

Navigating the New Realities of

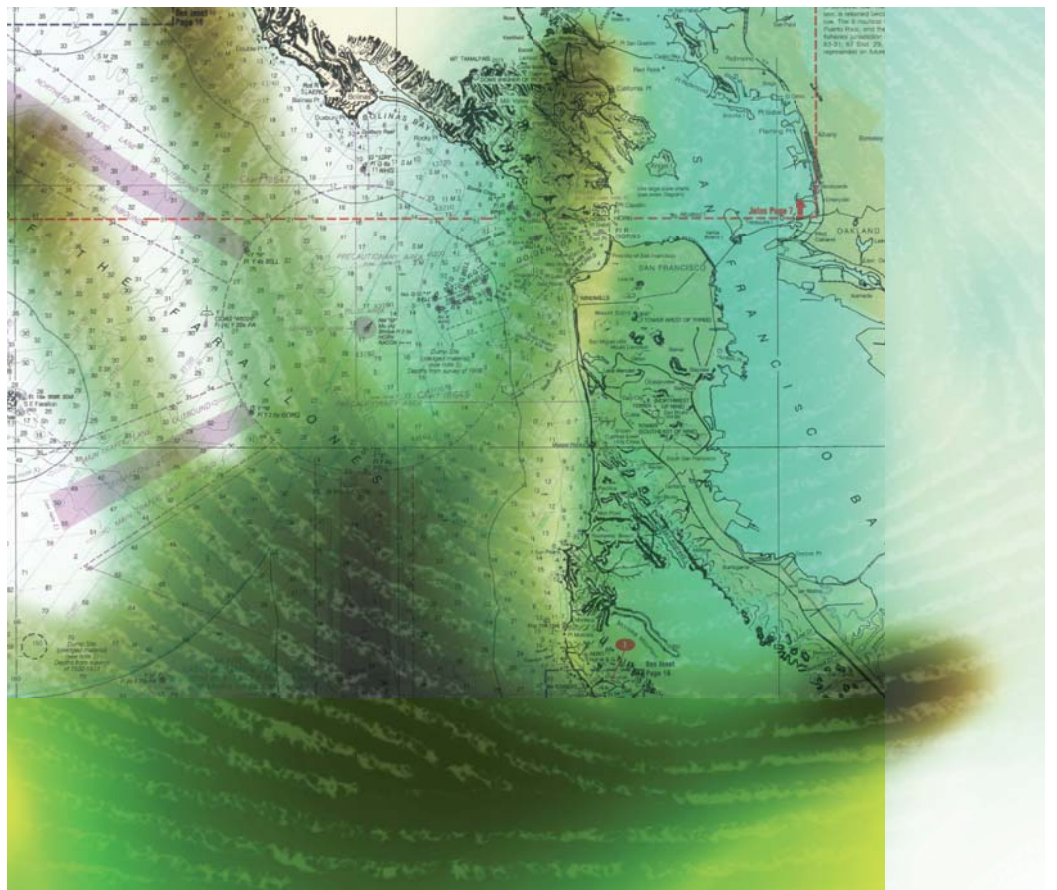
# RISK

A GBN WorldView Meeting Report

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# THE LANDSCAPE OF RISK

GBN's Annual Forum, directed by Lawrence Wilkinson and Rebecca Wayland, began with a look at the changing context of risk and uncertainties.

"The moment that you think that risk management is about answers, you are trapped."

— Enrique Rueda-Sabter,  
World Bank

CEO Eamonn Kelly provided a dynamic kickoff on Monday evening at the Yerba Buena Center for the Arts Theatre with a multimedia presentation that explored the major themes of his recently published book, *Powerful Times: Rising to the Challenge of Our Uncertain World* (Wharton School Publishing, October 2005). "The times are more powerful than our brains," Kelly asserted. In his presentation, he wove together the powerful "dynamic tensions" that will fundamentally reshape human life in the coming decades, exploring how these dynamics might interact to create different future scenarios, as well as new risks. Understanding (and taking advantage of) these forces requires us to let go of many long-held assumptions about how the world works, he said, while also adopting a "both/and" rather than an "either/or" approach to thinking about change.

A counterpoint to this idea was the quote that began Tuesday morning's session. As Peter Bernstein said in his landmark book about risk, *Against the Gods*, "The revolutionary idea that defines the boundary between modern times and the past is the mastery of risk: the notion that the future is more than a whim of the gods and that men and women are not passive before nature." The Code of Hammurabi was one of the first documented records of insurance, still a powerful risk-mitigation strategy. The first official insurance policy was written by Italian merchants in Genoa in 1347 to protect against the risks of global exploration and trade. Some of the noble families of Genoa made a great deal of money from these policies, proof of the opportunities that risk can create.

