

Marsh News Philippines

News for Marsh clients in the Philippines



Risk Denial or Risk Management?

Companies around the world are coming to the view that a piecemeal approach to risk is not good enough anymore. But many have been slow to adopt an enterprise risk management (ERM) approach to their business.

A recent survey result reported by *Insurance & Risk Professional* magazine in December last year found that only 10% of the world's leading 1500 corporations say their ERM program is fully embedded and integrated into their business processes.

In the Philippines, companies' adoption of ERM is still in its early stages. Reynaldo de Dios, a pioneer advocate of risk management in the Philippines, found in a recent survey of top Philippine accounting and management services firms that only eight of their clients had engaged them to introduce an ERM culture into their organizations, according to a report in *Asia Insurance Review* last year.

ERM represents a way that companies can coordinate how they deal with risks, which involves an overall evaluation of a company's risk framework. The Risk and Insurance Management Society (a United States non-profit organization) defines it as the culture, processes and tools used to identify opportunities and reduce uncertainty from both strategic and operational perspectives.

In recent years, many companies have been put on notice by ratings agencies such as Standard & Poor's (S&P) that they will soon be marked according to in-depth ERM criteria.

(continued on page 2)

This issue

■ **Philippines' Poor Infrastructure Result**
page 3

■ **Newsbites**
page 4

(from page 1)

Since 2004, S&P has used ERM analysis on financial institutions and by 2006 it had begun to have an effect on ratings, according to S&P's report *Enterprise Risk Management for Financial Institutions* in November 2005. The rating agency has flagged extending the use of this approach on other industries, such as energy and utilities, so that their risk management will be factored into the overall rating of the company's business risk.

The reason behind the slow shuffle towards ERM is that companies are generally reluctant to overhaul their existing systems and procedures no matter what benefits the effort promises, says German Plan Jr., Senior Vice President and Head of Broking for Marsh Philippines.

"Many organizations have also got legacy systems and procedures, and what they have done is tried to tailor them into what they are calling an enterprise risk management framework," Plan says. "But they soon learn that you cannot tweak old systems to get the full benefit of ERM."

Plan says the key to successfully adopting an ERM program is

that it begins with an organization's top management asking itself questions, such as: "What is our strategy? What is our risk culture? What are our incentives and disincentives for our leaders to deal with risk? Is our structure and governance right for the current environment? What is our risk appetite?"

Typically, banks are among the first adopters of ERM around the world. A big driver for the banks in taking this approach has been the introduction of the global Basel II banking regulations. These are due to come into effect in the Philippines by 2010. By proving they have superior levels of risk management processes, the banks can apply for advanced accreditation under this new regime. One of the benefits

of this is they can operate with substantially less capital held in reserve.

However, banks have derived other benefits from adopting ERM. For example, in Australia, where Basel II went into operation at the beginning of this year, the banking industry has been quick to adopt ERM. The Chief Risk Officer of one of Australia's largest banks says it has avoided substantial losses during the past two years because of its risk management framework. The officer credits ERM not only with cutting down operational errors for the bank, where wrong keystrokes can instantly cause huge losses, but helping to escape the US sub-prime mortgage meltdown relatively unscathed.

Key Points

- Only 10% of companies worldwide have embedded an enterprise risk management approach into their organizations.
- The international Basel II banking regulations is driving many banks to adopt ERM. The Philippines is expected to implement these regulations by 2010.
- Standard & Poor's is rolling out an ERM analysis in its credit rating for all industries.

Philippines' Poor Infrastructure Result

The state of the Philippines' infrastructure is a mixture of achievements and persistent weaknesses, according to the World Bank. In most categories of basic infrastructure in the 2007 World Competitiveness Survey Report, the Philippines remained near the bottom, ranking 51st out of 55 countries and territories in terms of development as measured by per capita income.

The biggest stumbling block in the development of the country's infrastructure is the persistent constraints on public sector funding. In order to address this concern, investments from the private sector needs to be stimulated by developing coherent sector plans supported by capable public sector agencies that include independent regulators, unbundled competitive operations, and clear rules on procurement using Public-Private Partnerships (PPP) instruments, tariffs and dispute resolutions.

Investments in infrastructure – transportation, ports and terminals, communications, and utilities – contribute greatly to a country's economic growth. High quality infrastructure has a significant impact on achieving sustainable development objectives by encouraging new investments across the economy, underpinning many aspects of economic and social activity and facilitating the flow of ideas, goods and services.

