



Chartered Institute of  
Internal Auditors

**airmic**

# Navigating geopolitical risk

Building resilience  
demands collaboration  
in a challenging world

February 2023

In partnership with



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# Foreword

## Airmic

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**Post the pandemic, global expectations and energy levels were high and the mood for international cooperation was optimistic. There was an expectation that people and societies would be re-energised after the years of restrictions, and that a surge in the development and use of technology would create a better digital ecosystem and opportunities to thrive. Today, the future feels less secure and settled than expected, and optimism is more restrained. Taking decisions in such an uncertain and fragmented world is more difficult.**

Most in the current employment pool have only lived in a period of relative peace and global stability. The risk landscape has now been changed by more risks occurring and new and different risks emerging. With an escalating velocity in change and an increase in the complexity and connectivity between risks, we now find that risks considered beyond the horizon have arrived sooner than expected, and we now discover that elaborate supply chains have significant fragilities that were exposed by the natural world and the behaviour of some nations.

Business leaders need to look further over the horizon but not be frozen into inaction by what they find, and they need to take time to assess the velocity and the nature and impact of change heading their way. While understanding these dynamics will not solve anything, achieving greater clarity about risks and their potential effects will make it easier to create appropriate interventions and to build a more resilient business.

Risk and internal audit professionals share an inexperience in dealing with the current risk environment. They must master new technologies, understand business and technology dynamics, and partner the business and their other business peers to help synchronise business reactions with external realities. However, with a tendency to be driven by schedules of work sometimes fixed up to twelve months ahead, and with a degree of rigidity in many of the risk management and internal control frameworks used, including the creation and management of risk registers, professional flexibility can be inhibited at the very time when these professionals should be at their most agile. Risk and internal audit professionals must be responsive to the pace and nature of change, and continuously consider adjustments in their activities to reflect the purpose, culture and risk appetite of the business. They must operate a feedback loop and have the courage to step up with informed and timely recommendations for adjusting their approach collectively, where there are signals indicating they should do so.

In late 2022, McKinsey & Company reported that geopolitical risk was at the top of the CEO agenda. “In the face of fragmentation and uncertainty, many business leaders are responding by intensifying their focus on resilience.”<sup>1</sup>

Geopolitical risk is becoming far higher in profile on the risk radar of most businesses and is a board agenda item – and according to our research conducted in support of this report, one which demands a collaborative response from risk and internal audit professionals.

It is harder for businesses to plan for disruption. Businesses are monitoring and navigating the short-term risk outlook, scenario planning for the longer view, but keeping an eye on strategic opportunities that can emerge from volatility. Building resilience is imperative. Businesses need to be prepared to deal with significant disruption caused by political incidents.

**Julia Graham**  
CEO, Airmic

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1. <https://www.mckinsey.com/capabilities/risk-and-resilience/our-insights/how-to-build-geopolitical-resilience-amid-a-fragmenting-global-order>

# Foreword

## Chartered IIA

**Geopolitical uncertainty has for several years been ranked by Chief Audit Executives as one of the top risks facing organisations, as evidenced by the Chartered Institute of Internal Auditors annual Risk in Focus survey. Indeed, last year it was elevated from seventh biggest risk to third. However, despite its growing prominence and severity, geopolitical uncertainty is still the risk that, according to our research, internal audit spends the least time auditing. There is growing recognition that this needs to change, and we hope that this report will support those making that change.**

There are three key messages that I would highlight to help aid internal audit's thinking on navigating geopolitical risk.

First, as we have seen from the War in Ukraine geopolitical risk does not sit in a silo and should not be viewed as a standalone risk. In our increasingly interconnected world, geopolitical events exacerbate and interlink with existing business-critical risks. Sanctions have exacerbated legal, regulatory and compliance risk. Cyber-attacks originating from hostile states mean organisations are now facing an increasingly weaponised cybersecurity landscape. Supply chains are being disrupted like never before and organisations reputations are on the line unless they act swiftly to end their links with hostile states. At the same time, the spike in energy prices is a threat to organisations' financial stability and in some cases their very survival. This means internal audit functions need to ensure they integrate geopolitical considerations into their risk universe.

Second, internal audit cannot work alone in grappling with geopolitical uncertainty. In particular, internal audit and colleagues in risk management need to work closely together to support their organisations in navigating the perfect storm of interconnected risks in this new geopolitical era. This is why we are delighted to collaborate with our colleagues at Airmic on this report.

Third, none of us has a crystal ball and can predict future events, and even 'expert' commentators regularly get things wrong. For example, in 2016 few called the Brexit referendum correctly or that Donald Trump would be elected as President of the United States. A year ago experts on Russia never believed Putin would go ahead and invade Ukraine, and nobody could have predicted that the United Kingdom would have three Prime Ministers in less than a year! That these things did happen goes to underline the increasingly uncertain and volatile world we now find ourselves in. But what internal audit functions can do is work with their colleagues in risk to make sure their organisations have robust scenario planning processes in place, for when the unexpected does happen. Effective scenario planning will help to support greater resilience.

Geopolitical tensions continue to rise around the globe and there can be no doubt that geopolitical uncertainty is here to stay. I therefore hope this report provides you with ideas, approaches, and practical tips to help you support your organisations in navigating geopolitical uncertainty.

**Anne Kiem OBE**

*Chief Executive, Chartered Institute of Internal Auditors*

## Key takeaways:

# Building geopolitical resilience

Geopolitics is used broadly to refer to international politics – and sometimes even to aspects of domestic politics, especially when policy impacts relations between countries.

We are at an inflection point in geopolitics. The spectre of war has returned to Europe. Decoupling between the economies of the US and China, the world's two largest economic blocs, is reversing globalisation as we have known it. The International Monetary Fund's (IMF) World Uncertainty Index readings have hit elevated levels in recent times.

This report demonstrates why risk and internal audit professionals need to relook at the way they collaborate, as their organisations build resilience amid the maelstrom of geopolitical risks. Elevated uncertainty created by an increase in volatility, complexity and pace of change in a new geopolitical era calls for the following approaches to be adopted:

1.

**Be agile in responding to the challenges of 'once-in-a-generation events' occurring with regular frequency.** With Russia's invasion of Ukraine happening on the back of the pandemic, there is the danger of organisations making long lists of all the things that could possibly go wrong in geopolitics. But geopolitics is not a game of predicting the future. Some political observers have been chided for advising organisations that Russia had no rationale to invade Ukraine, but geopolitics is predicated on human behaviour – of leaders and citizens – which does not always go to script. All of this calls for organisations to be agile in responding to geopolitical crises and to be in a permanent state of readiness that recognises the nature of the crises we find ourselves in today.

2.

**Scenario planning and horizon scanning are the keys to preparing for geopolitical risk.** Organisations must resist the temptation to be events-led and retain agility for when crises may strike. But agility is not a licence for them to improvise their response on the fly. They have to constantly challenge, stress test and update all of their baseline assumptions about the likelihood and impact of the risks they face. Meanwhile, horizon scanning should focus on assessing the velocity, impacts and likelihood of major trends. A key output from this process would be a shortlist of risk scenarios captured in an emerging risk register, which is used to stress test the business planning cycle and development of future strategy.

3.

**Stereotypical profiles of risk and internal audit professionals need to be reviewed to ensure they meet future needs.** Risk management and internal audit have distinct responsibilities, but they must work together and at the same pace. Synchronicity is critical to the successful use of the Three Lines Model as adopted by the Institute of Internal Auditors (IIA), to achieve effective alignment, communication, coordination and collaboration. Professional education needs to balance soft and technical skills. The talent pool for the professions needs to be adequate for the needs of the future.

4.

**Take a long-term view of geopolitics.** ‘Long-term’ may be five years in certain Financial Reporting Council (FRC) guidance, or it may be 30 years in energy and infrastructure sectors. Nevertheless, organisations need to bear in the mind the geopolitically-related risks relevant to them and their supply chains, and not only in the short to medium term – reliable countries may no longer be friendly ones further down the road.

5.

**Stay true to the organisation’s purpose.** After Russia’s invasion of Ukraine, Western organisations were forced to make decisions as to whether to withdraw their operations from Russia, often after decades of investment there. It is imperative for organisations to be clear about their purpose, risk appetite and strategy, while also being agile in their responses to crises.

6.

**Geopolitics is not just all about downside risk.** Organisations must have the agility to seize upside opportunity, to cushion the impact of geopolitical crises, and enhance upside growth potential where possible.

7.

**Risk and internal audit need to operate as strategic enablers** by providing executive decision-makers in their organisations with information that is appropriate and timely as they make difficult decisions in a challenging environment.

# Introduction

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## Why should geopolitical risk matter?

As the word suggests, geopolitics is about how political power is linked to geographical space. But often today, 'geopolitics' is used broadly to refer to international politics – and sometimes even to aspects of domestic politics, especially when policy impacts relations between countries.

Geopolitical risks are rapidly becoming more prominent, and more severe. They are increasingly having a major impact on the long-term sustainability of a range of organisations and sectors.

The immediate geopolitical risks that many organisations are currently grappling with relate to soaring energy prices, rising inflation and the consequential increase in interest rates, to name just a few.

Some of these risks were already prominent and growing in severity as the global economy began to spring back to life following the Covid-19 pandemic. However, Russia's invasion of Ukraine, the biggest geopolitical event in decades, has now magnified and broadened the range of geopolitically related risks that organisations are wrestling with. Indeed, the war in Ukraine is arguably an event of historical significance which has transformed the post-Cold War consensus, with ramifications for years to come. In turn, it will reshape the risk landscape and global trading environment in which organisations operate.

With 2022 officially declared the hottest year ever in the UK, following the record-breaking temperatures last summer, accelerating climate change could increase and exacerbate geopolitical tensions further still. As well as resulting in countries competing over resources, increasing levels of mass migration from uninhabitable regions could lead to humanitarian crises and become a catalyst for military conflict.

All of this means geopolitical uncertainty is here to stay for the foreseeable future and will contribute to a more risky and volatile business environment for the years ahead. Therefore, geopolitical and geoeconomic risks should matter to both risk and internal audit professionals alike, as the respective third and second lines in the Three Lines Model. Both have a vital role to play in collaborating to address geopolitical risk.



# 1. Identifying geopolitical risks

**Despite not having featured in the top 10 risks in 2020 or 2021, according to Airmic’s annual survey of leading risk professionals, 2022 saw geopolitics rise to second place overall, in the wake of Russia’s invasion of Ukraine.<sup>2</sup> Internal audit professionals also recognise geopolitical and geoeconomic risk as being key, as it was identified as the third biggest risk in the Chartered IIA’s Risk in Focus 2023 report<sup>3</sup> – yet we also know from this research report that it is currently the risk that internal audit professionals are spending the least time and effort auditing.**

This suggests that while both risk and internal audit professionals have clearly registered geopolitical risk on the radar, they could be doing more to deliver value through thought leadership and guidance on how to effectively tackle it.

