the tightening links between risks and long-term global trends. Interconnected trends in geopolitics, technological advances, global economic integration, social instability and climate change, mean that the manifestation of one risk is increasingly likely to influence others with unforeseeable impacts. Risk interconnections are exacerbating volatility and creating new vulnerabilities with the potential to significantly damage organizations that have not prepared for the convergence of the old and the emerging risks.[1]

51% of survey respondents anticipate that accurately forecasting risk will be more challenging three years from now

Anticipated Difficulty of Forecasting Risk Three Years from Now (2019) Versus Today
(Percentage Distribution of Respondents)



[1] Global Risks Report, World Economic Forum, prepared with the support of Marsh & McLennan Companies and see also, Emerging Risks: Anticipating Threats and Opportunities Around the Corner, Excellence in Risk Management XIII, Marsh and RIMS, 2016.

Risk Factors Having the Greatest Impact on Earnings in the Next Three Years

There are numerous risk factors that can impact a company's earnings. Looking ahead, corporate practitioners rank the highest risk factor impacting organization earnings in the next three years as tougher competition (cited by 40 percent of survey respondents), followed by customer satisfaction/retention (33 percent) and U.S. political and regulatory uncertainty (32 percent).

Tougher competition and customer satisfaction/retention are considered greater risk factors by smaller organizations and privately held ones than by other companies. Corporate practitioners from organizations with annual revenue of less than $1 billion (44 percent) and those privately held (44 percent) are more likely to suggest that tougher competition will affect their companies' earnings than are their counterparts from larger companies (38 percent) and publicly owned ones (37 percent). Respondents from larger organizations (annual revenue at least $1 billion) and those that are publicly owned believe U.S. political and regulatory uncertainty to be more of a risk factor than those from other organizations.

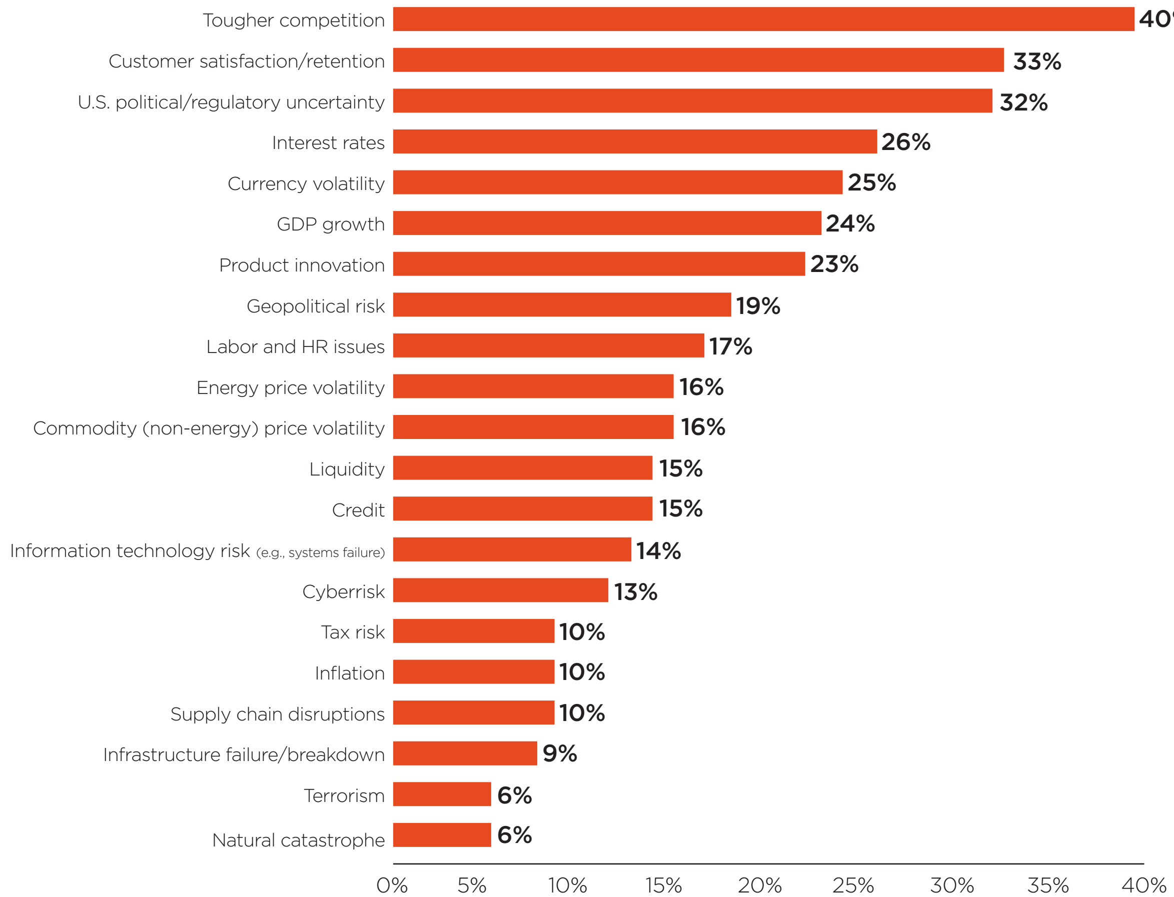
It makes sense that competition ranks at the top of the risk factors given globalization and the rapid pace of new technologies being developed. Commerce is conducted increasingly on a global basis; that opens doors for various companies to enter previously untapped markets. This, combined with the ability of new entrants to participate in these markets by deploying new technologies, puts even the best and most mature companies at risk of being displaced.

Take the fintech industry, for instance. It is rapidly changing the payments and banking landscape with potential widespread impacts on all aspects of supply chains and payment processes across all economic sectors. The biggest and most discussed fintech innovation is Blockchain. This technology is no longer something in the distant future. Indeed, many entities have tested a distributed ledger for settling trades and letters of credit.

Rounding out the top five future risk factors are currency and interest rate risk. Foreign exchange markets have been increasingly volatile for a number of years, even more so after the Brexit vote and Donald Trump's election (although this survey was conducted before the U.S. presidential election). In fact, on a basket of currency trade-weighted basis the U.S. dollar (USD) hit a 14-year high in mid-December 2016 (after this survey was conducted). Similar developments surround interest rate risk. After the election, the U.S. bond market experienced a rout, with longer term interest rates (10-30 years) increasing by 50 basis points in just a week.