For the purposes of Forum, Wilkinson and Wayland defined risk as "an uncertainty that matters," with these characteristics:

- Risk has both upside and downside
- It has both known and unknown uncertainties
- It is linked with potential changes in existing systems

Throughout the next three days, Forum participants explored the emerging landscape of risk through a series of panels, conversations, and experiential learning exercises. The sessions used a holistic, outside-in perspective that was grounded in the real-world realities of interrelated risks. The goal was to develop navigational tools and approaches; a contextual framework for management decisions and tradeoffs; and the first steps toward an integrated and portfolio-based approach to risk.



We would learn that risk is not just about being passive before nature. It's fundamentally about making decisions and making choices. Risk is also a complex process that involves both knowledge and judgment. Thinking about risk as an uncertainty that matters takes us away from thinking of risk only in a defensive posture. It allows us to see that risk presents us with both an upside and a downside, because an uncertainty, as we know, can unfold any number of ways. And there's a role for action in that context, linked with potential changes in existing systems.

### Levels of Risk

Traditional discussions of risk mostly deal with its quantitative side: hedging strategies, portfolio-based approaches, and the like. Within organizations, "risk management" covers a wide range of specialized areas, including risks caused by technology, business models, credit markets, intellectual property, supply chains, and legal and compliance issues.

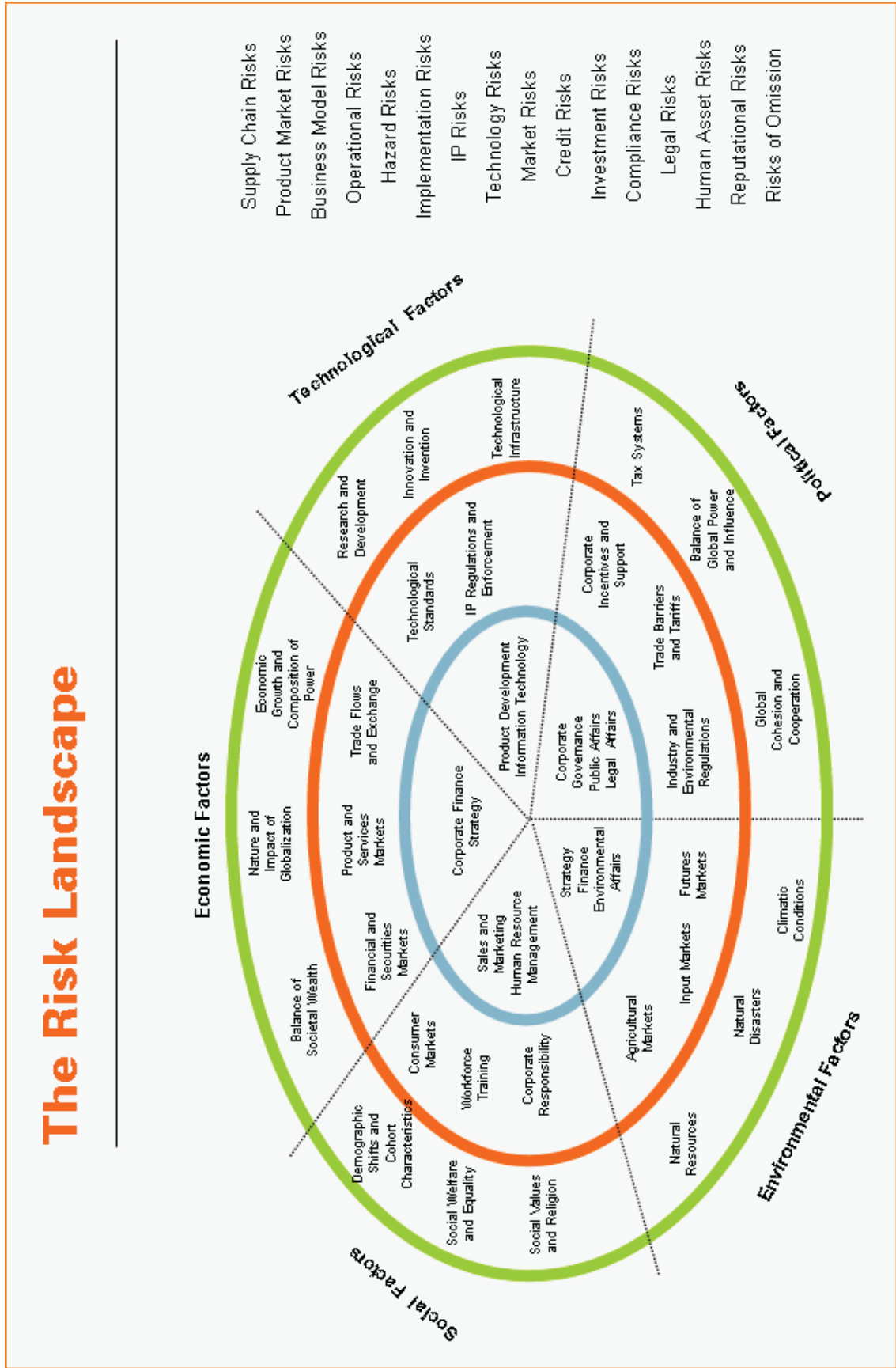
Rather than take this approach, we looked across all of these dimensions to try to understand how risks emerge from the environment and the different ways in which they might manifest themselves and interrelate. To do this, we used an outside-in framework that mapped the economic, technological, political, environmental, and social forces impacting our companies at three levels of the environment: external, market, and organizational (see Figure 1, "The Risk Landscape").