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*“Every time there is a geopolitical event, there is an almost immediate impact on pension funds and the value of people’s retirement incomes and savings. Even the rumour of a geopolitical risk could have a significant and immediate effect. Nothing has to actually happen for it to have a massive impact on our everyday decision making as a corporate organisation. The velocity of geopolitical risk is very, very high.”*

*Group Chief Internal Auditor, Asset Management Company*

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## Geopolitics as a risk, a theme, or events

The question therefore is whether geopolitics ought to be treated as a risk, or a theme, or whether it should be regarded in terms of events.

In surveys, geopolitical risk may indeed be regularly ranked alongside other risks such as

supply chain failure or the loss of reputation. But it is soon apparent that geopolitical risk in fact encompasses a range of interconnected risks, in a way that cannot be said for supply chain risk, for instance. Russia’s invasion of Ukraine may have been the realisation of a geopolitical risk, but it has also directly brought about supply chain failures, a spike in energy prices that has fuelled inflation and cyber incidents, among other risks.

Indeed, geopolitical risk is different from other risks in that it is a strategic risk, whereas some of the other risks it is connected to tend to be operational.

One can think instead of geopolitics as a theme – or specific occurrences such as the invasion of Ukraine as events – under which a range of risks can be mapped.

Some organisations take their principal risks – for instance, supply chain risk – and overlay themes such as geopolitics, geoeconomics, pandemic and climate across all of them. During the 2008 global financial crisis, these organisations were finding that the crisis touched on approximately a third of their top 10 or top 20 risks. When the Covid-19 pandemic occurred, organisations which did this exercise again found that the pandemic touched as much as 90% of their top risks.

Regardless of how we resolve this debate, we will continue to refer to geopolitical risk in this report for ease of reference.

2. <https://www.airmic.com/technical/library/airmic-annual-survey-2022-risk-and-resilience-perfect-storm>

3. <https://www.iaa.org.uk/policy-and-research/research-reports/risk-in-focus/>



### The impact of geopolitics on all other risks

*We don't really treat geopolitical risk as a primary risk. We see it as having an impact on all the other risks that we manage. As a major global investor, credit risk is our biggest risk by a considerable margin. But obviously, geopolitical risk and the uncertainty it creates have a significant impact on credit risk, and on credit markets and equity markets. We consider events as being geopolitical, and they bring consequences to our existing, underlying risks.*

*Group Chief Internal Auditor, Asset Management Company*



### Geopolitics is not about predicting events – scenario planning is essential

Many of the best political observers read the situation wrong and did not expect Russia to invade Ukraine. Russian troops were indeed amassing on the Ukrainian border in the lead-up to 24 February 2022, but these observers did not believe it was in Vladimir Putin's rational self-interest to carry out his threat of invading his neighbour. Nor was Putin preparing the Russian population for war, judging by what was on state-controlled media in the lead-up to the invasion.

Years earlier, the reputation of election pollsters took a battering when most of them wrongly called the result of the 2016 Brexit referendum in the UK. They also largely did not expect Donald Trump to be elected as US President that same year.

But monitoring geopolitics is not about predicting events before they happen. It may not always be an exact science – which is more an indication of how the assumptions underlying our world today are rapidly shifting, rather than an indictment of political observers and pollsters. But it is certainly not a crystal ball gazing exercise. It would be unwise to hedge your bets on just one possible outcome, no matter the degree of confidence one holds in that reading. Rather, the focus should turn to scenario analysis and planning, which the next chapter of this report will look at in depth. In other words, we should be forecasting several scenarios, rather than just betting on one outcome.



### Nobody can predict events

*It's a mistake to try to predict events. I don't think anybody can predict events. The value in forward thinking is to thoroughly understand what you might do if certain things did happen, rather than to try to predict what exactly would happen."*

*Head of Risk Management and Business Assurance, Mining Company*



## The ‘low-likelihood environment’ today

We can easily agree that geopolitics should be more about scenario analyses than about predicting the future. But even that requires difficult calls to be made. In prioritising the scenarios to prepare for, how much weight are we to give to low-likelihood events?

We find ourselves today in what has been called a ‘low-likelihood environment’, where once-in-a-generation events such as the pandemic and the invasion of Ukraine have followed each other in rapid succession.

Things are indeed in a state of flux now, with increased instability and complexity in geopolitics, and there is no clear answer as to the importance we ought to assign to low-likelihood events. After all, an organisation’s preparations could not be effective if it were to prepare for an overly long list of scenarios.

What this means is that risk and internal audit professionals must constantly challenge, stress test and update all of their baseline assumptions about the likelihood and impact of the risks their organisations face.



### Preparing for low-likelihood versus high-likelihood risks

*At times, we tell senior executives that they are spending too much time thinking about low-likelihood events. They were not thinking enough about high-likelihood events that may be less interesting. Instead, most senior executives are now worried about China invading Taiwan. We say to them: ‘Look, you’re worrying about the wrong thing.’ But they come back to us and say: ‘But you told us that Russia was unlikely to invade Ukraine!’*

*Political Analyst A*



### Don’t make long lists of what can go wrong

*Through the Ukraine crisis, we have seen two approaches. Some companies try to make the longest list possible of things that can go wrong, and make sure that they are prepared for all of them. That’s probably not a very good use of time. Others try to assign values to the likelihood of different types of events occurring, and prioritising what goes to the top of the list through this exercise*

*Political Analyst A*



## Problems faced in addressing geopolitical risk

Despite a deluge of information, organisations are often none the wiser as to what to make of geopolitics. The key lies in how risk and internal audit professionals can tie geopolitical risks back to their organisations to make these risks relevant.

Other problems faced in addressing geopolitical risk, as shared by risk and internal audit professionals, include the following:

**It is difficult to measure geopolitical risk unlike, say, how one can assign clear credit limits to an organisation's exposures across the globe.** The best way to tackle geopolitical risk is to have conversations, and to get different views, voices and opinions – but depending on such qualitative methods of monitoring risks means that those lacking expertise or knowledge in geopolitics may feel inadequate for the task of prioritising and preparing their organisations for them.

**Geopolitical risks sit very high up on risk registers in years like 2022, but the effort and time spent in managing and assessing those risks is very low.**<sup>4</sup> This is partly as a result of the challenge mentioned above, which creates a vicious circle.

**Outside of highly regulated industries such as the financial services sector, expertise in geopolitics tends to be less well developed.**

There is a sense in some quarters that aside from those in financial services, senior management tends to be led by instinct, which could often be wrong. This may well be an unfair judgement, but the bottom line is that in-house expertise in geopolitics tends to be more prevalent in the financial services sector than others.

**It takes a certain maturity for the organisation to think about things that could go wrong and spend time discussing it.**

Many organisations have literally been in a perpetual state of crisis management since the pandemic. During such a polycrisis, most organisations would be fixated on immediate operational challenges. They may not have the luxury of time or resources to devote to such discussions.

## The upside risks to geopolitics

Geopolitics is not just all about downside risk and avoiding those related risks. Rather than bemoan the state of geopolitics today, much of which is beyond the control of most organisations, they should tap into the opportunities from upside risk where they exist. There can be gains to be had even during periods of volatility if organisations are nimble and aware of their geopolitical environment.

When a company became aware of a possible change in the Brazilian government's stance on welcoming foreign direct investment in specific sectors, it modified its engagement

with Brazil and prepared plans to invest. That seemed counterintuitive at first. But because of the company's first mover advantage, it became the global leader in its product within five years following the change in Brazil's policy on foreign direct investment.

The company had looked to the upside of political risk and benefited from having highly skilled talent in Brazil and a large market in South America. In contrast, its key competitor lost 30% of its market share during this period and blamed this on the Brazilian government's attitude to it. This presents a clear case where political risk to one company was an opportunity to another.

4. Risk in Focus 2023: <https://www.iaa.org.uk/media/1692518/risk-in-focus-2023.pdf>

## 2. What's different today in geopolitics

### Globalisation, and now deglobalisation?

Geopolitics has changed dramatically since the end of the Cold War in 1991, when the Soviet Union collapsed, leaving the US as the world's sole superpower. While the situation is still in a state of flux, we are now seeing the possible signs of deglobalisation, after years of trade liberalisation which was made possible by the myriad of free trade agreements.

Decoupling between the economies of the US and China, the world's two largest economic blocs, is creating a host of risks. Could the world be fragmenting into blocs, each with different payment systems, reserve currencies and regulatory regimes?

With the rise of populist politics, and now with Russia's invasion of Ukraine, ominous warnings have been sounded that we could be on the cusp of another major global conflict similar to that of the 1930s. Could organisations once again find themselves unprepared, just as many were unprepared for the Covid-19 pandemic, despite pandemics being a regular occurrence throughout history? Even if another war does not come to pass, given the current geopolitical context, there will undoubtedly be other major events on the horizon that will have the potential to cause significant business disruption. If ever there was a time for risk management and internal audit to think the unthinkable, it is now.

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*"A whole generation had grown up since the 1990s, when international interaction was basically a free ride. There was no great power competition. The US Navy ruled the waves. People thought China was going to go capitalist. The last five years have shown the fallacy of all that thinking."*

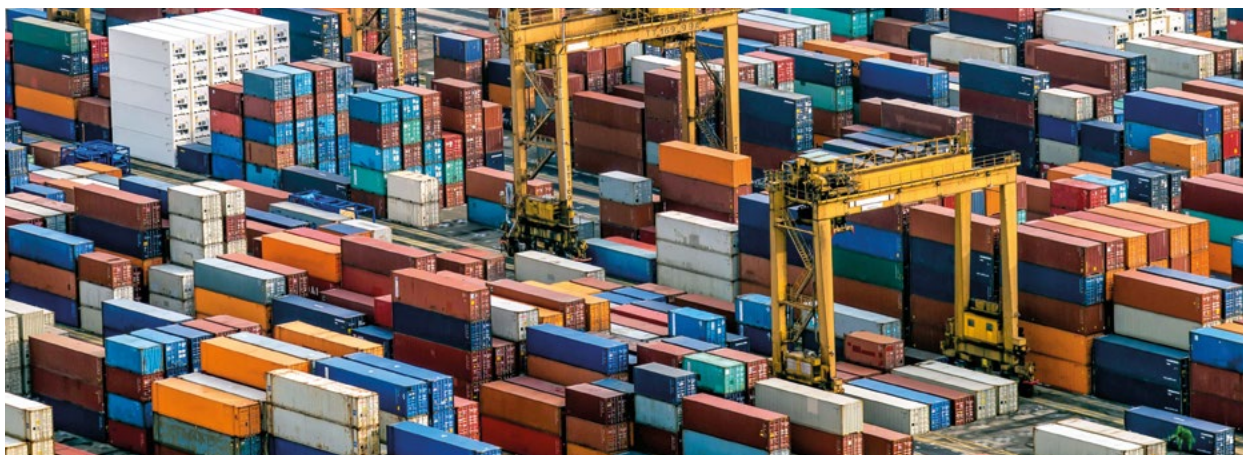
*Political Analyst B*

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*"It has been riveting over the past year to watch how two completely unrelated risks – the pandemic and Russia's invasion of Ukraine – combined to exacerbate all other risks. Before the Ukraine crisis, we were already dealing with supply chain issues coming out of the pandemic. All that has happened since has been exacerbated with inflation."*

*Senior Internal Audit Advisor*

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## Is geopolitics today just more of the same?