Tougher competition, customer satisfaction/retention, and political and regulatory uncertainty are the top three risk factors expected to have an impact on organizations' earnings in the next three years

Key Risk Factors which Will Have the Greatest Impact on Organization's Earnings in the Next Three Years
(Percent of Respondents)



While the three top-ranked factors are similar to those in the *2016 AFP Risk Survey*, the order differs. In that survey, political and regulatory uncertainty ranked first (cited by 43 percent of respondents), with tougher competition ranking second (42 percent) and customer satisfaction/retention third (40 percent). It is interesting that in an election year (during which this survey was conducted), finance professionals believed competition would have a greater impact on their organizations' earnings than would any uncertainty surrounding the U.S. political and regulatory environment.

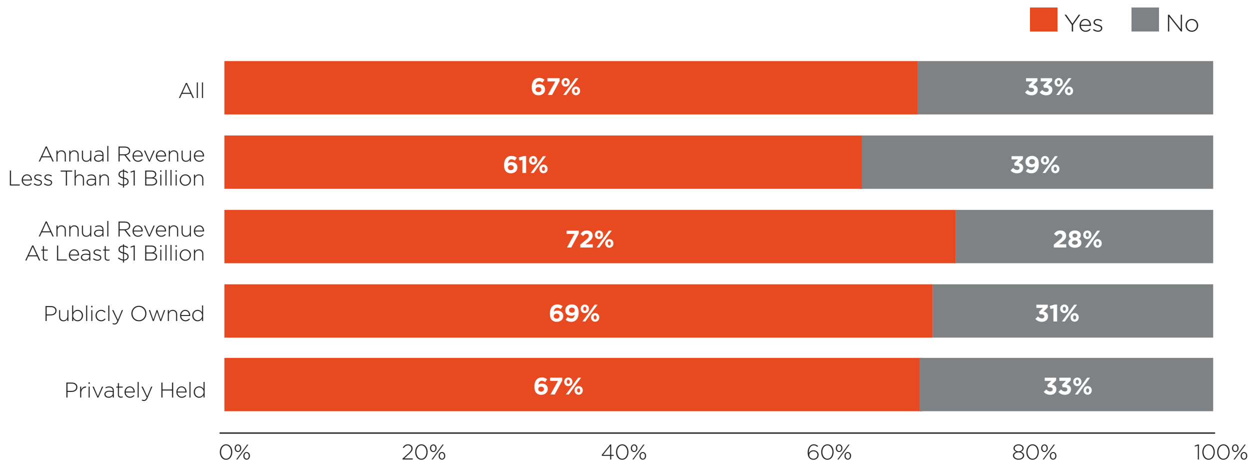
Changes in Risk Factors Expected to Have Greatest Impact on Organization's Earnings over Next Three Years

Risk Ranking	2015	2016	2017
1	Political and Regulatory Uncertainty	Political and Regulatory Uncertainty	Tougher Competition
2	Tougher Competition	Tougher Competition	Customer Satisfaction/ Retention
3	Customer Satisfaction/ Retention	Customer Satisfaction/ Retention	U.S. Political and Regulatory Uncertainty
4	Product Innovation	Currency Volatility	Interest Rates
5	Interest Rates	Product Innovation	Currency Volatility

Organizations Continue to Actively Mitigate Risk Exposure

Two-thirds of organizations are actively mitigating risk exposure in direct response to current and emerging threats. A greater share of finance professionals from larger organizations (annual revenue of at least $1 billion) than from smaller ones reports that their companies are actively mitigating risk exposure (72 percent versus 61 percent).

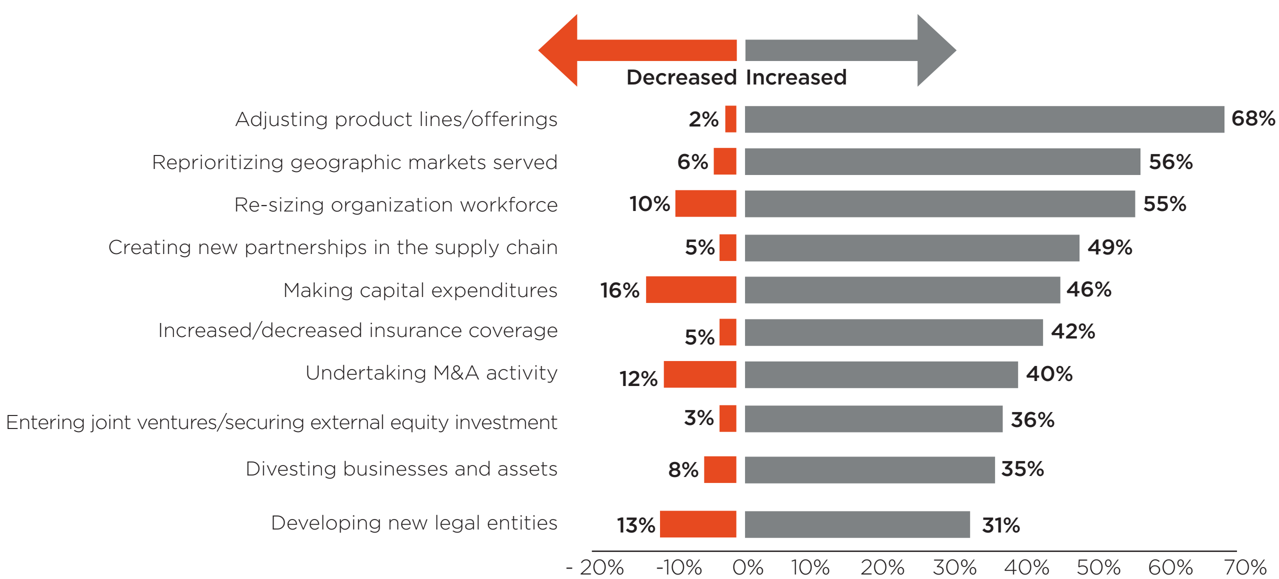
Mitigation of Risk Exposure in Direct Response to Current and Emerging Threats
(Percentage Distribution of Organizations)



Business leaders are taking various actions to minimize risk and most of those actions align with protecting organization's earnings. A large majority of companies—68 percent—is minimizing the impact of exposure to risk by adjusting product lines and offerings. More than half are minimizing risk exposure by reprioritizing geographic markets served (56 percent) and resizing their organization workforce (55 percent).