Private investments in infrastructure in the Philippines have been steadily flowing in.



In 2006, investments into this sector amounted to about 35.33% of the total investments or an equivalent of about Php96.72 billion. Total foreign direct investments (FDI) in the same year for all sectors amounted to about US\$2.35 billion (Php 96.1 trillion) or a 27% increase on the previous year. In the first quarter of 2007 alone, FDI already increased by 18.5% compared to the same period in 2006.

Foreign investors often encounter a difficult, and occasionally hostile, environment during project preparation and operation. Transparency and predictability are some of the keys to the development of an attractive framework. Investors have tended to stay away from countries where selection is perceived to be based more on the strength of political ties and other non-transparent criteria rather than on technical and financial strengths.

Foreign investors need assurance that they will be able to convert project revenues into foreign exchange that they can repatriate.

They face the danger of large exchange rate fluctuations, jeopardizing the adequacy of the project's cash flow in hard currency. Another concern is the extent to which the future business environment will be reasonably predictable. Investors want a well-developed and reliable framework of regulations.

Since most infrastructure projects are highly dependent on PPP and external lenders, their unique business propositions need to be understood and accommodated. One area where they often need assistance is having an insurance program designed for their specific requirements. They frequently need reference materials and benchmarking tools that can assist in such an exercise.

For more information on benchmarking tools for insurance programs supporting infrastructure projects, contact Jeremy Jacob Y. Abaño, AVP – Specialty Practice Leader for Infrastructure and Large Open Market of the Institutional Risk Management Group, telephone: (632) 7551001 or email: Jeremyjacob.Y.Abano@marsh.com.



Newsbites

Marsh #1 Broker In China

Marsh has been ranked the number one international insurance broker in China by the China Insurance Regulatory Commission (CIRC). The ranking of China's top 20 intermediaries was based on their annual invoiced revenue in the CIRC's 2007 Insurance Intermediary Market Report.

Marsh (Beijing) Insurance Brokers ranked top among all international brokers and fourth of all brokers in China. Marsh Greater China CEO, Paul Wilkins, says he is thrilled with the result for 2007 – just one year after the CIRC granted Marsh China with the first and only Wholly-Owned Foreign Enterprise insurance broking licence.

“Our ranking as China's number one international broker is a tremendous honour,” says Wilkins.

Marsh also serves Chinese clients offshore through its China Global Client Services network in key markets in the Asia Pacific, United States, United Kingdom, and Europe, Wilkins says. “Marsh's ranking clearly shows that in a market expanding as rapidly as China, organizations value the unmatched support, service, global footprint and technical expertise of Marsh.”

Of the 322 insurance broker companies operating in China, five are international brokers.

PAGASA Gets Funding from United States

The Philippines weather bureau received a grant of \$381,000 (Php15.5 million) from the United States government in February to help it modernize and improve its early-warning systems and natural disaster risk management resources, according to statement from the US embassy.

The Philippine Atmospheric, Geophysical and Astronomical Services Administration (PAGASA) will use the funding for a study to identify upgrades needed for its meteorological and hydrological telecommunications systems, according to the statement.

“The USTDA [United States Trade and Development Agency] grant agreement supports PAGASA's efforts to improve its capacity to monitor potential weather hazards, including typhoons, monsoons, and landslides, and inform the public about them,” the statement said.

Competitors for the study's contract will bid on the US Federal Business Opportunities website, and PAGASA will then select the US contractor for the study, the statement said.

Meanwhile, the World Bank approved a \$US12.9 million loan in February to rebuild electricity infrastructure in the southern Bicol region damaged by two super typhoons in 2006, according to Forbes magazine. The project also aims to strengthen the power system against future typhoon damage.

Mercer College's New Programs

Mercer College, the learning division of Mercer, is offering new public learning programs in Manila for 2008. Mercer, which specialises in advising on human resources, is a sister company to Marsh.

The new programs are:

- Compensation Planning and Budgeting (March 13)
- 3P Compensation Management (April 29-30)
- Becoming an Effective HR Business Partner (May 22)
- Maximizing the Value of Remuneration Surveys (August 11-12)

Mercer College is a virtual business school and has trained more than 12,000 human resources professionals and business leaders in Asia since 2004.

More information on Mercer College's programs can be found at www.mercer.com/referencecontent.jhtml/dynamic/idContent/1129440

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