Despite claims that we are living in a ‘new’ era, geopolitical risk is something we have been living with for a long time. Governments often change, whether because of elections or revolutions. That in turn has determined the direction of foreign or economic policy. Industries also regularly evolve – as the outcome of government policies or boom-and-bust economic cycles.

The tools, techniques and skills for risk and internal audit professionals to tackle geopolitical risk have therefore all been around for some time. They may need to adapt these for their contexts and to the present age – but they need not reinvent the wheel. They also need to be more agile. For internal audit professionals, it also means moving away from fixed audit plans that are set a year in advance. Risk and internal audit professionals need to ensure the agility of risk assessments and assurance, and ensure they have spare capacity, so they can react to events more nimbly and flexibly to meet the needs of the business and the volatile risk universe of the 2020s.



### Three questions

*The three questions I focus on amid geopolitical risk are: **How do I keep relevant? How do I keep resilient? And how do I be responsible?***

*Non-Executive Director, Investment Company*



## Geopolitics and purpose

In the wake of Russia’s invasion of Ukraine, many Western companies were forced to make a stand and withdraw their operations and investments from Russia. Consequently, public relations departments have found themselves under unexpected pressure to make statements on political issues.

Businesses are more visible and more actively scrutinised than ever before. This has come as the result of social and economic shifts in the wider society, and changes in attitudes, thanks to rolling news and social media. Public concern over climate change and the disruption caused by it will increase over the coming decade.

Avoiding political controversy is becoming more difficult as consumers and campaigners demand that organisations take a position on the key

issues of the day. Typically, most businesses try to avoid becoming involved in anything political, but that stance is becoming increasingly difficult to sustain.

A clear definition of an organisation’s purpose and stakeholders can provide a reference point for managing and mitigating risks in these areas. In a rapidly changing world, it is easy to lose focus when running a complex business. In this new environment, corporate purpose is taking on a new salience. High-profile investment firms are increasingly asking questions about an organisation’s purpose, who it serves and who its stakeholders are.

Purpose, though, is more than just nice-sounding statements. It is essential that purpose is embedded within the organisation. Its purpose statement should therefore inform its strategy, its operating model, its performance measurement, its culture and its reward systems.

## Risk and internal audit professionals in collaboration

Geopolitical risks often lie outside the bounds of what businesses, and even the largest corporations, can control. Geopolitics could cause a global shortage of microchips and, suddenly, an entire sector could be in trouble. Businesses are not able to go ferreting out single points of failure in their supply chains. This transforms an operational challenge into a strategic one.

This brings us to the rationale that led Airmic and the Chartered Institute of Internal Auditors to collaborate on this report. Risk and internal audit professionals need to work closer together in order to navigate their organisations through the perfect storm. During the pandemic, risk and internal audit professionals stepped to the forefront of their organisations. As the debates and case studies in this report will show, greater collaboration is needed to tackle the heightened uncertainty and volatility of the new geopolitical era.

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*“There are big strategic questions as the world becomes increasingly divided. For instance, does a globalisation strategy still make sense? And these are very difficult questions to deal with using traditional frameworks. This calls for risk, internal audit, and strategy to work a lot closer together.”*

Political Analyst C

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## Potential geopolitical risk scenarios on the horizon

In course of the research, we explored six thematic case studies based on geopolitical scenarios that are either happening right now or could potentially be on the horizon. These are all scenarios that both risk and internal audit must take into consideration as they carry out their audit, assurance, and risk assessment work.



**Economic meltdown:**  
A global crisis on the horizon?



**Conflict involving China:**  
Taiwan and the South China Sea



**War in Ukraine:**  
Global implications



**Climate change and geopolitics**



**US politics and democracy:**  
Challenges to global stability



**Cyber security and geopolitics**

Each of the thematic case studies, included in the appendix of this report, are based on insights that were garnered from a series of roundtable discussions that we had with chief audit executives, chief risk officers and geopolitical experts from September to November 2022.

### 3. Risk and internal audit in collaboration

#### How risk and internal audit professionals approach geopolitical risk

When it comes to how best to assess geopolitical risk, there is no one-size-fits-all approach, even among the largest and most sophisticated organisations. The principle is to tie geopolitical risk back to the organisation's business. Geopolitical considerations need to be integrated into existing risk management and audit frameworks, and in the risk areas where geopolitical events can have the most impact.



#### Geopolitical risk as strategic risk

*In our risk taxonomy, geopolitical risk sits under our strategic risk. We always think of it like that because we are a global organisation with globally dispersed teams. We have risk professionals sitting in different regions around the globe, and they are constantly feeding information back to us about what's happening where they are. There are elections going on in some countries at any given point of time, or some kind of political instability in each region.*

*Then we keep indicators – red, amber, green – on the direction of travel of the trends they pick up. If there are particular issues of concern, they go into another framework we manage which looks at key emerging risks.*

*From an operational point of view, this is our daily business. It is also from a reputational point of view that we are watching these things all the time, to see if it all makes sense for us and for our strategy.*

*Global Director of Internal Audit, Consultancy Firm*



#### Along with other external risks

*We assess geopolitical risk along with the other external risks we face. We assess the impacts that external risks could have on our business objectives – financial impacts in terms of revenue or cost, or in terms of the impact they may have on our assets or liabilities, or our people. On the whole, the approach we take is qualitative rather than quantitative.*

*Internal Audit Director, Multinational Electric Utility Company*



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### Using the whole toolbox

*I would say that there isn't any risk out there that we're not looking at. We have a team looking at geopolitics, monitoring what's happening in all territories of the world. From their research, we can see what might become a geopolitical incident or a major risk. I don't think there's any tool out there that we haven't looked at, or that we haven't used. Dealing with geopolitical risk is part of our core business.*

*Head of Insurance, Technology Company*

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### Tools are only as good as the time invested in them

*Our risk team does PESTLE analyses, and a lot of horizon scanning. We also rely on our board members, as well as other public bodies, for intelligence and to contribute towards those analyses. I haven't seen any particular tool that cracks geopolitical risk. What I have seen in organisations, though, is where it isn't done very well – because they don't invest sufficient time in a particular tool to make it work well.*

*Head of Internal Audit, Public Body*

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### Probing the assumptions

*Audit should test the efficacy of processes, rather than tick boxes to say processes have been followed. When it comes to risk mapping, it's really important to capture how the people contemplating the risks actually came to those conclusions, rather than to just focus what's on the page.”*

*Business Unit Head, Insurance Group*

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### Asking the right questions

*We don't have any specific tool for identifying geopolitical risk. Once the risks are out there, the important thing is to ask: What does it mean for your business? To me, that is the most critical and most difficult question to answer.*

*Group Audit Director, Telco*

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### **Remember to audit for alternative scenarios too**

*We already had geopolitical risk and the macroeconomic environment as among our principal risks. To address these, one of our key mitigation actions has been to have very robust incident management and crisis resolution procedures in place when a major geopolitical event occurs.*

*So as part of our plans this year, we did an audit of how well this process is actually carried out. We had already been performing simulations of what could happen, so we went back to those simulations and audited the whole process.*

*No matter the type of crisis that occurs – whether it was an invasion of one country by another, or something else – we needed to provide assurance the process was in place and that it was working. So while a Russian invasion of Ukraine was one of the key potential scenarios for the year, we also had to be flexible and adjust our audit plan to test for other potential key events in geopolitics.*

*In providing assurance, it is critical that you are able to see what you can change in your audit approach, in order to find alternative scenarios to test for.*

*Corporate Audit Director, Fast-Moving Consumer Goods (FMCG) Company*



### **Demonstrating the value of risk management frameworks**

*How do we use the component parts of our risk management system to actively manage risk? We have built great frameworks for managing risk. But when the conversation happens somewhere else, we then have to update those frameworks retrospectively, rather than using them as an active tool.*

*So, take for instance a tool such as risk sensing – how do we use it? How does it inform our risk appetite? Do we change our risk appetite off the back of what risk sensing is telling us? How does that tie into our strategy and our capital plan, so that there is a clear cause and effect for each component part? Do we have to update our early warning indicators?*

*So as internal auditors, we need to ask these questions in demonstrating that the risk management frameworks we built have a place and a value.*

*Chief Audit Officer, Pension Fund*





## Geopolitics and hedging to the US dollar

*Every month, my team look at our net asset position, and we hedge all of our assets and liabilities back into US dollars. Obviously there are some currencies in the world where we can't do that. But even if there are tax costs to doing so, we think it protects us in ensuring we have enough US dollars in the organisation to meet all our liabilities. This is very closely aligned to geopolitical risk, but it's also just managing the overall balance sheet of the organisation.*

*Global Director of Internal Audit, Consultancy Firm*



## Tools, frameworks and approaches

### Stress testing

Financial services organisations are used to doing stress testing – and now even reverse stress testing, because of the regulatory framework. In determining the organisation's capital levels and the risks to that, which is what stress testing sets out to assess, a thorough understanding of geopolitical risk and other external risks is required. Risk culture and appetite shape the decision-making processes of banks and fund managers, which would have their own research departments. In contrast, smaller organisations, and smaller risk and internal audit functions, would be less likely to have the skillsets to monitor geopolitical risk in-house.

That said, some financial services organisations are facing challenges auditing some of their functions because they have to adapt much more quickly to the changes around them. A stress test model from even just three years ago would already be irrelevant today, so it would be pointless to audit it. For all their sophistication and maturity in using stress testing models, even financial services organisations know they need to be much more agile in adapting to the environment.

Models are a major component of what financial services organisations use to perform some of their analysis. Given the fast-changing environment, the models need to be updated more quickly, regarding the underlying assumptions they use as well as their sources of information.

Nevertheless, models still provide a useful indicator of things and a guide as to how organisations should look at different scenarios.