Other approaches being adopted by organizations to counter risk exposure include creating new partnerships in the supply chain (cited by nearly half of survey respondents), making capital expenditures (46 percent) and increasing insurance coverage (42 percent).

Actions Taken in Response to Current and Emerging Business Risks
(Percent of Organizations)



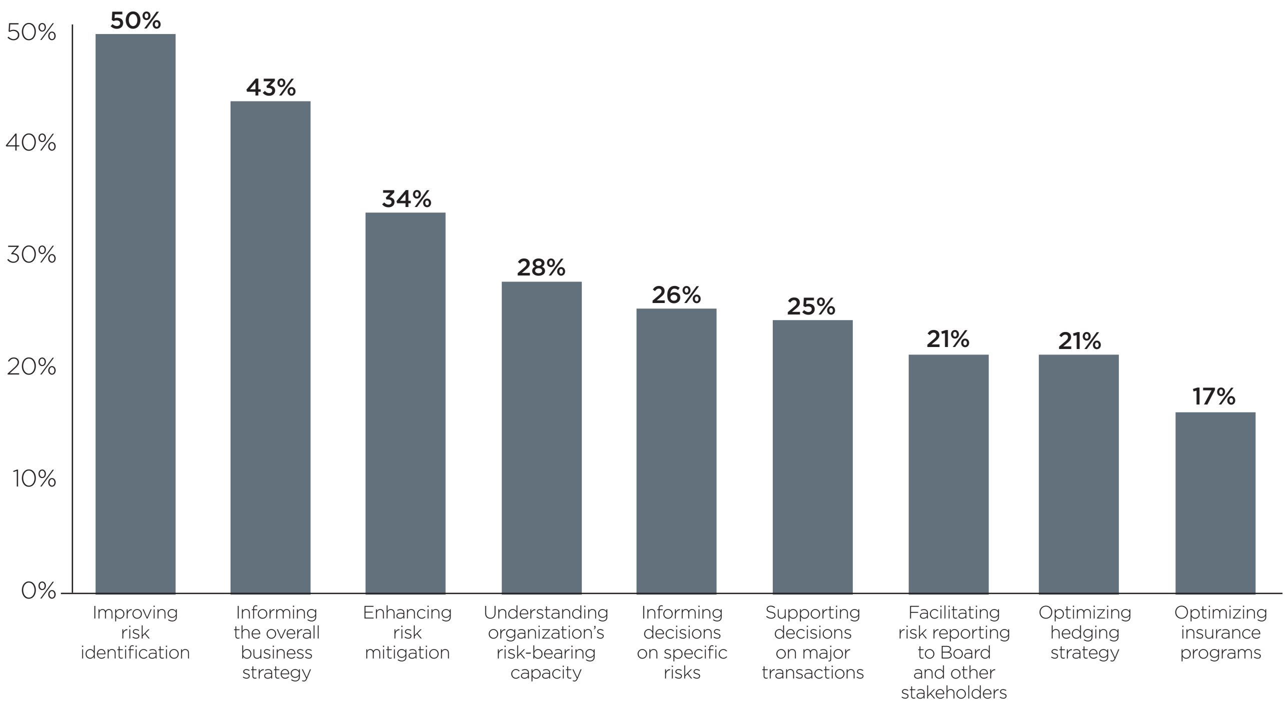
Risk Data and Analytics Used to Support Business Strategy

Survey results suggest that companies are continuing to actively integrate risk data and analytics into their decision making. Finance professionals are looking to reduce the impact of risks by focusing on improving risk identification, informing the overall business strategy and enhancing risk mitigation. These priorities mark a shift from the previous survey, and perhaps indicate that risk leaders in organizations are putting a greater focus on identifying emerging and evolving risks, and highlight a growing awareness to not simply manage risks but to leverage risk insights to improve the business strategy.

Finance professionals from smaller organizations that are privately held are more likely than those from other companies to believe that more effective use of risk data and analytics will improve both risk identification and inform overall business strategy. Their peers from larger organizations and publicly owned ones are more likely to suggest that risk data and analytics will enhance risk mitigation.

Finance professionals are seeking to reduce the impact of risks by focusing on improving risk identification, informing the overall business strategy and enhancing risk mitigation

Effective Integration of Risk Data and Analytics in the Organization
(Percent of Organizations)



Geopolitical Risks

Political risk—also known as" geopolitical risk"—is the risk to an investment's returns resulting from political changes or instability in a country. Instability affecting investment returns could stem from a change in government, legislative bodies, other foreign policy makers or military control. (*Source: Investopedia)*. 2016 was a year marked by extreme volatility and uncertainty. Among recent examples are the attempted coup in Turkey, terrorist attacks in Europe, Asia, the U.S. and Africa, a continuing migrant crisis, ongoing conflicts in Syria, Iraq and Afghanistan, the Brexit referendum and its aftermath, and the U.S. presidential race. (See exhibit on page 10.)[2]

A number of geopolitical events including the unexpected outcome of the Brexit referendum, terrorist attacks, and political uncertainty in the U.S. and elsewhere impacted the global economy. It is likely we will see more such events as a number of European countries—including Germany and France—will be holding elections in 2017; some parties and their candidates could be described as controversial. In Italy, a vote on constitutional reform was held on December 4, 2016, the impacts of which have already led to a change in that country's government. Additionally, some unprecedented events in Asia—e.g., the rise of a non-establishment leader in the Philippines, continued nuclear threats from North Korea (having conducted its fifth and largest nuclear test) and the conflict surrounding the South China Sea—are other events which have heightened global risk, thus adding to already existing uncertainty.

The driving forces behind rising geopolitical risks are varied across countries but include common themes of economic stagnation in advanced economies, and economic slow-down in emerging economies increasing economic inequalities and the vulnerabilities of lower income groups. Along with this, there are rising social tensions in the face of long-term trends such as demographic shifts and migration. Perilous economic circumstances have intensified the spotlight on the shortcomings of the political establishment in many countries leading to populist politics, the rise of anti-establishment parties and rising nationalism.
The knock-on impacts on business activities are varied and range from civil disturbance and terrorist attacks to policy reversals and regime changes.

