Why risk managers must take stock of their firms' geopolitical impact

By David Claridge, CEO of Dragonfly | 1 June 2023

David Claridge, CEO of Dragonfly, explores why companies may be unwitting political actors and how risk managers can deal with the exposures this creates

With increasingly dominant stakes and visibility in often unstable emerging and frontier markets, large multinationals need to recognise that they may be active players in geopolitical conflicts, not merely passive observers.

Global companies risk incurring substantial operational and reputational costs unless they give serious thought to how their economic and social footprint might cause this to happen – even if they regard themselves as disinterested parties.

Multinationals are more exposed to such entanglements than in the past because their activities are exposed to greater scrutiny from local activists and international advocacy groups, who are increasingly adept at deploying social media to amplify their causes.

Whether well-founded or not, claims that a company is fuelling a situation can leave it open to further embroilment as it seeks to adjust its messaging, as well as leaving staff, physical assets and supply chains vulnerable to security threats.

Why sector matters

Broadly speaking, multinational companies' engagement in - and exposure to - geopolitics varies according to their sector and lines of business.

Defence and aerospace firms are, by their nature, effectively extensions of their home governments' foreign policy objectives. They largely operate within a highly regulated approval and engagement framework, and by their nature, their products directly shape the geopolitical context.

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Extractive and manufacturing industries have the potential to sow the seeds of dispute by disrupting and distorting economic and social stability, often over the long term.

Tech firms whose platforms are more likely to be exploited to stoke tensions, and global retailers whose brand messaging may lead to them being perceived as partisan, are often the more visible faces of business engagement in geopolitical risk.

How to measure the risk

International companies may routinely conduct political risk assessments when moving into new markets to better understand how the policies of current and future governments are likely to impact their business operations. These are, essentially, relatively well-understood risks.

But the task of assessing the more complex and less predictable impact of a company's activities on regional political and security dynamics is now also business-critical, given the potential operational and reputational threats.

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In recent years, Chinese hackers launched cyberattacks on European companies involved in energy projects in the disputed South China Sea, and anti-Beijing Hong Kong protesters damaged the premises of local franchises of global brands deemed sympathetic to China.

At the outbreak of the Ukraine war, tech giants came under pressure in the US and Europe for not doing enough to stem Russian misinformation. And defence contractors have faced censure from human rights organisations for allegedly supporting Saudi Arabia's military campaign in Yemen.

Mitigation tactics

To mitigate such operational and reputational risks, [the risk managers of] multi-nationals need to begin by asking themselves whether they might be considered a player in an existing or emerging geopolitical conflict.

Key to this is an evaluation of whether their presence or actions may, inadvertently or not, contribute to raising tensions.

Such consideration should extend to business connections, such as franchisees and other commercial partners.

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For instance, companies might become embroiled in a geopolitical dispute indirectly through their supply chains, particularly as they diversify them in Asia in the wake of the pandemic and given the continuing trade war between the US and China.

Indeed, firms shifting at least some of their production from China to Southeast Asia risk entering jurisdictions subject to growing geopolitical rivalry between Beijing and Washington.

Indonesian President Joko Widodo recently urged other ASEAN nations not to allow the tensions to turn into a "new Cold War" in the region.

Don't forget supply chains

It is also important for companies to determine how instability in a country of operation could set off a chain reaction, with spillover possibly undermining access to key supply chain nodes across a whole region.

The Sudanese civil war has forced tens of thousands to flee across the country's borders, creating a humanitarian emergency that could undermine regional security and trade. The Venezuelan socio-economic crisis and the Syrian civil war similarly triggered the mass exodus of civilians, destabilising neighbouring countries.

Robust assessment of their possible geopolitical impact and chain-reaction risks should help inform and shape scenario planning and mitigation strategies.

These may include plans to downscale or relocate in a volatile jurisdiction in order to reduce the risk of being implicated in security crises; interrogating the geopolitical orientation and sympathies of local partners; and enhanced monitoring of regions of operation.

Know your position

But critically, when companies find themselves operating in the midst of a regional conflict, they need to be able to explain or defend their position.

Maintaining neutrality or refusing to comment is not an option, as it may raise suspicions among local communities and draw negative international headlines that are highly likely to influence consumers and investors.

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For example, Western companies with significant operations in Russia were called out in mainstream and business media for their silence on Moscow's invasion of Ukraine, based on research by the campaign group the Moral Rating Agency. Whether they like it or not, businesses are already geopolitical actors.

As companies devote more attention to geopolitical risk, the possibility of being seen as geopolitical actors themselves may not have been considered or anticipated.

Assessing whether they are, requires different risk calculations to the ones they are accustomed to making, but evidence increasingly suggests that such assessments have clear strategic value.

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