Focus

RISK MANAGEMENT, THE NEW DISCIPLINE

The financial crisis has made MENA businesses aware of the need for serious governance and risk management strategies.

RISK MANAGEMENT IS DEVELOPING RAPIDLY

as a serious discipline and businesses in the MENA region are moving fast to embrace global standards.

Neal R Brendel, partner at law firm K&L Gates says: “Until recently, there was a sense that firms here were aware that it was important to pay lip service to the ideals of corporate governance but that there was very little actual infrastructure, such as codes of governance or even dedicated risk managers, to implement these aspirations.

“In the years since the financial crash, this area has been receiving much more serious attention. This was particularly obvious when the situation was difficult, and the big cash flows that had obscured some elements of bad practice were drying up.”

Speaking anonymously, one chief risk officer said: “Eight years ago, risk management was in its infancy. However, organisations have developed this a lot in the intervening period, even if problems still remain with board charters and board training and few organisations have proper business continuity. They may have a crisis management strategy, but in terms of how they recover afterwards they have little to go on.”

One of the main factors driving an increased awareness of risk management is that much of the region’s economic diversification has involved partnerships with US or European brands. When western companies come into the region, they require a certain level of risk management from the companies with which they deal.

“There is a building pressure on companies that want to partner with western brands that they will have to develop their approach to risk management,” says Paddy Lord, managing director at Control Risks.

As a result, regional businesses are becoming more and more sophisticated. However, this is a process that takes time, as well as serious investment in people and training. “Companies need to invest in more sophisticated staff and give them the mandate necessary to make their presence felt,” says Brendel.

“Businesses need to be talking to the kind of sophisticated brokers and risk advisers who can identify risks and suggest customised ways of addressing them.”

One of the biggest obstacles to change is the widespread lack of transparency. It can be hard for firms to determine who they are dealing with – and crucially whether they would be deemed a ‘government official’ according to the US’s Foreign Corrupt Practices Act (FCPA). “The US has expanded its jurisdiction in a lot of ways and this lack of transparency presents a real risk,” says Brendel.

Lord agrees. “Awareness is growing about the UK Bribery Act 2010 and FCPA, but there is still some way to go,” he says. “The level of litigation in the region is still low and companies usually prefer to reach a settlement before getting to court.”

Low insurance penetration

Another major barrier to modern risk management standards is the relatively low penetration of insurance. Although the insurance market grew overall from $20.4bn to $44.1bn (€19bn-€41.5bn) between 2006 and 2012, penetration has remained flat at 1.5%. Most of the growth took place within the United Arab Emirates (UAE), Saudi Arabia and Qatar as a result of major infrastructure projects such as the Qatar World Cup and new universities in Saudi Arabia.

“Although the Middle East does have a much lower insurance penetration compared to most western countries, this continues to increase year on year and provides the insurance fraternity with a continued focus on expansion,” says Paul Holmes, managing director, Middle East, for Al-Futtaim Willis.

“Low insurance penetration is partly explained owing to the measure against GDP, whereby a large proportion...
Economic growth is not materially affected by a low insurance penetration. "There is at least one significant barrier to insurance penetration that is specific to the region: sharia law frowns on many aspects of profit-making financial services. There are signs that products complying with sharia law – known as takaful – which are structured so that risks and rewards are shared in a similar way to a co-operative or mutual, could deliver a breakthrough. Growth has already been strong across life, non-life and medical cover. "In the UAE, Bahrain and Qatar, takaful companies that were start-ups a few years ago are becoming better established, and the challenge for them is to find ways of differentiating their products and finding new distribution channels," says Tony Saada, chief executive of UAE-based Lockton (MENA). Takaful is a powerful reminder that risk management is not a one-way street and newcomers and investors could learn some lessons from regional firms. "One of the ways that local family groups manage their exposure is by placing family members in different divisions of the company or even different territories to make sure that they retain an appropriate level of influence," says Lord. "In this region, much comes down to relationships and businesses have to work hard to maintain those relationships."

Some remarkable changes have taken place in the past few years and the direction of travel seems clear. The economic crisis has exposed shortcomings in risk management and provided a powerful incentive to handle things better.

Now that the business climate is improving, the challenge is to maintain that focus. SR

www.strategic-risk-global.com

**COMPLIANCE CULTURE**

The culture of corporate governance and risk management in the MENA region is very different to that of the US and Europe. "It is not unusual for companies not to have in-house compliance and risk management personnel or for the head of legal to assume the compliance role. This is a significant responsibility for the person allocated with such a dual role, particularly given the diversity of risk across the region," says Natalie R Boyd, partner at law firm K&L Gates.

"It can be difficult to explain to managers why and how their businesses are affected by extra-territorial legislation." This is starting to change, she says. "Legislators and regulators recognise the need to provide for international best practice. Companies are beginning to acknowledge that they cannot ignore the risks, particularly in terms of breaching anti-money laundering laws and extra-territorial laws and sanctions, which represent significant risk for the business and the individuals involved," says Boyd.

For example, recently there has been a significant push in the United Arab Emirates to apply international best practice, such as corporate governance codes and binding and non-binding guidelines for regulated banks. "Application of laws and regulations to government sector companies and individuals, however, is not always clear," says Boyd. "Confusion may arise as to who would fall within that sector and this can cause problems for firms operating within the territory."

There is no room for mistakes, however, and regulators in the region are becoming much more aggressive.

"A number of prominent financial institutions have been the subject of regulatory sanctions for failure to comply with corporate governance and compliance regulations," says Boyd. "This is reflected in the growth of specialist risk management companies setting up in the region. It is often easier for local companies to outsource to experts than to build up their own internal capacity."

"The region is reacting to changes that are evolving in other parts of the world and laws and regulations relating to risk management issues, and they are developing accordingly."

Paddy Lord, Control Risks

Doha, Qatar