Geopolitical risks have entered mainstream conversations and are now part of discussions among finance professionals in organizations' treasury, finance and operations functions. As featured in an article in the September 2016 issue of *AFP Exchange Magazine* entitled "Cracking the Code," geopolitical risk is mentioned as one of the newer risks on the horizon and should be taken into consideration when weighing the deployment of capital.

[2] Resilience amid Disorder: Steering a Path through Social and Political Unrest," Marsh & McLennan Companies' Global Risk Center, 2016

Political and Social Instability in 2016 to Date

Region | **Incidents (Selected)**

- **US:** Heightened racial and police tensions, lone-wolf terror attacks, incendiary campaigns for presidential primaries and run-off
- **Venezuela:** Chronic food and energy shortages, soaring inflation, widespread unrest, institution of emergency powers
- **Brazil:** Senior politicians engulfed by Petrobras scandal, mass anti-regime and anti-corruption protests, President Rouseff impeached
- **Chile:** Violent student demonstrations, mass protests against ailing state pension system
- **Argentina:** Former President implicated in corruption scandals, prolonged anti-austerity protests

- **UK:** Historic referendum vote to exit EU, resignation of Prime Minister, spike in hate crime and abuse, resurgence of Scottish nationalism hopes
- **Germany:** Turkish-refugee tension, lone-wolf terror attacks, regional election gains by anti-refugee party
- **Belgium:** Brussels bombings, high ethnic tensions, violent anti-austerity protests, mass strikes
- **France:** Multiple demonstrations and worker strikes, lone-wolf terror attacks, high religious and ethnic tension (burkini ban)
- **Spain:** Prolonged political gridlock, separatist determination with significant public support (Catalunya)

- **China:** Ongoing protests and Uighur terrorists attacks, Hong Kong seats won by anti-Beijing activists
- **India:** Rise in Kashmir violence after the killing of a separatist icon, strike by ~ 150 million against Prime Minister Modi's 'anti-labor' policies
- **Thailand:** Army-endorsed constitution following tightly controlled referendum, coordinated bomb attacks on tourist resorts
- **Phillipines:** Violent anti-drugs campaign of new populist President, 'state of lawlessness' declared following Davao bomb attack
- **The '-stans':** Land protests and suppression in Kazakhstan, bombing of Chinese Embassy in Bishkek, uncertainty following the death of Uzbek President after 27-year rule

- **Turkey:** Multiple terrorists attacks, attempted military coup, institution of emergency powers, crackdown against the Kurds, incursion into Syria
- **Tunisia:** Repeated extensions of nationwide state of emergency, violent unemployment protests, multiple terrorists attacks
- **Saudi Arabia:** Protests and strikes over layoffs and the non-payment of wages, suicide bombings at holy sites and US consulate
- **Syria:** Prolonged conflict and refugee crisis due to the competing interests of regional and global powers
- **Libya:** Ongoing civil war, ailing internationally-backed government, oil terminals captured by opposition forces, coup attempt

- **Nigeria:** Renewed Niger Delta Avenger militancy in the oil-rich South, Boko Haram insurgency in North East, famine concerns
- **Gabon:** Disputed re-election of President Bongo, violent demonstrations (1000+ arrests), parliament building set on fire
- **Burundi:** Prolonged political violence and civil unrest arising from debate around constitutionality of President's third term
- **Ethiopia:** Protests and anti-government violence, destruction of foreign company property
- **South Africa:** President Zuma corruption charges reinstated, violent protests and nationwide strikes, African National Congress election losses

Source: Press, analyst reports, MMC analysts

Assessing the Impacts of Geopolitical Risks

Whether it is Brexit, a terrorist attack or devaluation of a major currency, the consequences of geopolitical events can be extensive, especially considering the high levels of global interconnectivity. Some of the effects are immediate and obvious—stock market volatility, currency fluctuations, etc. (see exhibit below).

But an individual organization's growth and expectations of risks to growth can be impacted too. The question is whether senior leaders are closely anticipating and planning for the risks and impact on the bottom-line of their organizations as these geopolitical events arise.

Corporate Threats from Political and Social Instability

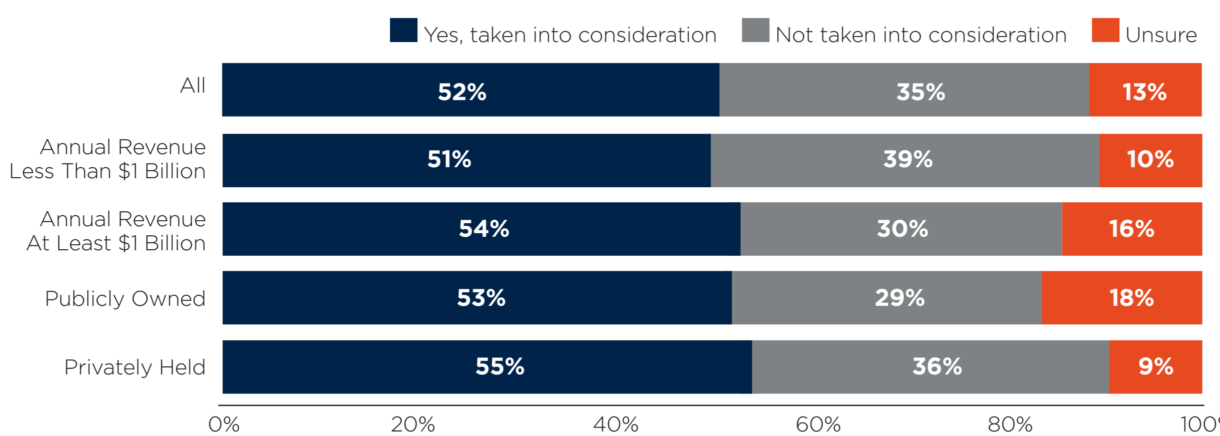
	Business degradation	Transactional discrimination	Strategic challenges
Challenge	• Asset damage • Business operations interruption • Supply chain and logistics interruption • Product/services boycott • Market decline (e.g. tourism) • Personnel safety threats	• Tariff hikes • Taxation increases • Contract repudiation • Construction permit denial • Operating license denial or revocation • Import/export license denial or revocation	• Delays in enabling legislation or regulations • Indigenization measures (local ownership/content) • Asset requisiition, confiscation, or nationalization • Currency inconvertibility • Forced abandonment • Economic sanctions (especially trade embargos)
Likely primary cause	• Terrorism and insurgency • Civil disturbance	• Protectionism (national/local) • Corruption and other government failures	• National-level protectionism • War or coup d´état