**RISK - EXTERNAL ENVIRONMENT - QUESTIONS & ANSWERS**

- Techniques Embrace Uses**
  - Use the FRAMEWORK as scaffolding... be willing to dismantle it.
  - DIVERSITY in the CONVERSATION.
  - MIX of objective & subjective
  - BE EXPLICIT IN CONVERSATIONS.
  - TECHNIQUES DENISE USES
    - drill down with analysts themselves
- CHALLENGE**
  - HIDDEN ASSUMPTIONS
  - ask the Oracle...
    - visit a positive future
    - visit a negative future
    - an indirect tool to get ACT hidden assumptions.
- How to make sure it doesn't become a RISK ADVERSE CULTURE?**
  - TOPGUN False bravado!!
    - Superb planning
    - Ability to cope
- Strategies for getting people to TAKE RESPONSIBILITY**
  - IT DEPENDS
    - A continuity person in the org.
    - Two Step Process
      1. Management team OWNS the risk.
      2. Someone is assigned the remedial action.
- When to STOP discussing and START acting?**
  - Analysis by analysis
  - Assign someone
  - A resource function
    - TIME - MONEY - PEOPLE
  - A VERY PRACTICAL QUESTION
- Strategies... when Sr. Mgmt is leaving (looking toward retirement)?**
  - with personnel issues?
    - The person at the TOP needs to be a CONTINUITY person.
    - Got to consider TOP person's personal long-term goals
- QUALITATIVE DIFFERENCES**
  - how to COMMUNICATE in ways it will STICK
    - Good storytelling. Suspension of disbelief.
    - Communicate as MUCH as POSSIBLE
    - INCENTIVES !!
      - REWARD
      - DANGER
      - Emphasize the search for the intangible asset.
    - how to MAINTAIN the BALANCE?
      - REWARD
      - DANGER
      - Just can't POSSIBLY happen.
      - My idea of a beach is...
      - My idea of a beach is NOT what mine is.
- how to MAINTAIN the BALANCE?**
  - Create an opportunity for a conversation by both sides.
  - Create a common framework the proportions risk appropriately.

**Figure 1 The Risk Landscape**

Forces impact our companies at three levels: external, market, and organizational. Within each ring of the "bull's eye" are specific technological, economic, environmental, political, and societal factors that come into play at each level of the environment.



The outer ring of the framework is the external environment of contextual risks and systemic crises that could occur at the level of technology, economics, the environment, politics, and society. The middle ring is the market environment, where we see competitive, legal, and transactional risks; industry and competitive dynamics; supply and demand; and the rules that govern exchange. The center of the bull's eye is the organization, where we have strategy, operations, and procedures that are in place to manage the organization. That's where the heart of decision-making occurs.

Of course, all these areas interrelate, as the scenario of China's rise illustrates (see Figure 2, "The Potential Impact of the Growth of China"). Here we see rapid economic growth, a shift in the balance of wealth, and major technological and infrastructural developments. We also see a number of cascading effects: demographic shifts; changes in social equality, values, and religion; shifts among global economic players and financial markets; and broad changes in consumer markets. In developing a market strategy, for example, it would be important to understand the broad and wide-ranging effects of something like the growth of China.

To begin our own explorations of risk, we worked in small groups to populate the bull's-eye framework, with Post-it notes representing the existing and emerging risks each of us face in doing business. These risks clustered heavily in the outer rings, and especially in the social and economic areas of the external environment (see Figure 3, "Mapping Uncertainties and Risks," page 7). Another significant concentration appeared in the innermost ring of the organizational environment. Interestingly, hardly anyone pointed to environmental risks, perhaps because they are thought of as areas we can't control or that government will somehow handle.

### **Risk in the External Environment**

After taking the pulse of Forum participants, we moved on to a panel discussion featuring Denise Caruso, GBN Network member and founder/executive director of the Hybrid Vigor Institute; Enrique Rueda-Sabter, director of strategy and integrated risk management at the World Bank; and Peter Schwartz, cofounder and chair of GBN. The goal was to push the group's thinking about the dynamics at play in the current environment, particularly those that are most uncertain and present us with risks.