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*“We can all be hit with new risks and issues. You just have to continue to figure out the most effective ways to grow your resilience and your capabilities, while continuing to think about the latest challenges coming your way that your research is telling you about. Are you trying to build resilience around that?”*

*Head of Internal Audit, Large Financial Institution*

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*“It's all about recognising the context in which your organisation sits, and how you measure and manage the changes in that context.”*

*Non-Executive Director, Investment Company*

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## Sources of information and intelligence

We cannot expect all risk and internal audit professionals – or indeed people in any other roles within their organisations – to be trained in geopolitics. Despite how prevalent geopolitics may have been in the media headlines in recent years, it does still take a certain specialism to follow developments in the space and to get to grips with these.

In this age of free-flowing information online, there is no shortage of reports on geopolitics and economics to keep up with. Subject matter

experts can be engaged to weigh in. There then arises the challenge of weighing the different findings of each expert or report, especially when they are contradictory.

This is where roundtables can bring value, particularly when they can coalesce different skills, roles and insights both from within and from outside an organisation. They bring experts and managers together to debate their various findings, which may sometimes be at odds with each other, and crucially to link these back to the organisation so that the outcome of the roundtable discussion is always relevant.



### You need a view

*There is so much information out there, more than you can ask for. So, what you need is a process. To navigate a shape-shifting world which constantly transforms itself, you need to have a view. It's less about your information sources, because you can always find them.*

*Non-Executive Director, Investment Company*



### Dangers of silos

*Large organisations inevitably have different teams with deep specialism focusing on specific risks, or even components of a risk. That is where collaboration becomes even more important, because of the dangers of silos and blind spots in a large organisation.*

*Regional Insurance Manager, Food and Agricultural Company*



### Roundtables, diversity of thought

*Our approach is much more about roundtable multidisciplinary. The value that we have gained from that is the diversity of thought. No one now thinks they have a monopoly on the good ideas, because it has now been shown that black swan events are no longer once in 100 years or 200 years.*

*Chief Audit Officer, Pension Fund*





### **The importance of aggregating information**

*As an insurer, one of the things that is clearly important is to look at our aggregations. What we have learned from this exercise is that there were impacts which, on their own, would have been relatively benign. But when they aggregate with other impacts across multiple lines and industries, and also considering time phasing – where the order of magnitude of the impact on day one might be very different from that on day six – that’s where real risk management capabilities need to come in.*

*Business Unit Head, Insurance Group*



### **Links with intelligence and diplomatic services**

*We have a safety and security team which has close links with the Foreign, Commonwealth and Development Office, which gives them privileged intelligence information. Globally, we also have very close links with embassies and high commissions in many countries.*

*Enterprise Risk Manager, Public Body*



### **Disguising your sources in sensitive contexts**

*In each country that we operate, we have a corporate affairs presence whose role is to keep track of what’s going on, and send feedback to the centre. In some countries, that’s a bit difficult.*

*So China being one example. What we have are people in China whose job it is to kind of look at what’s happening in China. But as I was saying to some colleagues in our strategy team in the centre today is that we have to be very careful, because there are certain things our Chinese colleagues based in China can’t really say. They can’t say to us that the regime is in imminent danger of collapse, if that were the case. They just can’t.*

*Interestingly, we segregate the information that our folks in China have, and the information held in our centre. And when we run scenarios on China, we deliberately exclude our sources based in China, almost to protect them so that they won’t be challenged by the authorities there. This would allow our Chinese colleagues in China to say: ‘It was those guys in London [in the centre] who dreamed it up’.*

*Head of Risk Management and Business Assurance, Mining Company*



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**Intelligence sharing as a standing item on the board agenda**

*Intelligence sharing is key. One of the really good examples of best practice we have seen in the past six months is where boards devote a slot of 15 minutes or so for updates on geopolitical threats – primarily focusing on the Ukraine-Russia conflict, but also discussing wider issues including on Taiwan. Having that standing item on the board agenda to share intelligence for people who need to know, and to ensure that leads to actionable items, is really quite helpful.*

*Cyber Threat Analyst*

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## The applicability of the Three Lines Model to geopolitical risk

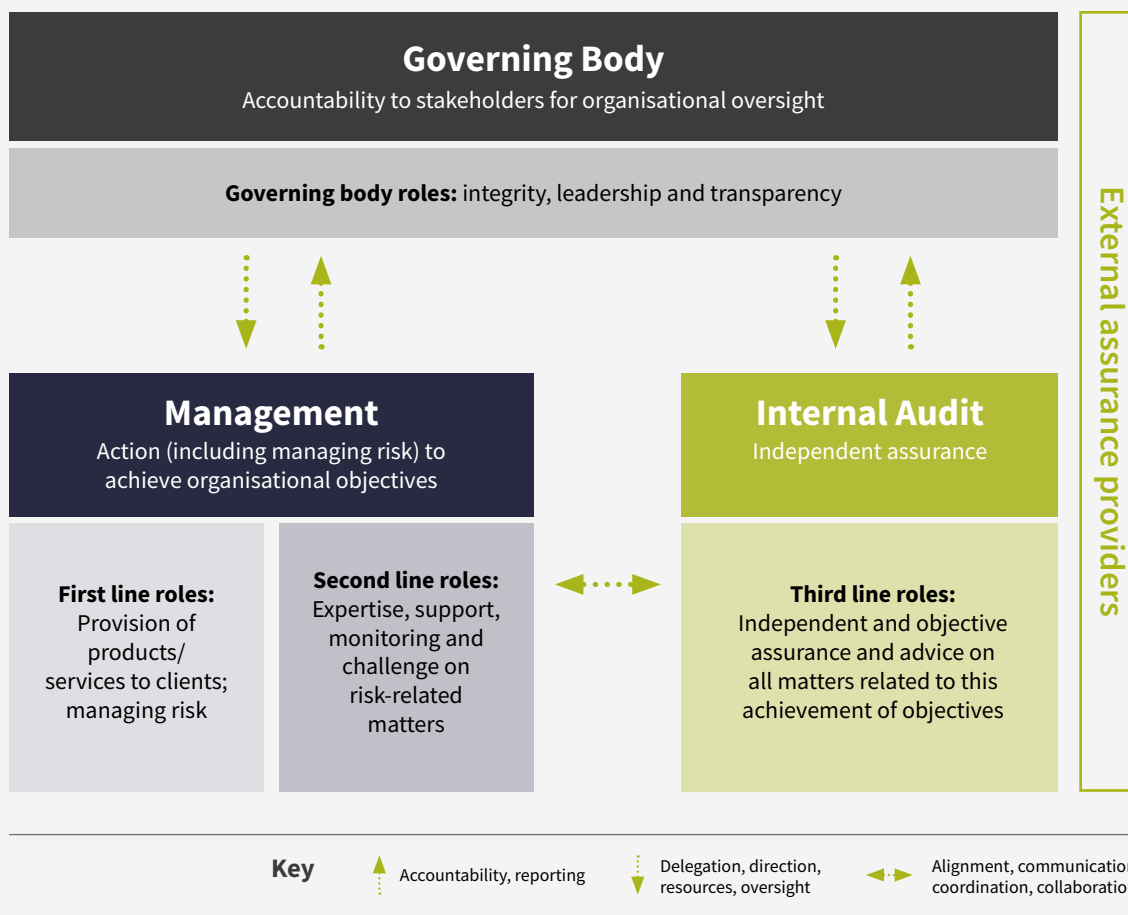
The Three Lines Model provides a basis for building and implementing robust assurance across an organisation, including providing transparency over the effectiveness of governance, risk management, internal audit and control processes. It can apply to all organisations, whether they are SMEs, corporates or regulated entities.

The purpose of the Three Lines Model is to protect and create long-term value, while setting out the expectations of different groups within the organisation:

- o Accountability by a governing body to stakeholders for organisational oversight through integrity, leadership, and transparency.
- o Actions (including managing risk) by management to achieve the objectives of the organisation through risk-based decision-making and application of resources.
- o Assurance and advice by an independent internal audit function to provide clarity and confidence and to promote and facilitate continuous improvement through rigorous inquiry and insightful communication.

Risk management and internal audit are complementary but distinct. But in no way does this mean that they should not collaborate. The successful use of the Three Lines Model requires effective alignment, communication, coordination and collaboration, with all roles operating concurrently.

## The Three Lines Model as adopted by the IIA (2020)



Strategic, tactical and operational risks must be synchronised to avoid the creation of lags. Risk management and internal audit must synchronise the different speeds at which geopolitical (or external) risk, tactical risk and internal (or operational) risk run. The job of risk and internal audit professionals is to challenge the organisation to make sure that lags do not emerge.



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*“As the second line, my role as risk management is to challenge the business, whether it’s about strategic or operational risk. And if I see something which is not properly done, it’s my role to say so and challenge it, and to work with the business to tackle it.”*

Head of Corporate Sustainability Risk Management  
and Risk Transfer, Stock Exchange

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*“The internal audit function should be willing to step up to the mark and say to the senior management, to whom they are providing reports: ‘Are you coming up with Plan B or Plan C, in case something happens?’ The answer might be ‘no’ or ‘not yet’. The internal audit team should be happy to say that’s not good enough. You may sometimes incur the wrath of senior management in doing so. But I think you need to be quite brave and be willing to sort of stick your neck out, and say what you think.”*

Vice-President, Corporate Audit, Auto Parts Company

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*“Traditionally, auditors used to do things such as testing operational controls and making sure that no one’s committing fraud in accounts payable. I’m seeing the world of internal audit evolving. It’s not just about assurance – it’s also advisory. If I think of topics that are not being talked about, or I think that management is doing too much navel-gazing, looking at the things that are happening on the day-to-day basis and not horizon scanning, that’s where I think internal audit can play quite an important role.”*

Chief Internal Auditor, Financial Services Firm

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*“We have a risk council for EMEA [Europe, the Middle East and Africa] which helps to identify geopolitical and other risks. We also have a risk council for middle management, and that’s really quite important because sometimes, people don’t tell the C-Suite or the VP [Vice-President] level what’s going on. By gathering the heads of all the pillars in your organisation in this two-layer format, it’s amazing what you will start to see emerging that you wouldn’t have otherwise seen.”*

Head of Insurance, Technology Company

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*“We collaborate closely with our risk colleagues, and then we try to give our input in terms of the internal aspects of the organisation. And of course, they talk with many other people at the senior level. When we prepare our audit plan, this is one of the most important inputs that we have.”*

Group Audit Director, Telco

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*“For us, internal audit and risk are very much a part of the same team. We identify the risks. We also work very closely with the business as well. So yes, anything that we find out in risk goes through into internal audit and we get information back from internal audit and the business.”*

Vice-President, Risk and Assurance,  
Chemicals Company

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## Engaging with the board

Risk management and internal audit must make sure that there is regular and open communication with the board on geopolitical risk. Geopolitical events can have a significant impact on the business’s ability to execute its corporate strategy and mission effectively, which is why the board must take geopolitical risk seriously. Risk and internal audit professionals should feel empowered to speak up and raise concerns they have about the impact of geopolitical risk events with the board.