Source: Marsh & McLennan Companies

A majority of treasury and finance functions—52 percent—has considered the impact on their organization's growth and the risks involved from a geopolitical change or event. However, 13 percent of finance professionals are unsure whether or not the treasury and finance functions at their companies are doing the same. Over a third of survey respondents (35 percent) indicate that their senior treasury and finance leaders are not planning for any changes to their company's growth expectations as a result of geopolitical events. A greater share of finance professionals from larger organizations (those with annual revenue of at least $1 billion) and those that are publicly owned is unsure about whether any concerns would be raised regarding the expectations of growth at their companies after a geopolitical event.

A majority of treasury and finance functions would consider the impact on their organization's growth and the risks involved due to a geopolitical change or event

Consideration by Treasury and Finance Function of Impact on Organization's Change in Expectations of Risk to Growth due to Geopolitical Event
(Percentage Distribution of Organizations)



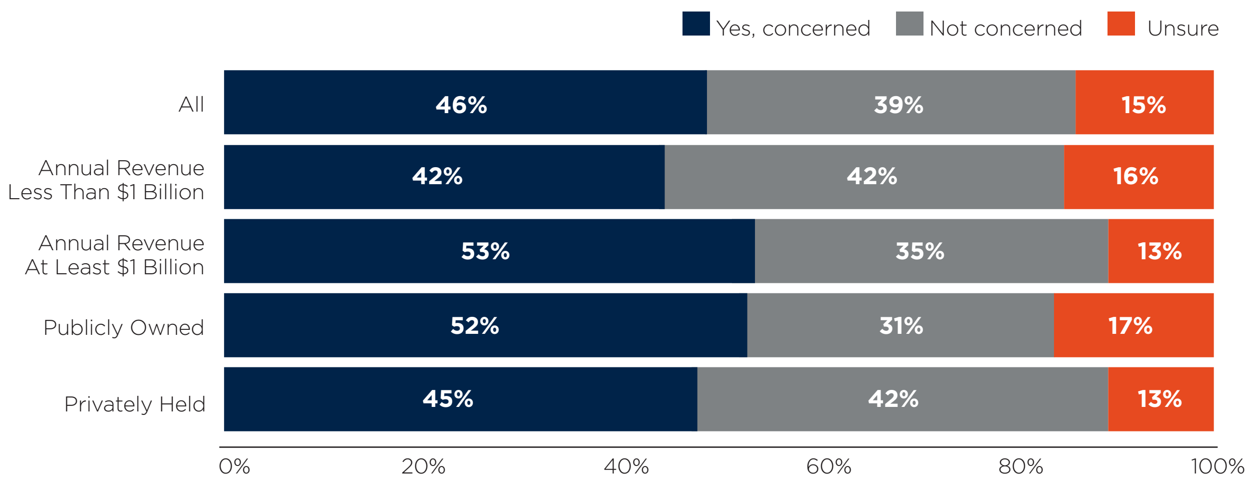
C-Suite and Board's Concern Regarding Geopolitical Risk

There are some obvious reasons why an organization's C-suite and Board should be aware of and concerned about certain geopolitical risks. The most direct risk is operating in countries with a history of "bad behavior," such as Venezuela and Argentina where corporate assets have simply been frozen. But there are other geographies around the world where there is plenty of risk to operations and thus to revenue and profits. These countries include Egypt (which is struggling to maintain a functioning government) and Nigeria, as well as foreign states with ongoing civil wars. Turkey is also a prime example, having experienced a failed military coup in the summer of 2016, as well as a number of terrorist attacks last year. One rather large quick-service restaurant chain operates about 1,000 stores in southwest Turkey, and the impact from such events can manifest itself in supply chain disruptions and loss of infrastructure/operations.

Forty-six percent of finance professionals report that their organizations' C-suite and Board had concerns about the geopolitical risks in 2016. Surprisingly, 39 percent indicate that their senior leaders showed no signs of unease regarding such risks; the remaining share is unsure whether their C-Suite and Board felt any apprehension regarding geopolitical risks in 2016. Not unexpectedly, a slight majority of business leaders from larger organizations with annual revenue of at least $1 billion and those that are publicly owned is concerned about the impact of geopolitical risks on their organizations—most likely because these larger organizations are more active in more markets. Finance and risk leaders who can provide insights to the C-suite and Board regarding these risks can take a leading role in raising the effectiveness of these critical discussions.

46% of finance professionals report that their organizations' C-suite and Board had concerns about geopolitical risks in 2016

C-suite and Board Concern Regarding Geopolitical Risk
(Percentage Distribution of Organizations)