In thinking about these issues, it is helpful to be both systematic and imaginative, said Schwartz. On the systematic side, he organized his discussion of "apparent risks" around the simple framework GBN uses called STEEP: social, technological, economic, environmental, and political. In each category, we face specific risks in the external environment, said Schwartz. He speculated that the most important risks in the coming five to 10 years include:

- **Social.** The consequences of immigration for diversity in societies. The U.S. has seen huge immigration most recently from Asia and Latin America. Look for huge tensions over immigration to emerge in Europe and Russia as their populations decline.
- **Technological.** "There is a misperception that somehow technology is going to slow down," said Schwartz. "There is no hint, in my view, that it is going to slow down in any way. It's continuing to accelerate, though there is resistance to it."

# The Potential Impact of the Growth of China

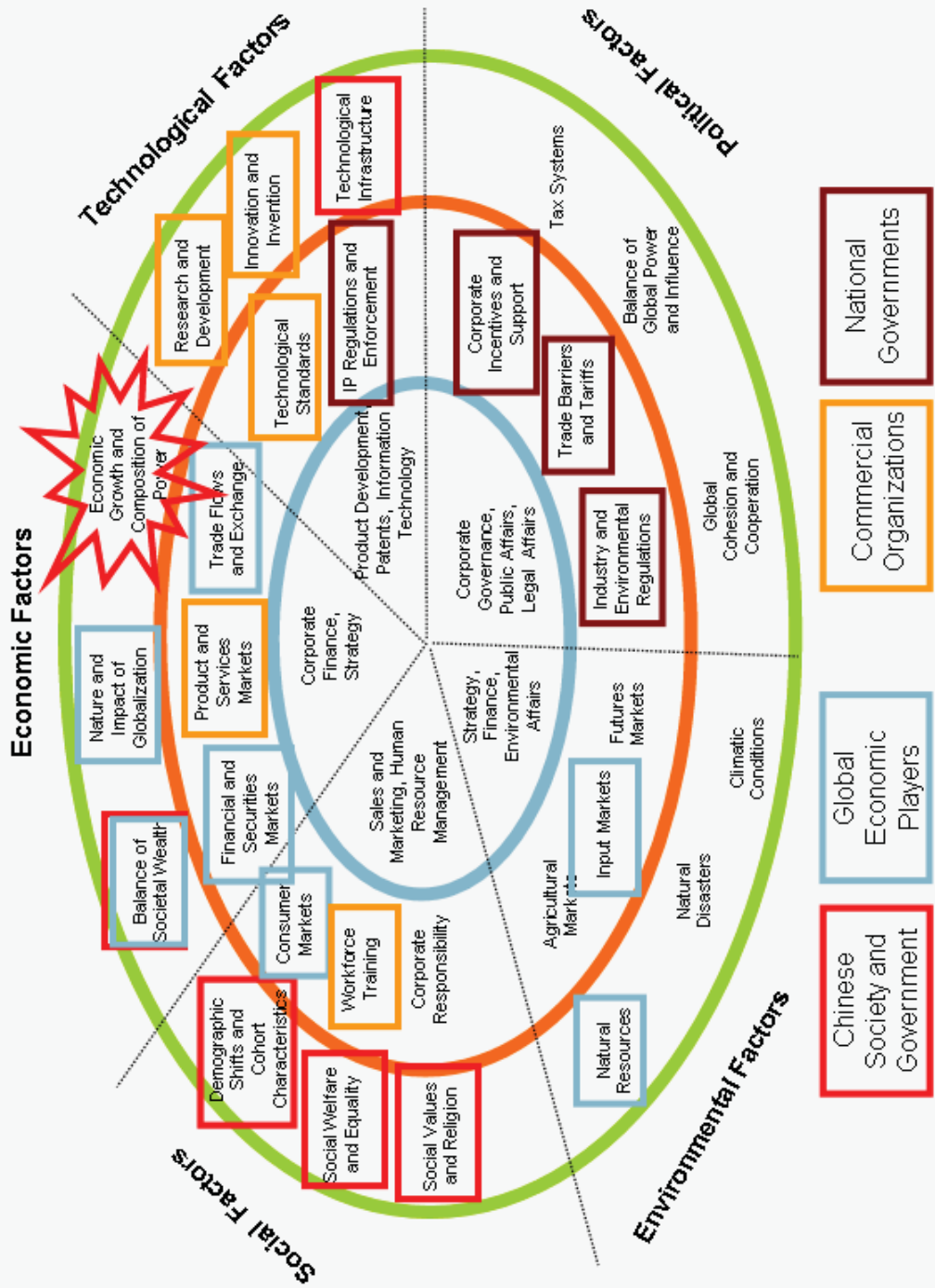


Figure 2 The Potential Impact of the Growth of China.