When communicating with the board on geopolitical risk, it is vital that risk and internal audit professionals eschew technical language in favour of clear, business-like speech – especially on technical subjects such as cyber risk.

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*“I think the biggest turn-off for a board is to talk in a technical language which they don’t understand. It’s really important that we spend time and effort to communicate in business language.”*

CEO, Trade Association

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### Cyber and geopolitics: Two views

*To protect the customer, data is at the core of our strategy. The board is fully focused on how we protect data that comes from our customers. In at least every other risk committee meeting, we focus on managing cyber risk in the business, talking about plans or potential incidents which may have been raised in the internal audit reports we produce.*

*Group Audit Director, Telco*

*Some board committees are terrified by cyber security. Everybody's saying it's the biggest risk, but they don't fully understand cyber, so they could get very confused. The debate is usually about whether we have done enough on cyber security. The result is sometimes a scattergun approach, as opposed to a proper cyber risk management approach which would tell you whether or not we have proactive assurance in these areas.*

*Head of Internal Audit, Public Body*

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### Bespoke board sessions on cyber risk

*There is a trend for board committees to have bespoke sessions on cyber risk, splitting that out from their broader conversation on risk. That way, you can afford to spend a bit more time on building knowledge to assess things such as your own risk appetite as a company – and for board members to upskill themselves on the cyber threat landscape.*

*That doesn't necessarily mean you need to articulate the deep technical aspects of cyber threats to the board. Being able to talk through how a breach works, being able to understand which of your servers are encrypted and what data has been stolen – all this will eventually help them make a decision as to whether to pay a ransom or not, after a ransomware attack.*

*Cyber Threat Analyst*

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## Scenario analysis and planning: The key to geopolitical risk

Rather than focusing on predicting what would happen next in geopolitics, organisations should devote their energies to scenario analysis and planning. When risk and internal audit professionals ask questions along the lines of ‘what if?’, ‘so what?’ and then ‘now what?’, it helps their organisations adopt a mindset of being agile and adaptable, and thereby build resilience to tackle a range of risks in a volatile and unpredictable world.

Risk and internal audit professionals can work together by identifying geopolitical risks on the horizon, mapping their potential impact on their organisation and then running crisis simulation programmes to test the organisation’s responses.

Collaboration should not stop there. When it comes to issues relating to security and energy supply, risk and internal audit professionals should also work with governments and regulators where possible. They need to recognise that government policy will dictate or influence quite significantly some of the potential outcomes from these issues.



### Scenario planning: Making preparations in advance

*It can be hard to get boards to look at something that isn’t imminent. They tend to look at the immediate crisis in front of them, and then deal with the other crises when they happen. And of course when they happen, it’s too late. You could have made all sorts of interventions in advance. You could have made your life a lot easier by doing scenarios.*

CEO, Trade Association



### The how-to of scenario planning

*To devise scenarios, we have a global network of experts, not just in politics or economics, but also in a much broader range of areas. I think going broad is terribly important. You also need the right set-up. You would definitely need good information sources, and we also need to be quite all-embracing in that regard. We will then find the right people within the organisation who can process all that information, disseminate it and contextualise it for the organisation. Beyond that, it’s also important that you have the right structure and culture to use that information.*

Political Analyst B

*We build scenarios based on multiple inputs. We also do specific simulation exercises for particular risk events, which we find quite helpful because it helps the executive team understand how well equipped it is to deal with them. Usually there are deficiencies that show, and so one can then fix them. We have a central capability looking at geopolitical risk – typically people with diplomatic backgrounds. Some other companies would use people with an intelligence background.*

Head of Risk Management and Business Assurance, Mining Company





### **Actions, not just analyses**

*It was of course predicted that there may be a pandemic and it was a very prominent risk. In the UK, the government had that as a scenario, but people didn't want to make the investments to be sufficiently prepared for it. And I think that's a critical point on risk analysis and risk assessment – your risk analysis is only as good as the actions that you are prepared to take when that risk materialises. It's the actions that come out of your analyses that matter.*

*Head of Risk Management and Business Assurance, Mining Company*



### **Simulation and practice are important**

*It's surprising how many organisations don't have a well-defined crisis simulation programme, or they only do that once a year. Every organisation should regularly pretend something has gone terribly wrong, and practise 'flexing the muscles' you need in response. Because if you flex those muscles, you build them up and when it actually happens, you will be better at responding.*

*When we were seeing the build-up of Russian troops at the border with Ukraine, one of our colleagues in the cyber team asked: 'What can we do today to pre-empt, just in case something goes wrong from a cyber perspective?' So, one thing we considered and put into practice was to seal Ukraine from the rest of the cyber environment in which we operate. This would ensure that if something bad were to happen in one territory, it wouldn't affect another territory. It's the small things which come out of simulating unthinkable, complex scenarios that will matter when push comes to shove.*

*Vice-President, Corporate Audit, Auto Parts Company*



### **Doing scenario modelling with governments**

*What has become apparent from the Ukraine crisis is that scenario modelling really needs to be done with governments – and with corporates, as in our case as an insurer – particularly when you are looking at those kinds of security and energy supply issues. They cannot really be done in isolation by individual risk managers in individual companies, without recognising that government policy will dictate or influence quite significantly some of the potential outcomes.*

*Business Unit Head, Insurance Group*



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### **Don't write too many scenarios**

*You can write a limited number of scenarios, and you might get lucky when one of those comes true. You can write a huge number of scenarios, and it's a library, but they are basically unusable. There's a point somewhere in the middle where you should try to land.*

*Political Analyst B*

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### **Be agile, don't follow the book**

*But the most important thing is having an awareness around you, and to be agile in adapting your responses. When crisis strikes, you should not be saying: 'Oh my God, what does the book say we should do next?' Because the playbook is almost certainly not going to be right about the situation you are actually facing.*

*Political Analyst B*

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### **Unpredictable geopolitics and human beings**

*With scenarios in geopolitics, we are dealing with human beings, and they can be highly unpredictable. What we are finding is that the data hasn't caught up with the behaviours. So, in the short term, we are moving away from a lot of detailed analysis and scenario planning to much more qualitative overlays. So, we are using the data, but we are caveating its use.”*

*Chief Audit Officer, Pension Fund*

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### **Connecting geopolitics with other risks**

Having conducted a scenario analysis, it is important to connect geopolitical risk with the organisation's other principal risks. In some of the more technical types of scenario analyses such as those relating to climate, it is also crucial to take into account tipping points, step changes, and macroeconomic impacts and trends, rather than just making linear projections of the future.



## Climate scenario analysis 2.0

*A climate scenario analysis 1.0 can be converted into a climate scenario analysis 2.0 to include risks related to geopolitics, cyber security, financial credit markets, and so on. The climate scenario analysis that companies generally apply now has limited ownership – it is undertaken either by sustainability teams or risk divisions to address reporting requirements basically. And it's very technical, academic, and it comes up with outcomes that are very linear.*

*What's possible going forward is to embed scenario analysis with stress testing, engaging the C-suite and engendering more ownership, in order to achieve some practical and tangible solutions to implement. Only when different business units come to the table to talk about decisions related to geopolitics, as well as climate, would the scenario analysis be representative of the real world. We can then consider tipping points, step changes, macroeconomic impacts, and trends. This means the company is actually taking a strategic outlook rather than just ticking boxes because of regulatory requirements, or to satisfy a reporting standard.*

*Sustainability and Climate Advisor*



## What is it?

### Climate Scenario Analysis 1.0

Engages with a core group, focusing on long-term climate trends and impacts at a high-level where the outcomes are plotted on a linear basis.

### Climate Scenario Analysis 2.0

Engages with the C-suite and senior management through an interactive exercise tied to the organisation's strategy, assessing the implications of climate trends across all timeframes that are relevant to the organisation. Crucially, it takes into consideration tipping points, step-changes, macro trends, and outcomes – which may not always be linear – to be more representative of the real world.<sup>5</sup>

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*“We have a team that does nothing but just come up with different scenarios. We work out which ones we believe are most likely to happen, and then different teams will address them. With the Ukraine-Russia risk, for example, an American multinational corporation put together a cross-functional group which included our organisation. We met on a weekly basis and looked at how literally all of the impacts you would know about could happen. We also looked at longer-term things, things that haven't happened yet. For example, what happens if China invades Taiwan?”*

*So we do have many different scenarios that we plan in advance for, and we have active planning committees to deal with day-to-day events when they happen.”*

*Head of Insurance, Technology Company*

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5. <https://www.sustainability.com/globalassets/sustainability.com/thinking/pdfs/2022/climate-scenario-analysis-blueprint-nov2022.pdf>

## What are the skills and competencies needed?

The sense among risk and internal audit professionals is that specialist skills such as geopolitics expertise can be met through partnerships with third parties – through an expert or consultant in geopolitics, for instance. Rather, it is interpersonal management skills that are key for drawing the intelligence on geopolitical risk back to the organisation, to understand how it will be impacted and what steps need to be taken.



### Future of the internal audit profession

*Many young auditors have lived through a world of low inflation, low interest rates – and generally, a world of low volatility. And we’re bringing a young cohort into the world of internal audit where we’re throwing at them non-procedural, uncertain topics. How do we deal with macroeconomic risk? How do we deal with a pandemic? How do we deal with war? We must look after our young auditors, so that they would want to stay in this important profession.*

*Vice-President, Corporate Audit, Auto Parts Company*



### Interpersonal skills matter more

*It’s not really about the skills or the qualifications [when it comes to geopolitics]. It should be more about the ability to think outside of silos, and to network with people, to listen and to collaborate. If anyone thinks they have got all the skillsets they need and can solve things on their own, they are the problem, not the solution.*

*Head of Insurance, Technology Company*



### Upskilling in the fast-moving climate space

*There is not enough talent around the world who demonstrate these skills and understanding, or who have the necessary educational background. So, we harness the transferable skills that exist in our company, and upskill those of our people who demonstrate intellectual curiosity, and who are willing to be agile in an ever-changing topic. Because one day, it could be about environmental standards and, the next day, it could be about tackling the energy crisis, because topics move so fast. So, I think those who demonstrate agility, adaptability, and who are not afraid of uncertainty and change, are those who will be successful in this space.*

*Sustainability and Climate Advisor*



## 4. Conclusion

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**Geopolitical uncertainty is here to stay and will contribute to a more risky and volatile business environment for the years ahead. Therefore, geopolitical risk should matter to both risk and internal audit professionals alike. They need to relook at the way they collaborate, as their organisations build resilience amid the maelstrom of geopolitical risks. The conclusions from this report include the following:**

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1

**Geopolitical risk is not a standalone risk that sits in a silo.**

It connects and exacerbates a wide range of business-critical risks including reputation, legal and regulatory, cyber security and even financial stability and liquidity, to name just a few.