Key Areas or Concerns with Regard to Geopolitical Risk

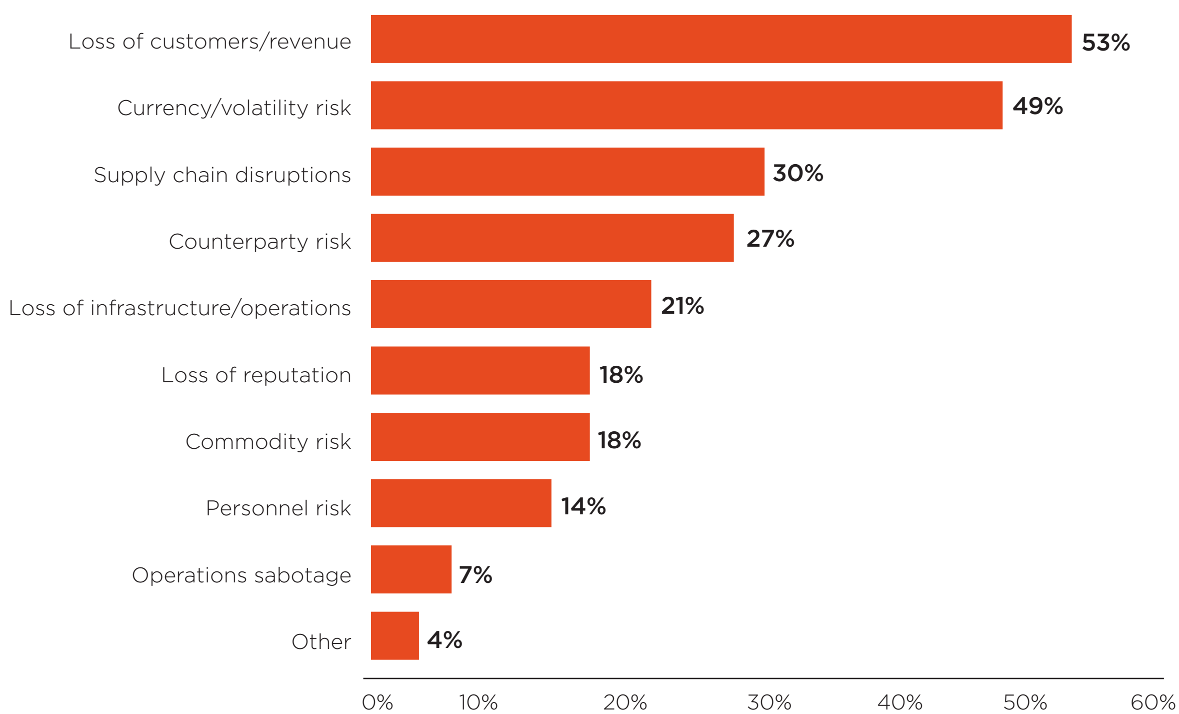
A majority of finance professionals—53 percent—cites loss of customer/revenue as a key concern with regard to geopolitical risks. Other concerns/opportunities cited by respondents include:

- **Currency volatility risk** (cited by 49 percent of respondents)
- **Supply chain disruptions** (30 percent)
- **Counterparty risk** (27 percent)
- **Loss of infrastructure/operations** (21 percent)

Finance professionals from smaller organizations (with annual revenue less than $1 billion) and privately held ones are more concerned about the loss of customers/revenue due to geopolitical risks than are respondents from larger organizations. The impact of a geopolitical event on currency/volatility risks is a bigger concern for larger organizations with annual revenue of at least $1 billion and those that are publicly owned than for other companies.

The majority of finance professionals cite loss of customers/revenue as a key concern with regard to geopolitical risk

Organization's Key Areas of Concern or Opportunity with Regard to Geopolitical Risk
(Percent of Organizations)



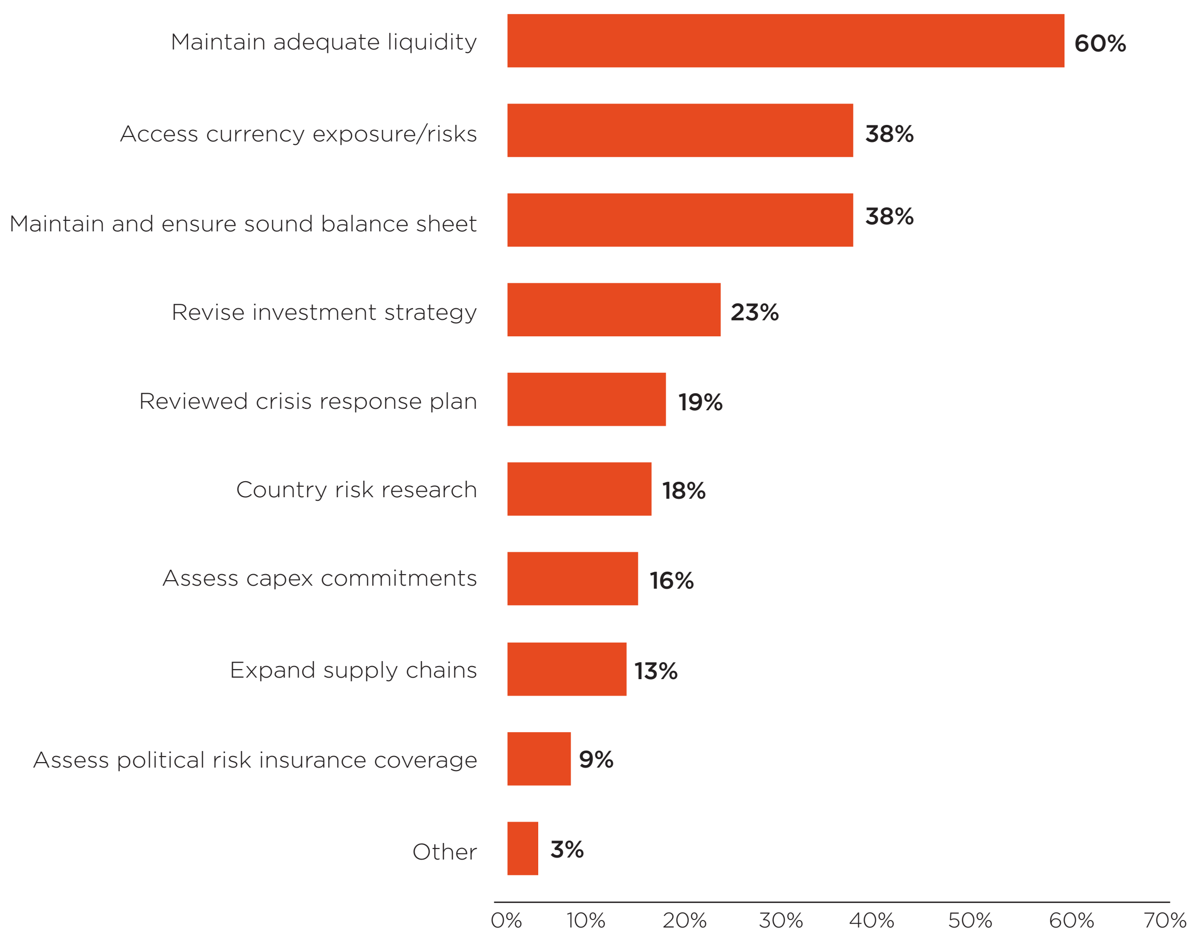
Actions Taken to Respond to and Mitigate Potential Impacts of Geopolitical Risks

There are various responses organizations can take to help manage these potential impacts. For example, some organizations consider the use of trade credit insurance which enables companies to extend more generous payment terms (e.g., 90 days instead of 60 days) to their customers. This can provide a competitive edge in tough markets and help retain clients. Organizations can also take a closer analysis of their suppliers' financial strengths to look to minimize potential supply chain disruptions.[3]

Survey results indicate that in order to help respond to and reduce any potential impacts of geopolitical risk, organizations are most focused on maintaining adequate liquidity (cited by 60 percent of respondents). Additionally, business leaders are actively maintaining and ensuring a sound balance sheet and assessing currency exposure risks (each cited by 38 percent of respondents) to reduce the effects of geopolitical risks on their organization's bottom line. A greater share of larger companies than smaller ones is paying attention to maintaining liquidity (65 percent versus 57 percent).