### THE FATE OF HUMANKIND

Peter Schwartz raised four questions that he thinks will determine the fate of humankind over the next 50 years, and perhaps the next century:

- Do we face a major conflict, either between China and the U.S. or between the West and Islam?
- Are we able to sustain economic growth and raise the wealth of the world?
- Will that wealth be relatively well distributed or highly concentrated?
- Can we make the next 2 billion people rich without destroying the world's environment?

"If the answer is yes to all four of those questions, it's going to be a happy world in 50 years," he said. "And if the answer is no to any one of the four questions, it's going to be a miserable world in 50 years."

- **Economic.** The risk of 1970s-style stagflation is very real in the world's major economies, and could be driven by high energy prices and slowing economies. A related risk comes from the rise of protectionism. "When we talk to our clients, they're interested in five countries: China, China, China, China, and India, in that order," he said. "It's almost impossible to have a conversation with business about what's going on in the world without beginning with China."
- **Environment.** The most obvious risk is climate change, which is already having global implications. "I think the issues of energy have become very much on people's minds," he said, "not just because of pricing, but because of climate change and the arguments that are being put forward about peak oil."
- **Political.** Schwartz pointed to two huge risks: the potential for new rivalries, particularly between the U.S. and China, and the rise of a bloc of countries interested in impeding the spread of U.S. power in Latin America. "Nobody likes the biggest guy on the block, so everybody lines up against the U.S. in coalitions of denial," said Schwartz. "We are now in a position where containment is aimed at us. The question is, will we get a hegemonic group of countries, led by China, attempting to block our hegemony?"

### Emergent Risks

Caruso shifted the discussion to "emergent risks"—risks for which we haven't yet worked out the full dimensions and for which we don't even have proper vocabularies. "How risk is generally evaluated now inside of organizations is very much quantitative: What can you count? What can you measure?" she said. "One complaint about quantitative risk analysis is that often people make up numbers or pretend like numbers are important when they're actually not, just because that's the only way you can sell a risk to your board."

She said that increasingly with new technologies there is no good data to predict risk, precisely because we have such limited experience with these technologies. Moreover, we know from the history of science and technology that surprises are inevitable, and that there will always be unintended consequences. "No one talks about what happens outside the frame," she said. "And what's outside the frame is very often, maybe even always, where the unintended consequences are going to come from."

Ultimately what's needed is to look at the qualitative issues that most people miss when they look through the "spyglass" of quantitative analysis. Caruso recommended a methodology from the National Academy of Science, published in *Understanding Risk: Informing Decisions in a Democratic Society*, in which the best risk scholars opened up the conversation to the stakeholders in an organization. "It's very powerful to bring into the conversation the appropriate people in the appropriate numbers, to have a conversation where you bring in as much data as is relevant to the problem but also bring in people who have a different perspective," she said. "People are very accustomed in risk analysis to one person making the decision. In order to change that, you have to change a culture and to believe that it's actually useful to have more people make that decision." She

also recommended communicating as much as possible about the assumptions behind decisions: what data was and was not available; what could we analyze; and what did we assume about the future?

## The Organizational Level

Rueda-Sabter then brought the conversation down to the level of the organization, from his perspective at the World Bank. His organization defines risk as “anything that is a threat to our ability to deliver on our mission,” he said. “Our mission is poverty reduction, so that’s a pretty huge thing.”

For any organization to effectively navigate risk, the key is to ask lively questions, Rueda-Sabter noted. “The moment that you think that risk management is about answers, you are trapped. Scenarios then become a way that you keep asking questions and you force people to answer questions that they don’t normally want asked.” He cautioned against thinking of risk management as “risk avoidance.” Then your risk is one of missed opportunities, of not deliberately taking risks. He outlined several “focal areas” for risk management, which he defined as things the World Bank must ensure that it does properly:

### FOUR QUESTIONS THAT SURFACE HIDDEN ASSUMPTIONS

- You’re visiting an oracle. What would you like to know from the oracle?
- What’s your positive future?
- What’s your negative future?
- What’s your legacy?

- Strategic effectiveness. Are we doing the right thing? Are we being alert to changes in our external environment?
- Operational effectiveness. Are we including a wide range of stakeholders in the discussion?
- Stakeholder support. How can we lose it or gain it? “Who is going to hate this project? An honest answer to that simple question would have saved us from some of the worst messes we have gotten ourselves into,” he said.
- Financial soundness. Are we overcautious? And are we over-investing in risk management? “There is a huge danger of over-investing in risk management on financial kinds of things, because it’s easy to do them,” he said. “You have models and you get enamored with the clever techniques behind the models.”

