Shock events that threaten global companies

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Geopolitical shifts around tariffs, governmental actions that affect trade, and terroristic activity are ever-increasing factors affecting today’s global business environment. As a global company, are you prepared for the impact this could have on your balance sheet or employees?

In a recent survey of Fortune 500 CEOs, the top threat cited (at 40%) was increased regulation, trade friction and other political events. Why? There are a variety of recent and current events driving some of this concern:

- In March 2019, it was estimated that $1.7 billion would have been lost daily if the US government shut down the US-Mexico border.
- US tariffs on goods imported from China are affecting company supply chains. According to the Wall Street Journal, companies such as Crocs, Yeti, Roomba vacuums and Go Pro have started producing goods in countries other than China to avoid as much as 25% tariffs on approximately $250 billion of imports. Apple is also considering shifting final assembly of some of its devices out of China to avoid US tariffs.
- Terrorism is another threat many companies face today. Per the Global Terrorism Index, the global economic impact of terrorism was $52 billion in 2018. This includes five countries with more than 1,000 deaths as a result of terror attacks.

The points above speak specifically to geopolitical/terrorism events that can endanger a business and its employees. However, there are a variety of “shock events” that can detrimentally affect both the balance sheet and safety of employees.

- What if there is a fire at your main production facility and production ceases for two months?
- What if a country in which your business operates experiences a nationalist movement and that nation's government confiscates your assets?
- How would your business, from the aspects of both profitability and employee well-being, recover from an active shooter crisis?

Are the answers to the above questions consistent for all of your global operations? Here we will discuss considerations and solutions that can help global companies protect themselves against these risks.
Identifying risks

From an enterprise risk management standpoint, the key consideration is to have a comprehensive understanding of your risk profile. Where is your stock located? What is the political environment in the country or countries where you operate? What is your US versus foreign risk? What are the links of the supply chain that lead to your finished product? Where are your employees located? Where do your employees travel? Identifying where your highest risk exposure lies allows you to develop a holistic strategy to mitigate risk, and further, determine what forms of risk transfer will be most beneficial for your balance sheet.

Protecting the balance sheet

The financial repercussions of a shock event can be significant. The most commonly used form of business interruption insurance is associated with property policies, and governmental actions are generally excluded. In an unendorsed property policy, to claim business interruption, the type of loss must be covered under the property policy. Examples of covered property losses include fire, lightning or explosion.

Would this coverage be beneficial in protecting the balance sheet if a factory had to close for two months due to a fire? Yes. However, there are other types of shock events that are not covered by this form of business interruption insurance that require further contemplation in understanding how to adequately protect against these risks.

US-domiciled company protecting US business interests

In the example given previously regarding the US-Mexico border, US government action could have triggered a retaliatory action by the Mexican government, causing a business interruption for US companies. If third-party governmental actions or terror events are an excluded cause of loss on a property policy, a trade disruption policy could protect the balance sheet interests of the US company.
The consequences of a border closure would be damaging for any affected business, but these industries, in particular, would feel the most significant impact:

- Manufacturers.
- Retail.
- Perishable/food industries.

Generally speaking, a trade disruption policy can indemnify against:

- Loss of profits.
- Contractual penalties.
- Resourcing expenses.
- Relocation costs.

Triggers can include:

- Trade embargoes.
- Border closures.
- Terrorism, war, strikes or civil commotion.
- Confiscation or nationalization.
- Emergency closures to supply routes.
- Insolvency.

A trade disruption policy is the most effective form of risk transfer for a US company looking to protect its balance sheet against the perils of political shock events that could disrupt its supply chain.

**US-domiciled company with foreign business interests**

We have discussed how business interruption applies in conjunction with a standard property policy and how US companies can protect their balance sheets from US-driven governmental actions that can trigger retaliatory actions by foreign countries, affecting trade. What about a US-domiciled company looking to protect its foreign entities or investments against the political actions of foreign governments where these assets are located? A political risk policy can help protect a US company’s balance sheet in the case of certain political events that affect their foreign assets.

This policy can provide coverage for both asset and contract risk. Claim triggers regarding asset risk can include:

- Confiscation, expropriation and nationalism.
- Forced abandonment or divestiture.
- Deprivation.
- Political violence.
- Trade disruption and business interruption.

**Political risk insurance is a type of insurance that can be taken out by businesses, of any size, against political risk — the risk that actions of a foreign country’s government or its citizens will result in a loss.**
Claim triggers for contract risk can include:

- Contractual default for nonpayment of goods or services, or nondelivery of goods or services paid for in advance.
- Contract frustration by the government of a foreign country.
- War or political violence.
- Wrongful calling of on-demand contract and bid bonds.

Like trade disruption, net asset value is used to determine the amount of the covered loss. From a risk transfer perspective, this policy is beneficial in minimizing the impact of a shock event on a company’s foreign entities due to the political actions of a foreign government or its citizens.

Protecting employees

The political environment of a country can be an indicator of the safety of employees around the world. For good reason, insurance is one of the last thoughts that may come to mind in the case of a shock event that causes harm to employees. As companies move forward, the financial and morale consequences of this type of loss can be detrimental. In response to this type of risk, Lockton developed a product called Terrorism Crisis Solutions. This coverage can include:

- Terrorism and sabotage coverage.
- Active assailant.
- Therapy for affected employees.
- Business interruption.
- Loss of attraction.
- Cleanup and forensics.

Geopolitical turmoil is a reality for global companies. Key impacts may come from business interruption, trade disruption, confiscation of foreign assets or harm to employees. An overall risk evaluation is needed to determine how a supply chain can be affected by a shock event and the extent of its severity. At Lockton, we have teams dedicated to these specific types of risks. If you would like to learn more, contact your Lockton account team or email international@lockton.com.

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