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2

**Geopolitical risk should be viewed as a strategic risk.**

One that exacerbates and heightens a wide range of risks, as we have witnessed with disruption to supply chains, inflation, interest rates and cyber-attacks, among other issues.

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3

**None of us has the power to predict future geopolitical events – but we have the means to do scenario planning.**

By making plans based on plausible potential events, organisations can be prepared for geopolitical disruption. Simulation exercises and practice are therefore vital in managing and mitigating geopolitical risk. Financial stress testing, as is common across financial services and publicly listed firms, can also play a key role.

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4

**Risk and internal audit professionals must speak up and say the unthinkable on geopolitical risk and scenarios.**

Even where this risks them being unpopular with senior management or the board. The bigger risk is of senior management or the board turning around and saying ‘Why didn’t anyone see this coming?’ or ‘Where was risk management and internal audit – why didn’t they see this coming?’

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5

**Risk management, internal audit and the board must work closely together as partners in good geopolitical risk governance.**

The key to this is sharing intelligence and rendering it relevant to the organisation.

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# Appendix

## Case study



## Economic meltdown: A global crisis on the horizon?

### Background

Much as geopolitics refers to international politics, geoconomics is about how countries use their economic power to achieve political ends. For instance, Russia has cut off energy supplies to Europe in the midst of its invasion of Ukraine, as a means to pressure Western countries over their support for Kyiv.

Macroeconomic risk derives from the behaviour of industries and governments, and the relationships between them. It concerns fiscal and monetary policies, trade and investment flows, and political developments on a national and international scale, and the effects of these factors on financial portfolios and company valuations. Intermediate variables of particular importance to macroeconomic risk include equities and commodities markets, business cycle, unemployment, inflation, interest rates, prices and exports/imports.<sup>6</sup>

- While economies recovered in 2021, following the deepest global recession since World War II, the sharp return of demand caused prices to soar, in some cases at rates not seen in decades.

One-third of interviewees, including chief audit executives, audit committee chairs and CEOs, who participated in the Chartered Institute of Internal Auditors Risk in Focus 2022 research expressed concerns over macroeconomic uncertainty, with some singling out rising prices as an area to watch.

- The war in Ukraine has further exacerbated the economic challenges many countries now face, putting even more pressure on the cost of energy, wheat, cooking oil and other goods, all of which are likely to fuel inflation further still, along with consequent interest rate rises.
- As a result, businesses will need to keep a close eye on their cost of production and revenue management to determine whether recent developments are merely a blip or spell a more fundamental and lasting macroeconomic pressure. In this context, internal audit is well placed to ask the right questions such as:
  - Is the business in an industry that is especially exposed to inflation?

6. Global Risk Institute <https://globalriskinstitute.org/research/macroeconomic-risk/>

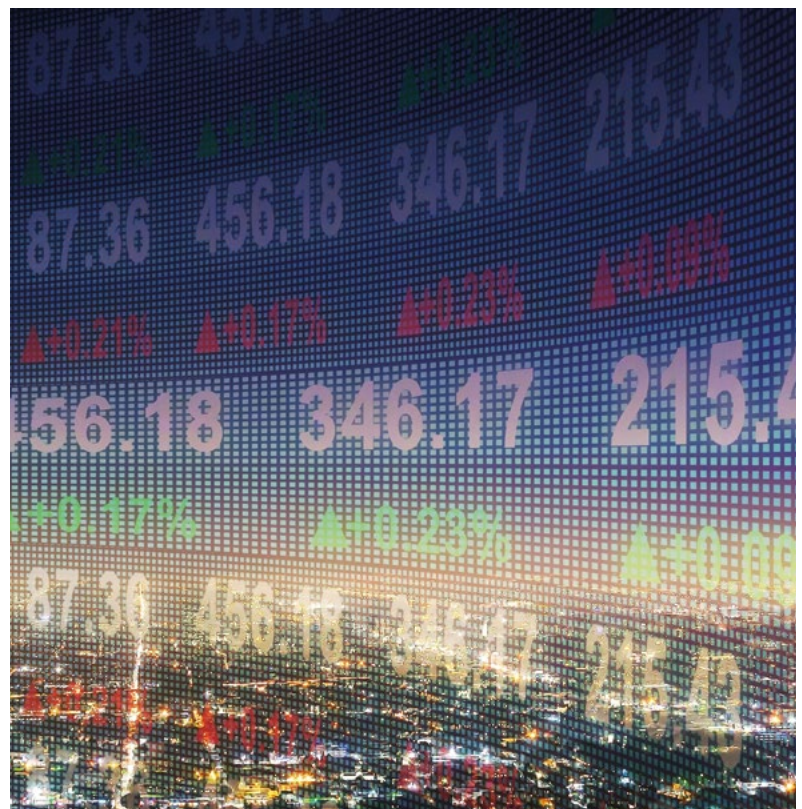
- o Is senior management having discussions about the potential for long-term inflation and what it means for the business?
- o Is the revenue management function assessing any price increases that need to be made in order to maintain and grow profitability without putting turnover at risk?

Meanwhile, the metrics clearly bear out the shift of economic gravity from the West to the East. In 1970, the largest bank in the world was Bank of America, with \$25 billion in assets. As of 2021, the largest bank in the world is the Industrial and Commercial Bank Of China (ICBC), with \$5.5 trillion in assets.

Macroeconomic and geopolitical uncertainty is having a strong impact on many other risk areas such as financial stability, reputation, supply chain, business continuity, cyber security or even human capital, diversity and talent management. As businesses battle against soaring energy prices, rising inflation, supply chain issues, disrupted workplaces and so on, it seems that internal audit should look at macroeconomic and geopolitical uncertainty more closely than it is at present.

The risk and internal audit professionals in our roundtables shared the following observations:

- There may be a financial crisis looming, but the banking sector is in a stronger position than it was on the eve of the 2008 global financial crisis – largely due to the measures imposed on the sector since then, which have built resilience and reserves. So, while there is clearly a geopolitical crisis ongoing, there is unlikely to be a global financial crisis, which is a distinctly different situation.
- It will be more of a social crisis that is looming, as the rise in the cost of living starts to bite.
- Nevertheless, given that the sterling has weakened, it does leave UK businesses vulnerable to takeovers, as the price point of the UK businesses becomes attractive. Mergers and acquisitions risk is therefore likely to rise in prominence.
- The board and executive level need to understand the environment they are operating in. Organisations need to understand their risk-reward model and how that is changing – because that is what drives decision-making.
- The role of governments has changed and, with that, the expectation that people have of governments. During the pandemic – and now the energy crisis – it was governments rather than banks who were the lender of last resort. This also signifies a new relationship between the state and businesses.



## Case study



# Conflict involving China: Taiwan and the South China Sea

## Background

- While underlying tensions between China, the US and other Western countries have been ongoing for a long time, not least with their fundamentally different political systems and their divergent views on international relations, the relationship took a definitive turn for the worse with the 'trade wars' when Donald Trump was US President.
- Chinese President Xi Jinping has been increasingly bellicose about 'taking back' Taiwan, which he regards as a Chinese province, raising fears of an imminent invasion of the island. The 2022 visit to Taiwan of Nancy Pelosi, the then Speaker of the US House of Representatives, which resulted in China conducting military exercises in the area, underlines the volatility and unpredictability of the situation.
- China has also become more assertive in the South China Sea, much of which it continues to claim as its own territory, rejecting the 2016 ruling of an international tribunal. The US and China are also in disagreement over the freedom of navigation in the South China Sea, and there is a real risk of clashes between the two sides.
- Tensions between China and the West have heightened since Russia's invasion of Ukraine. Partly because of the 'partnership without limits' declared between Russia and China in the lead-up to the Ukraine invasion, fears have been stoked that China is getting serious about invading Taiwan.
- Taiwan manufactures around two-thirds of the world's microchips, which are needed to make phones, drones, and set up supercomputers and cellular networks, and even weapons.<sup>7</sup> A conflict that engulfs Taiwan will therefore cause major disruption to the semiconductor supply chain and all the industries around the world that rely on it.

7. <https://asia.nikkei.com/Business/Tech/Semiconductors/Taiwan-s-share-of-contract-chipmaking-to-hit-66-this-year-report>

## The concerns of organisations regarding China:

- **Losing the licence to operate.** “One of our principal risks is losing our licence to operate in China, because of the reliance of our business on China.”
- **Sanctions on China will be even more impactful than sanctions on Russia.** “The UK’s sanctions regime on Russia during the Ukraine crisis has gone beyond what we have ever seen, in terms of how deeply the professional services sector has been drawn into that. We worry about how much more far-reaching the impact would be of such a sanctions regime potentially applied to China.”
- **An overnight supply chain break with China following any acts of military aggression.** Besides the impact on the global semiconductor supply chain that conflict involving Taiwan would bring, there would be widespread disruption in global supply chains affecting many industries, by virtue of how much more China is integrated with the global economy than Russia has been.
- **Diminished trade would disrupt our markets.** “We have no major operations in China. But if a serious split between China and the West occurred, leading to heavily diminished trade between China and the rest of the world, that would have a dramatic effect on the market for what we produce.”
- **A rise in anti-West sentiments within China.** “I have been interacting with colleagues at a state university in China for more than 20 years. But over the past year, I have sensed a real hardening of their views regarding the West ... I picked up a lot of resentment and hostility coming from colleagues there as they watched how Western countries responded to the Ukraine crisis.”
- **“Damned if you do, damned if you don’t”.** A mining company exited China because it wanted to ‘do the right thing’ in view of reports about China’s human rights violations, among other issues. However, its credit rating was subsequently downgraded by the international rating agencies, because of how its financial outlook worsened as a result of exiting the lucrative China market.

## Trends to watch out for

### Friend-shoring

With an eye on China, US officials are leading a trend for organisations to shift their manufacturing operations to countries with shared political values. This has meant moving production and jobs away from China to ‘friendly’ countries in the Asia-Pacific region such as Indonesia, Malaysia and Vietnam, as a means of safeguarding their supply chains and reducing their reliance on authoritarian regimes such as China.