60% of organizations are focused on maintaining liquidity to help respond to and reduce any potential impacts of geopolitical risks

Actions Taken by Treasury and Finance Function to Respond to and Reduce Potential Impacts of Geopolitical Risks
(Percent of Organizations)



[3] See, "The New Weakest Link in Your Supply Chain: Supplier Credit" and "Managing Counterpart Risk in the Supply Chain," Oliver Wyman and AFP, 2012.

Actions for Treasury and Finance Functions to Help Organizations Mitigate and Respond to Geopolitical Risk

- **Manage credit risk.**
  When a government collapses or descends into crisis, it often loses its ability to honor financial obligations. This can create a chain reaction of default that spreads into the private sector. Businesses should review their credit risks and credit-control policies and procedures, and evaluate the potential impact of political risk on the countries in which they, their customers, and suppliers operate.
- **Build resilient supply chains.**
  Before a crisis develops, an organization should understand how a crisis in one country can disrupt its global supply chain. Businesses should also have response plans in place to allow for the use of alternative suppliers and/or ports, and to communicate with customers and suppliers as needed.
- **Protect people.**
  Developing and testing crisis plans in advance can help ensure effective communication during and immediately following a crisis.

Conclusion

Results of the *2017 AFP Risk Survey* suggest nearly half of all companies are exposed to greater earnings uncertainty than they were three years ago, with financial factors and business/operations the top two factors driving that uncertainty. But two-thirds of companies are actively mitigating risk exposure. The job of managing and forecasting risk continues to be either as challenging as or more challenging than it was three years ago, and a large majority of finance professionals anticipates that forecasting risk won't get any easier three years from now.

There is a wave of populism sweeping the globe. Voters are being polarized and unexpected outcomes from referendums and elections have shaken up the status quo in a number of countries. The U.K. electorate's vote to leave the European Union (Brexit) was a surprise, as was the election of non-establishment candidate Donald Trump to the U.S. presidency. In 2017, there will be elections to monitor in France and Germany, which may bring about unexpected outcomes. We witnessed wildly fluctuating currency and stock markets during 2016. In the wake of new political realities and extreme uncertainty and volatility in economic and financial markets, we may need to come to terms with what might be the "new normal."

Highlights from the 2016 AFP Risk Survey

Uncertainty in Earnings Continues to Dominate

Forty-nine percent of finance professionals believe their organizations are exposed to greater earnings uncertainty today than three years ago.

Financial Factors and Business/Operations are Top Reasons for Earnings Uncertainty

The top two drivers of earnings uncertainty are financial factors (e.g., credit, liquidity, interest rate, currency/FX) and business/operations (each cited by 24 percent of survey respondents).

Anticipated Difficulty in Forecasting Risk

Forecasting risk continues to be a challenge for a majority of finance professionals. A large majority of survey respondents (84 percent) reports that forecasting risk is either as difficult as or more difficult than it was it was three years ago. There is also a consensus among finance professionals that forecasting will only become more difficult in the future.

Risk Factor Having the Greatest Impact on Earnings in the Next Three Years

Corporate practitioners rank tougher competition as the greatest risk factor impacting organization earnings in the next three years (cited by 40 percent of respondents).

Organizations Continue to Actively Mitigate Risk Exposure

Two-thirds of organizations are actively mitigating risk exposure in direct response to current and emerging threats.

Consideration by Treasury and Finance Function of Impact on Organizations' Change in Expectations of Risk to Growth due to Geopolitical Event

A majority of treasury and finance functions (52 percent) are considering the impact on their organizations' expectations of risk to growth from a geopolitical change or event.

C-Suite and Board Concern Regarding Geopolitical Risk

Forty-six percent of finance professionals report that their C-suite and Board exhibited signs of concern regarding the geopolitical risks during 2016. However, 39 percent indicate that their senior leaders showed no signs of unease regarding geopolitical risks last year.

Key Areas or Concerns with Regard to Geopolitical Risk

A majority of finance professionals (53 percent) cites loss of customers/revenue as a key concern with regard to geopolitical risks.

Actions Taken to Respond to and Mitigate Potential Impacts of Geopolitical Risks

Survey results indicate that in order to help respond to and reduce any potential impacts of geopolitical risk, organizations are most focused on maintaining adequate liquidity (cited by 60 percent of respondents).

About the Survey

In September 2016, the Research Department of the Association of Financial Professionals® (AFP) surveyed its senior level corporate practitioner membership about earnings uncertainty and how their organizations manage risk. The survey was sent to AFP members and prospects who held job titles of CFO, Treasurer, Controller, Vice President of Finance and Assistant Treasurer. Responses from 480 professionals form the basis of this report. The respondent profile closely resembles that of AFP's membership and is presented below.

AFP thanks Marsh & McLennan Companies' Global Risk Center for being a valued partner and for its continued support of the AFP Risk Survey series, including sharing subject matter expertise for the design of the questionnaire and for the final report. The Research Department of the Association for Financial Professionals® is solely responsible for the content of this report.