He also laid out several traps that he worries about. One was Stalinism: “We just have to keep thinking about the five-year plans and delivering the things in the plan—but maybe that’s not what counted,” he said. Another was “reductionism,” as seen in the sophisticated thinking by financial institutions about segmenting what they call “expected and unexpected losses.” But, he noted, “the moment you allow that in your mind, that you think you know what the expected losses are, and just need to worry about the unexpected, you fall into a major trap. This is true particularly when you realize that the expected losses come from a very simplistic analysis of means and of precedents that may not be relevant, and from looking in your rearview mirror while you are trying to look ahead.”

Rueda-Sabter concluded by warning against the “framework as straightjacket.” He explained that “yes, we need frameworks, and we need to be systematic and imaginative, but we also have to be conscious that once we develop a very nice framework, it becomes a very nice trap.” What’s necessary is to align incentives with the long-term roots of positive outcomes, and to move beyond the quantitative by emphasizing the search for intangible assets.

# VENTURING OUT INTO THE WORLD

In the afternoon, we took to the streets of San Francisco and Oakland to see some of the issues we had been discussing at play in the world. Participants had a choice of seven Learning Journeys, each of which added detail and example to our conversations about the ways in which organizations identify, anticipate, and manage against both current and future risks.

The U.S. is spending a lot of time focusing on threats that are coming into ports, but not on dangerous materials that could be going out.

—Port of Oakland Learning Journey

## Learning Journey 1: The Federal Reserve Bank of San Francisco

Participants visited the San Francisco branch of the system of 12 regional Federal Reserve Banks across the U.S. that, together with the Board of Governors in Washington, D.C., serves as the nation's central bank. The Fed's mission is to "foster the stability, integrity, and efficiency of the U.S. monetary, financial, and payment systems in order to promote optimal macroeconomic performance." By definition, the Fed worries about risks to an incredibly complex economic system that affects billions of people around the world.

### Key Takeaways

We got the sense that the Fed thinks it has engineered dangers away, and may not be fully aware of the true risks to the monetary system. It has an enormous structure and many researchers tracking risk, but it all comes down to tinkering with one rate adjustment. The solutions seem out of scale to the risks being managed. On the other hand, it was encouraging to see that the analysts not only look at the data but have institutionalized informal, anecdotal monthly meetings to share perceptions and early indicators of change.

**Hosts: Paul Dillard, senior examiner; Jack Richards, community affairs manager; Gary Zimmerman, senior economist; Peter Schwartz, GBN**

## Learning Journey 2: Port of Oakland and Embarcadero Systems

One of the most talked-about risks facing the global economy is the threat of a terrorist attack via container ship. Participants visited one of the busiest ports in the United States to hear how it thinks about managing this critical risk to major cities and the global flow of goods. We heard from Embarcadero Systems, which provides the port with IT and surveillance security services.

### Key Takeaways

When we heard just how disorganized things are at the Port of Oakland, it gave us pause. We learned that the U.S. is spending a lot of time focusing on threats that are coming into the port, but not on dangerous materials that could be going out, or on sufficiently checking the backgrounds of those who drive in

and out each day. We are therefore highly vulnerable to an attack from a group that exploits these weaknesses in the transport system. Government could take a better coordinating role in managing risk.

**Hosts: Keith Dierkx, SVP, Embarcadero Systems; Ian Mitroff (Network), UCS Center for Crisis Management**

### **Learning Journey 3: DNA Direct**

This web-based company allows consumers to test their predisposition to a number of diseases like cancer and heart disease, learn to modify their risk factors, and get advice on sharing genetic risk information with relatives and medical professionals without the person's records entering the healthcare system. This new service raised both personal and privacy risks.

#### **Key Takeaways**

The journey explored the personal risk of learning your predispositions to disease (and the importance of offering and packaging that information in a relevant and customized context). We also focused on the (largely downside) privacy risks associated with employers and insurance companies obtaining such information, although IBM's recent announcement of an anti-discriminatory policy on genetic predispositions is an encouraging development. Network member Joel Garreau concluded the journey with a provocative story about medical information affecting a business partnership and the role of reciprocity in managing this new knowledge.

**Hosts: Ryan Phelan, cofounder; Joel Garreau, Network member and author of *Radical Evolution***

### **Learning Journey 4: U.C. Berkeley School of Public Health**

In 2002, the U.C. Berkeley School of Public Health initiated a Center for Infectious Disease Preparedness, with courses designed to prepare students to work with such public health threats as bioterrorism and infectious disease emergencies. This journey explored the threat of pandemic posed by the avian flu virus, and what that means for business.