### ‘Gray zone aggression’

Even when a state uses means short of military action, they could still weaken other states and cause losses for businesses. Elisabeth Braw, a senior fellow at the American Enterprise Institute in Washington DC, has termed this ‘gray-zone aggression’, which could involve cyber-attacks, intellectual property theft or coercive economic actions such as the cancelling of critical sponsorship deals, all of which could inflict economic harm. Gray-zone aggression can be hard to respond to because of the ambiguity behind who exactly is involved and what their intent is – but such tactics could nevertheless have the effect of exerting political pressure on the targeted country.<sup>8</sup>



### The risk of ‘fighting the last war’

*I think the scenario involving China and Taiwan is probably going to be quite different than what happened between Russia and Ukraine. Everyone is focused on learning the Russia lesson, which is important. But at the same time, there is a risk that we would be ‘fighting the last war’ and be caught out when the next war turns out differently. I think miscalculations between the US and China are more likely in the South China Sea, rather than around Taiwan.”*

Political Analyst C



8. <https://www.wtwco.com/en-GB/Insights/2022/09/geopolitical-risk-gray-zone-aggression>

## Case study



# War in Ukraine: Global implications

## Background

- While Russian troops had occupied the Crimea in 2014 and had more recently been massing near the Ukrainian border since late 2021, Russia's invasion on 24 February 2022 took many by surprise. There were no signs that Putin was preparing the wider Russian population for the war – which he continues to call a 'special military operation' – and indeed he kept plans for the invasion secret within a tight group of close advisors.
- There is uncertainty over how long the war will last. While Ukraine has retaken some of its territory lost to Russian forces in the early days of the war, one year on, the conflict continues and has drawn other countries in to a certain extent. Therefore, a long-term view on the conflict is required.

## How organisations responded to the invasion of Ukraine:

- **Prioritising different levels of impacts.** "When the invasion happened, it was imperative for us to identify the first order of magnitude impacts.

As an insurance company, we looked at people and the assets and operations that we insured on the ground. In terms of the second order of magnitude impacts, we looked at how the events actually impacted our risks in a broader sense. For instance, we looked at how Russia's threat to reduce the piping of natural gas and oil products to the West would impact our customers. And then in terms of the third order of magnitude impacts, we were trying to conceptualise what the proliferation of the war would bring about. Then we developed a number of scenarios."

- **Be prepared to respond with agility and speed, for business continuity.** "Within two weeks of the invasion, we withdrew our brands from Russia. It was very, very fast moving indeed for a company as large as we are, which was deeply established in Russia. It was also very important how ready we were to react to the changes that are happening there. What really helped was that we had already established a team looking at incident management and crisis resolution, which we mobilise when major unexpected events happen."

- **Mapping long-term scenarios.** “A long war was one of the four scenarios we modelled back in February 2022 when the invasion occurred. We looked at revenue, military, supply chain, energy crisis, economic, nuclear, cyber and other factors. In fact, the invasion itself could be said to be the outcome of a decade-long war going back to Russia’s annexation of Crimea in 2014. We had already been asking what the impact of such a decade-long war could result in during the year 2022.”
- **Disposing of assets in Russia.** “Many organisations have sold off their units or operations in Russia, and do not plan on returning anytime soon – although there are cases of some having written into their sale contract a right for them to buy back the asset some years further down the line.
- **Learning the lessons as we go.** “We are living through a ‘live’ stress test now and learning the lessons. We spent so much time doing scenario analysis and building our recovery and resolution plans – we are living through a test of those documents now. One of the things my organisation has really appreciated from this is that theory and practice are often quite different. And approaching this as a siloed team would not work. We have broken down some of those internal barriers and approached the issue in a more multidisciplinary way.”

## Reflections and lessons learnt:

- **The importance of scenario planning in an unpredictable world.** “We have had a Ukraine invasion scenario in our analytics tool since 2018. What eventually happened wasn’t exactly what our scenario said, but it was close. What we didn’t anticipate was how others would react – how our competitors would react or how our employees would react. On the eve of the invasion, we were still receiving advice that there was a 90% chance that Russia would not invade Ukraine. So, I’m a big believer in scenario planning.”



- **Risk and internal audit professionals are primed to think long term for their organisations.** It is often observed how the corporate world tends to think short term, because of the pressures of quarterly reporting. Risk and audit professionals, by the very nature of their work, have to take a broader approach.

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### Taking sides in Ukraine conflict

*Companies and investors are having to take sides. We have seen many Western companies leaving Russia, and vice versa too – Russian businesses leaving the West. If you think about supply chain implications and talent issues, and all the other things they might touch on, there is major real impact on markets, businesses and national economies.*

*Head of Internal Audit, Online Food Delivery Company*

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## Case study



# Climate change and geopolitics

## Background

- Most people may think of climate change action as primarily involving scientists and governments – but there is a clear geopolitical angle to it which keeps businesses and other organisations up at night.
- **Resistance from citizens.** There was much progress made at the COP26 UN climate summit in Glasgow in 2021, notably with the pledges on methane reduction and deforestation – but these pledges have been a difficult sell to citizens, as countries emerge from pandemic public debt. There seems to be a disjuncture between governments and their citizens.
  - For instance, in a June 2021 referendum in Switzerland before the COP26 summit, voters narrowly rejected a new law that would have helped the country meet its goal of cutting carbon emissions under the Paris Agreement on Climate Change. The draft law included measures such as increasing a surcharge on car fuel and imposing a levy on flight tickets.<sup>9</sup>
- **Ukraine and the energy crisis.** The war in Ukraine and the resultant impact on energy and commodity prices, and inflation, have heightened the challenges in coming to a global consensus at the subsequent COP27 summit held in Egypt. Governments have asked for coal-fired power plants to be kept open.
- **Developing countries and the issue of equitability.** More climate finance needs to be unlocked to help developing countries cut their emissions without negatively impacting their economic development and to transition away from fossil fuel dependence. Developing countries have argued that it is not equitable for developed countries to demand that they cut their emissions, as developed countries had polluted the planet during their economic development in earlier eras. Yet governments of developed countries struggle to convince their electorates that they need to unlock such climate finance for the benefit of developing countries.

9. <https://www.reuters.com/world/china/swiss-voters-decide-pesticides-ban-terrorism-law-covid-19-aid-2021-06-12/>

- **A zero-sum game between energy prices and green investments?** There are fears that the rise in wholesale energy prices is having the effect of reducing the amount of money available for green investment.

## COP27: The expectations of risk and internal audit professionals, and their organisations

In the lead-up to the COP27 UN Climate Change Summit, which took place in Sharm El-Sheikh, Egypt in November 2022, risk and internal audit professionals shared with us the expectations they and their organisations had in terms of the summit's outcomes, as well as their take on global climate action more generally:

- **Businesses recognise the importance of achieving the target of preventing average temperatures from rising by more than 1.5 degrees Celsius above pre-industrial levels.** But they sensed that the willingness, politically, for governments to cooperate had been dissipating since the COP26 summit in Glasgow, due to increased geopolitical tensions. They feared it would be harder to get that consensus or nearer that consensus at COP27, and therefore harder for governments and businesses alike to achieve their targets.
- Businesses also recognise that **if the developing countries do not have enough funds for climate-related solutions**, it would become a global problem which would sit on the balance sheets of companies through the value chain, and through the investment platforms.
- **It is important to take an industry sector approach when mooted energy efficiency solutions.** Consider for instance the construction sector, which has been responsible for about 40% of the energy demand in Europe. If the construction sector were to embark on a journey to utilise energy efficiency mechanisms and new ways of sourcing the energy it needs, it would release some of the energy supply for the other parts of the economy and for the world.

- **Businesses appreciate the need for climate-related regulation, but they want advance notice of such regulation.** Ideally, they would like governments to give early warning of two to four years of when such regulation would be imposed. Some businesses have been caught out in the past, where the introduction of new climate-related regulation resulted in the disappearance of some of their end-use markets. Having a handle on regulation in advance would make a big difference to them, especially smaller businesses for which it would help level the playing field.

COP27 was billed as the 'Implementation COP'<sup>10</sup> – the moment to implement the pledges made at the COP26 in Glasgow – but observers were disappointed on that front. The emissions cuts pledged did not add up sufficiently to limit the temperature rise to 1.5 degrees Celsius above pre-industrial levels.<sup>11</sup> Nevertheless, there were some bright spots, such as the fund established to help countries facing severe damage from climate change.



### Challenges today will seem like a picnic in 50 years

*If you've got positions as a company, or if you've got risk, the related things like achieving 1.5 degrees, that doesn't go away just because there's a conflict and there's terrible economic and societal consequences. It is indeed not easy, but the reality is that if we don't sort out 1.5 degrees, what's going on right now with the climate will seem like a picnic in 50 years' time. So, the challenge is how to act when we have some tough short-term issues, while we still have our 1.5 degrees commitment. We are still working with customers and with investing companies to work on their transition plans and help them manage the risk associated with the transition.*

*Head of Sustainability Risk, Insurance Company*



10. <https://www.un.org/africarenewal/news/cop27-outcome-reflections-progress-made-opportunities-missed>

11. <https://www.wri.org/insights/cop27-key-outcomes-un-climate-talks-sharm-el-sheikh>



## The case for renewable energy in times of crisis

*We shouldn't forget that technically, like every climate-related risk, the current challenges with inflation and the rise in commodity prices also present opportunity to the world to turn to renewable forms of energy, instead of going back to the old ways of providing energy through coal power plants.*

*Sustainability and Climate Advisor*

*If the government invests in insulating properties, and promoting new wind and solar farms, which can be built in one or two years, that would be far quicker than launching a new gas field or to start fracking – that will actually increase our energy security much more quickly than some of the higher carbon intensity forms of generation. And we would reduce people's utility bills much more quickly. So, I think as long as the message is delivered in the right way, progress in climate action is still possible at this time.*

*Internal Audit Director, Multinational Electric Utility Company*



## What businesses want governments and regulators to do

- A roundtable participant from a utility company wanted **governments to be more proactive rather than reactive**. Businesses understand that it would cost more to deal with the effects of climate change when they strike, and it therefore makes sense for governments to be more proactive and reduce emissions in the first place.
- **Governments need to include energy conservation within their climate change approach, as it is one of the lowest-hanging fruit.** It also represents the lowest marginal cost improvement that can be taken, with no investment required for it. Energy subsidies are all still going towards fossil fuels. In the words of one roundtable participant, “**Governments paying people to pay for more expensive fossil fuel energy doesn't make sense.**”
- A roundtable participant from the financial services sector found it key for regulators to **unlock some of the capital their sector is required to hold for regulatory purposes, and to allow them to invest more in research and development into solutions to the climate crisis**. Regulators in the financial services space are indeed closely engaged in dialogue and consultations with industry – which is crucial – but the increased ability for the sector to invest in climate solutions would help ensure they do their part in climate action.
- **Where businesses look to regulators to lead:** The cost implications of having solar panels installed, for instance, are not widely accepted by customers. Without regulation to force the construction industry to build to different standards and to enable them to pass on those costs, it becomes very difficult for businesses to deliver the green proposition.