Annual Revenues (USD)
(Percentage Distribution of Organizations)

Under $50 million	20%
$50-99.9 million	10
$100-249.9 million	11
$250-499.9 million	8
$500-999.9 million	8
$1-4.9 billion	26
$5-9.9 billion	7
$10-20 billion	3
Over $20 billion	6

Ownership Type
(Percentage Distribution of Organizations)

Privately Held	33%
Publicly Owned	52
Non-profit (not-for-profit)	9
Government (or government-owned entity)	6

Industry Classification
(Percentage Distribution of Organizations)

Agriculture	3%
Automotive	4
Chemicals	2
Communications	2
Consumer Products (Manufacturing, Sales, Distribution, etc.)	10
Energy (Utilities, Oil, etc.)	7
Financial Services (Banking, Investment, Brokerage, Insurance, etc.)	17
Government/Not-for-Profit	8
Healthcare Provider	3
Media/Professional Services	4
Mining and Metals	3
Pharmaceuticals/Biotechnology (Development, Manufacturing, Sales, Distribution, etc.)	2
Retail	5
Surface Transport (Maritime, Motor Transport, Rail)	3
Technology (Development, Manufacturing, Sales, Distribution, etc.)	8
All Other Manufacturing (excluding Consumer Products, Pharmaceuticals, Technology)	17

Appendix

Change in Exposure to Earnings Uncertainty Relative to Three Years Ago
(Percentage Distribution of Organizations)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Exposed to more	49%	45%	54%	56%	50%
Exposed to the same level	40	42	36	36	38
Exposed to less	11	12	9	9	13

Primary Drivers of Increase in Exposure to Earnings Uncertainty
(Percentage Distribution of Organizations That Have Experienced Greater Earnings Uncertainty)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Financial (e.g., credit, liquidity, interest rate, currency/FX)	24%	25%	23%	22%	28%
Business/Operations (e.g., supply chain disruptions, production interruptions, litigation, labor, outsourcing, IT, cyber)	24	27	17	22	24
External (e.g., country risk, regulatory, natural disaster)	22	19	20	19	18
Macroeconomic (e.g., GDP growth, inflation, consumer price index)	19	19	23	22	21
Commodities (e.g., energy, agricultural, basic resources)	11	9	16	16	8

Key Risk Factors which Will Have the Greatest Impact on Organization's Earnings in the Next Three Years
(Percent of Respondents)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Tougher competition	40%	44%	38%	37%	46%
Customer satisfaction/retention	33	39	24	26	36
U.S. political and regulatory uncertainty	32	29	34	30	27
Interest rates	26	23	27	25	24
Currency volatility	25	22	32	37	24
GDP growth	24	22	28	30	25
Product innovation	23	24	24	25	25
Geopolitical risk	19	16	23	28	16
Labor and HR issues	17	19	13	10	19
Commodity (non-energy) price volatility	16	15	19	22	16
Energy price volatility	16	18	16	17	19
Credit	15	16	12	14	15
Liquidity	15	14	15	13	15
Information technology risk (e.g., systems failure)	14	14	13	6	16
Cyberrisk	13	11	14	9	13
Supply chain disruptions	10	10	11	10	10
Inflation	10	13	7	5	11
Tax risk	10	11	8	13	10
Infrastructure failure/breakdown	9	11	4	3	10
Natural catastrophe	6	8	4	4	8
Terrorism	6	7	4	5	8

Actions Taken in Response to Current and Emerging Business Risks
(Percent of Organizations)

	Increased	Same	Decreased
Adjusting product lines/offerings	68%	21%	2%
Re-prioritizing geographic markets served	56	27	6
Re-sizing organization workforce	55	27	10
Creating new partnerships in the supply chain	49	34	5
Increased/decreased insurance coverage	42	47	5
Undertaking M&A activity	40	26	12
Entering joint ventures/securing external equity investment	36	34	3
Divesting businesses and assets	35	33	8
Developing new legal entities	31	39	13
Making capital expenditures	46	33	16

Benefits of Effective Integration of Risk Data and Analytics in the Organization
(Percent of Organizations)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Improving risk identification	50%	53%	46%	48%	52%
Informing the overall business strategy	43	48	36	35	48
Enhancing risk mitigation	34	30	41	45	28
Understanding organization's risk-bearing capacity	28	26	32	32	26
Informing decisions on specific risks	26	25	25	24	25
Supporting decisions on major transactions	25	25	26	24	24
Facilitating risk reporting to Board and other stakeholders	21	22	19	21	17
Optimizing hedging strategy	21	16	27	23	21
Optimizing insurance programs	17	18	15	14	19

Organization's Three Key Areas of Concern or Opportunity with Regard to Geopolitical Risk
(Percent of Organizations)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Loss of customers/revenue	53%	58%	46%	44%	60%
Currency/volatility risk	49	46	53	65	45
Supply chain disruptions	30	28	32	37	30
Counterparty risk	27	20	36	38	21
Loss of infrastructure/operations	21	22	20	17	21
Commodity risk	18	18	18	21	18
Loss of reputation	18	17	20	14	17
Personnel risk	14	15	13	9	14
Operations sabotage	7	9	6	4	8
Other	4	5	2	2	4

Actions Taken by Organizations to Help Respond to and Reduce Potential Impacts of Geopolitical Risks
(Percent of Organizations)

	All	Annual Revenue Less Than $1 Billion	Annual Revenue At Least $1 Billion	Publicly Owned	Privately Held
Maintain adequate liquidity	60%	57%	65%	57%	61%
Maintain and insure sound balance sheet	38	41	35	40	39
Assess currency exposure/risks	38	33	46	53	34
Revise investment strategy	23	21	25	24	20
Reviewed crisis response plan	19	19	19	14	20
Country risk research	18	19	18	22	17
Assess capex commitments	16	15	17	16	18
Expand supply chains	13	11	15	11	17
Assess political risk insurance coverage	9	10	9	10	10
Other	3	4	1	2	4

AFP Research

AFP Research provides financial professionals with proprietary and timely research that drives business performance. AFP Research draws on the knowledge of the Association's members and its subject matter experts in areas that include bank relationship management, risk management, payments, and financial accounting and reporting. Studies report on a variety of topics, including AFP's annual compensation survey, are available online at www.AFPonline.org/research.

AFP® ASSOCIATION FOR FINANCIAL PROFESSIONALS

About the Association for Financial Professionals

Headquartered outside Washington, D.C., the Association for Financial Professionals (AFP) is the professional society that represents finance executives globally. AFP established and administers the Certified Treasury Professional™ and Certified Corporate FP&A Professional™ credentials, which set standards of excellence in finance. The quarterly AFP Corporate Cash Indicators™ serve as a bellwether of economic growth. The AFP Annual Conference is the largest networking event for corporate finance professionals in the world.

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