#### **Key Takeaways**

Avian flu is a real threat. Although the H5NI virus has infected millions of birds, sustained human-to-human transmission has not yet occurred. If it does, that relatively small mutation could rapidly trigger a pandemic. At present, there are no effective vaccines and insufficient antivirals to prevent or slow the spread of avian flu. Moreover, only about half of all companies, and even fewer countries, have plans in place. Significant work remains to be done to monitor outbreaks, change lifestyles in countries with close contact to birds, and realistically assess and plan for the magnitude and cascading social and economic consequences of a pandemic. Most experts now believe that a pandemic is almost 100 percent likely to occur; the real question is when.

**Hosts: Dr. Arthur Rheingold, professor and head of epidemiology, BSPH; Larry Brilliant, epidemiologist, technologist, philanthropist, and GBN Network member**

**HOW SPECIES FIND OPPORTUNITY IN RISK**

By Peter Warshall, co-leader of the Crissy Field Learning Journey

- Avoid and then come back. An individual can die and come back through a seed; change place by migrating; or reproduce or metamorphose into a new form.
- Develop resistance and/or resilience. A great opportunity is a partnership that can withstand risk (mutualism); for example, yeasts that process nutrients living with cordgrass to balance salt. Morph to risk is another opportunity, as in prostrate bushes on windy beaches.
- Develop attention to risk signals to reduce danger or increase opportunity, like the elephants that felt the rare event, the tsunami, rumbling in the earth and headed inland. Many creatures “get” risk by tasting, touching, or listening. These adaptations to receive and evaluate risk were once opportunities. It’s a feedback and feed forward loop.

Peter Warshall is a GBN Network member and consultant whose works centers on conservation and conservation-based development around the world.

**Learning Journey 5: Crissy Field, Golden Gate National Recreation Area**

Participants explored a 20-acre restored wetland located on a former airfield at the Presidio, an Army base that was converted into a national park. Through a look at the evolutionary history of the native plant life, we delved into the risks these organisms experienced and the opportunities they could or could not take in order to survive, in some cases, for more than 125 million years. We also explored the risks to companies that fail to take advantage of new trading opportunities in markets for carbon emissions and logging rights.

**Key Takeaways**

In nature, risk is always one level above and one level below the system you’re looking at. This lesson has applications for business, which should be aware of the sources of risk above and a level below them. Nature has many ways of mitigating risk, such as evolving multiple access points for pollination that are often highly targeted in shape and color to the insects that those plants want to attract. There is also huge undiscovered value on companies’ balance sheets in terms of their stewardship of the environment, such as through emission credits and conservation easements.

**Hosts: Peter Warshall, conservation and environmental consultant/advocate and GBN Network member; Adam Davis, ecological investor and founder, Solano Partners**

**Learning Journey 6: U.C. Berkeley Center of Integrated Nanomechanical Systems**

The center focuses on mechanics at the nanoscale level as one of six nanoscale science and engineering centers across the country funded by the National Science Foundation. This learning journey asked the questions: What is likely to happen when scientists successfully manipulate matter at the molecular level? Will it be a set of opportunities around breakthrough improvements in health-care, environmental sensing, and manufacturing? Or are we actually looking at the risks of toxicity in human beings and other living things, or of biological weapons that can be easily concealed, or of the catastrophic “gray goo” scenario?

**Key Takeaways**

Nanotechnologies are slowly, but steadily, infiltrating the manufacturing of everyday products—from stain-resistant khakis to shinier paint. Just as boundaries between molecules are falling, so are boundaries between the academic and commercial worlds and between the different scientific disciplines. Nevertheless, we’ll need a continued stream of emissaries, diplomats, and joint-ventures to continue to bridge the gap between industry and academia. And if the U.S. intends to be a leader—or even just keep up with Asia—it will need to devote far more funding and investment to nanotechnology.

**Hosts: Jeff Grossman, executive director; Brian Sager, scientist and founder, Nanosolar, and GBN Network member**

## Learning Journey 7: YO! Youth Outlook

YO! Youth Outlook, part of Pacific News Service, is an award-winning literary journal that chronicles the life of youth ages 14 to 25 in the San Francisco Bay Area. From reporting interviews with gospel hip-hop bands to photo essays by homeless youth, YO! offers a unique window into California's youth subcultures. This journey looked at risk and opportunity at the intersection of ethnicity, generation, and media.

### Key Takeaways

This “newsroom of the global society” exemplifies humanity’s drive to communicate in order to avoid being alone and invisible. The half-dozen young reporters we met talked about risk as very personal: to their lives, to their reputation, for doing things differently. One surprise was their attitude toward ethnicity. In many ways, they were beyond ethnicity; all were such a mix that there were actually fewer differences. On the bull’s eye of risk and opportunity, inequality showed up solidly in the economic zone, inter-operability of communication tools appeared in the technology arena, and the human need to share registered in the social slice. Listening to their voices and understanding their reality was an opportunity for us.