## Case study



# US politics and democracy: Challenges to global stability

## Background

- As a major centre in the global security and economic architecture, the strength of America's public institutions and popular commitment to globalisation are key pillars of the system of international norms and protections that underwrite international trade.
- The US political landscape has been reshaped since Donald Trump's election in 2016. This year, the US midterm elections in November 2022 were keenly watched for indications as to how the even more critical 2024 presidential election would shape up. US voters have tended to punish the party of the president at midterm elections – in this case, Democrats – so there were fears it would put Donald Trump in a good position to run again in 2024 on the Republican ticket.
- While Democrats lost the House of Representatives, they performed better than expected, not least in retaining control of the Senate. Republican candidates who were personally endorsed by Donald Trump performed badly, which will dent the former president's chances in the Republican primaries

for the 2024 presidential election in favour of Ron DeSantis, the Republican governor of Florida and rising star of the party.

- US politics remains highly polarised, with the continued propensity for political violence as unleashed in the attack on the US Capitol on 6 January 2021, as well as dysfunction in policy-making due to more fragmentation and antagonism inside the major political parties.
- That said, Democrats and Republicans are in agreement on one major foreign policy issue: the US's relationship with China. Protectionist trade policies are becoming increasingly entrenched within both parties.

## The views and concerns of political observers

- **While the latest midterm elections did bring potential risks for businesses, they were mostly indirect ones.** For instance, Democrats had been accusing their Republican rivals of being a threat to US democracy, but that had been a line intended more for a domestic audience, rather than to cause panic around the world – although it did to some degree achieve the latter.

Rather, political observers were more concerned about the implications of the midterm election results for the 2024 presidential election and about issues of democratic legitimacy in the US more generally.

- **Protectionist policies are now fairly entrenched in both major political parties.** Questions are being asked as to what that is doing to America's brand around the world – for businesses looking to invest in the US, and for US allies who are increasingly jittery about rising geopolitical tensions and unsure of the US's commitment to providing a stabilising presence in key regions.
- **There was concern about any one party winning a landslide at the midterm elections and unleashing another round of 'impeachment theatre'.** The last two years of Donald Trump's presidency saw a lot of political theatre with attempts to impeach the president, whose position was relatively safe because of a lack of power to remove him from office. The impeachment of a president requires a high bar of a supermajority of two-thirds of the US Senate.

## Mid-term scenarios for the US

### Domestically:

- **Political violence.** While unlikely to be on a large scale, there could yet be incidents of political violence like the 6 January 2021 attack on the US Capitol, as US politics continues to take a more populist slant.
- **Businesses may be increasingly forced to take sides.** Companies increasingly are taking sides on political positions such as abortion or ESG regulations – and by doing so, they will increasingly become targets of lawmakers and activist consumers.
- **Divergences on strategic issues and policies that matter to corporate strategy.** As US politics becomes more polarised, the divergence on important policy areas between the states in the US will grow. For instance, states such as Texas and Florida have passed anti-ESG legislation which penalises

businesses for adopting ESG principles in their investment decision-making. There are more states with similar legislation in the works. These developments will matter to business strategy, rather than just business operations.

### On the international front:

- **There is bipartisan agreement in the US on what to do about China and on related aspects of industrial policy such as the decoupling of supply chains.** There is a sense that despite all the polarisation in US politics, the country has generally always pulled together on foreign policy and where its interests abroad matter. This is most clearly seen in how China is the one significant issue on which Democrats and Republicans can agree, amid their regular acrimony. The US's current policy on China means we are likely to see the US working more closely with its other international partners at China's expense. For instance, the **Trade and Technology Council (TTC)** was set up between the US and the EU in 2021 to deepen cooperation, facilitate trade and develop global standards on technology and security. The US would also be keen to engage more deeply with key Asian allies such as Japan and South Korea.
- **The US's relations with the UK.** The Biden administration has been reluctant to start negotiations on a free trade agreement with the UK post-Brexit, as was made clear in former UK Prime Minister Liz Truss's first meeting with the president in September 2022. While there are actors in Washington who are keen on a free trade agreement, not least with the impetus for reshoring critical industries to friendly countries, the Biden administration and the US Congress see the issues around Northern Ireland's status as a problem. The US was a broker to the Good Friday Agreement of 1998, which was designed to end decades of violent conflict in Northern Ireland, and the US's large Irish-American community means it continues to take an active interest. It is also becoming clear that the US is more interested in striking a trade agreement with the EU, which presents a larger market to them than the UK.

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**US foreign policy: The long-term view**

*The US has torn itself apart at moments throughout history over domestic issues, such as during the Civil War on the issue of slavery. But when push comes to shove on major international issues or global crises, the parties in the US somehow rally together. So, I think it's important to keep a long arc on some of these issues.*

*Political Analyst D*

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**Where the UK and US have worked well together**

*The UK still has a stronger partner in the US, in political and security terms. With initiatives such as AUKUS, the security pact between Australia, the UK and the US, the UK has worked hard to bind a lot of the other Pacific alliances over even in the chaotic post-Brexit era. On the economic front – on issues such as the decoupling of semiconductor supply chains from China, these are areas where the US's and the UK's economic interests align, and hence are more likely to gain traction than in trying to do a trade agreement.”*

*Political Analyst D*

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**Views of businesses**

Even where they may not be directly impacted in their roles by political polarisation in the US, risk and internal audit professionals have conveyed their concerns over how global instability will not be well served by a US that is domestically unstable. When posed with challenges from alternative political and economic models, and in view of a US that is perceived to be withdrawing from its role since the end of the Cold War as the ‘world's policeman’, organisations are most concerned about the resultant volatility and uncertainty for economies around the world.

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**The challenge from alternative political and economic models**

*Western societies have been underpinned by the principles of democracy for a long time. But if that faith in democracy starts to erode, alternative political and economic models might come along. The resultant volatility and uncertainty wouldn't be the best thing for economies.*

*Chief Internal Auditor, Financial Services Firm*

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## Case study



# Cyber security and geopolitics

## Background

- After Russia's invasion of Ukraine in February 2022, cyber risk for most organisations increased, especially for those related to critical national infrastructure. This may well be a short-term assessment, but as the conflict in Ukraine continues and as Russia looks to realign its cyber focus – which has been operational since the start of its war – the threat could stay at the current heightened level for some time.
- In the physical domain, Russia has potentially leveraged its capabilities to hit critical national infrastructure in Eastern Europe and the Baltic states. Russia certainly demonstrated its potency and capability in targeting critical national infrastructure at the start of the Ukraine war, when it hacked the US satellite company Viasat, causing significant loss of communication in the earliest days of the war for Ukraine's military.<sup>12</sup>
- For most organisations, there is a slightly increased indirect cyber risk through the targeting of Western states such as the US, the UK, France and Germany, including cyber-attacks against key suppliers, third parties, and energy and communications providers. The targeting of organisations supporting Ukraine is sometimes intended as a signalling impact.
- There has generally been an increase in cyber-crime threats as well in Europe and the US, as cyber-criminal groups – which may or may not have linkages to Russia – change their modus operandi to increasingly target energy infrastructure, be that oil and gas terminals or infrastructure for renewable energy.
- The **cyber threat in Asia-Pacific** is not as acute despite US-China tensions over issues such as Taiwan. Nevertheless, there is a growing cyber threat to organisations which have a presence in Taiwan, even if it is not as disruptive as that relating to the Ukraine crisis.

12. <https://www.technologyreview.com/2022/05/10/1051973/russia-hack-viasat-satellite-ukraine-invasion/>

## Who are these hacking groups?

While driven by financial gain through collecting ransoms, these hacking groups do tend to be aligned to a state which ensures that their infrastructure and operations are maintained. In some cases, it has been a more systematic kind of collaboration with a state.

## What risk and internal audit professionals did in the early days of the invasion of Ukraine

- For risk and internal audit professionals around the world, there was a critical need first to map out where the organisation's key cyber assets lay, and what its operations in Ukraine and Russia were like – and then consider what the drivers and external factors were that would impact those assets. Of course, those risk and internal audit professionals in Ukraine, out of necessity, responded in different ways. The closer you are and the more you are impacted by the risk, the more dynamic the role of internal audit and risk becomes.
- The next step was to undertake strategic scenario planning while tapping on intelligence techniques to better understand different scenarios – the best-case or worst-case baseline scenarios – with a view to identifying the more operational side of cyber risk as related to geopolitics. For instance, questions that were being asked included: What threat indicators and warnings should we be looking for in a given region or country? How do we know if we are getting closer to that worst-case scenario?
- **Plausibility-based scenario planning:** They would also monitor online discourse – for example, publications such as news articles or intelligence reports – for any indications that they were approaching a worst-case scenario.

## Other cyber risks

- **Systemic internet failure.** The sabotage of the Nord Stream gas pipelines under the Baltic sea in September 2022, blamed on Russia, sparked off discussion as to whether countries and organisations were prepared for a potential targeting of undersea internet cables, which would lead to a systemic internet outage. Already in 2017, the former GCHQ director Robert Hannigan warned: “In hybrid warfare you could tweak the UK economy, even without bringing it to its knees, by just cutting a few [fibre-optic undersea cables].”<sup>13</sup> That threat has been on the UK's National Risk Register for a number of years as a potential risk for UK infrastructure, but the security of these undersea cables continues to be an underinvested area.
- **The vulnerability of the smart aspects of industrial systems in the maritime sector.** As ships are increasingly equipped with complex automated systems that are connected to the internet, they also face new threats to their cyber security which have made them vulnerable to cyber-attacks.<sup>14</sup> There are cases, for instance, where the navigation systems of ships have been tampered with, placing the vessel in territorial waters where they are not meant to be.

13. <https://www.thetimes.co.uk/article/economy-vulnerable-to-russian-attack-on-undersea-cable-links-rqqf0fxj8>

14. <https://www.mdpi.com/2673-8732/2/1/9>

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**Cyber: Preparing for a perpetually high risk**

*We have seen some increase in terms of cyber-attacks, but in a company as large as ours, we look at millions of potential attacks [all the time]. So, it's very difficult to say that we have seen a very significant increase as a result of the Ukraine crisis. In most of these attacks, we don't know the origins of the hackers, so it's very difficult to say which states they are linked to. So in that respect, cyber continues to be a very high risk before and after the Ukraine crisis.*

*Group Audit Director, Telco*

*Cyber is what we're all about, and protecting the cyber infrastructure is what we're all about. So it's not an emerging risk, nor an increased risk. We get millions of attacks that we stop every single day. In terms of what escalates into something that actually causes damage – no, we haven't seen much of an uptick in actual impact since the Ukraine crisis. Look, if you don't put locks on your doors, what do you expect?*

*Head of insurance, Technology company*

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