**Hosts: Sandy Close, founder, and GBN Network member; Lawrence Wilkinson, GBN**



## RESPONDING TO RISK AND OPPORTUNITY

Moving in from the outer ring of the concentric circle, the second day of Forum delved deeper into the roles of markets and organizations in risk management. We began with a panel discussion with Ian Mitroff, professor of business policy and founder of the Center for Crisis Management at the University of Southern California Business School; Steve Tomlin, a venture capitalist at Avalon Ventures; and Cynthia Schmitt, vice president of enterprise risk management at Pitney Bowes.

“Proactive companies are substantially more profitable than reactive companies, and they live longer.”

—Ian Mitroff, USC

Mitroff has been studying organizations in crisis for years, and has mapped them into two types: proactive and reactive. Reactive organizations make up the vast majority and are generally unprepared for crises, he said. Proactive organizations, on the other hand, make up about 5 to 10 percent of companies, and prepare for crises much differently. Proactive organizations:

- Test assumptions. “There are methodologies for surfacing, challenging, critiquing, and replacing assumptions,” he said. “They’re not as widely known as they should be, because the half-life of assumptions is shorter than it’s ever been.”
- Do total crisis audits of the organization. Mitroff has grouped crises into 11 families. Proactive organizations prepare for at least one type of crisis in each of the families. “It doesn’t matter what the particular one is, because no crisis ever happens in reality as you have prepared,” he said. “But the important thing is organizations thought the unthinkable before it happened.”
- Don’t look at crises in isolation. “Every crisis is cause and effect,” he said. “A crisis sets off a chain reaction.”
- Integrate crisis management with total quality management. “Proactive companies use crisis management as a tool to improve the total performance of the organization and hence, justify the cost,” he said.
- Often have a chief crisis officer. They realize they need a different structure for handling crises than the one they have for normal business.
- Have a broad crisis portfolio. “Proactive companies don’t just put all their eggs into one basket and prepare for one kind of crisis,” he said. “They begin to prepare systemically. They have a trained crisis team that meets regularly.” The crisis team tends to include the head of the legal department, all the heads of the major business functions, and often the CEO.
- Learn from the past. “Proactive companies not only attempt to learn the lessons, but also to keep track of the lessons and attempt to instill them in the organization,” he said.



- Do pre-crisis trauma training. “Anybody who’s been through a crisis will tell you that the psychological impacts are so deep, it’s akin to somebody who’s hit with the fact that they have cancer,” he said. “The various stages that you go through, proactive organizations bring people through, and they do realistic simulations.”
- Pick up early warning signals. “Virtually all crises send out a trail of early warning signals,” he said. “Yes, there is tremendous noise, so the signal-to-noise ratio is critical. Proactive organizations filter through this blizzard of information, and they’re picking up these signals with regard to the chief assumptions that they’re making about the enterprise, the stakeholders, and all the parts.”

All of these factors are key to becoming a proactive, and ultimately adaptive organization, Mitroff said. And he has found that these efforts pay off: “Proactive companies are substantially more profitable than reactive companies, and they live longer.”

### **A Venture Capitalist’s View**

Shifting gears, Steve Tomlin explored the nature of risk at the market level, as seen from the perspective of a venture capitalist. His firm specializes in early-stage investments in biotech and wireless companies, operating at “the hairy edge of risk,” he said. “Venture capitalists are in the business of understanding risk, assessing where the big risk elements are—they’re in the risk-valuing business. Once you’ve made an investment, we then focus on how to manage or mitigate risk to enhance your return, as they’re both related.”

One big unmanageable risk that venture firms face is the fact that too much capital is now chasing too few investments. “If everybody thinks the same way, you have this herding instinct,” he said. “No matter how brilliant you are in managing your portfolio, when you’ve got eight companies all founded to do essentially the same thing, beating each other’s brains out over an emergent market, you’re going to have lousy returns.”

An element VCs can control is where they choose to invest along the spectrum from early- to late-stage investments. “As in the game of Texas Hold ’Em, where you’re given more cards and bet at periodic points in the process, an early-stage firm has to place its bets very early,” observed Steve. “Later-stage firms get to see more cards before they make their bets, but, presumably, the returns are smaller. When you control your entry point, you can choose the valuation at which you enter. That’s where we try to mitigate risk, as well, by going in very early.”

VCs also have more control over the industries in which they choose to focus their investments. His firm invests in early-stage wireless and biotech firms in the San Diego area, two industries in which San Diego excels. Ultimately, the biggest risk he sees is the “failure to innovate,” which can make you vulnerable in other ways.

## A Risk Manager's Perspective

Cynthia Schmitt then took things down to the organizational level, explaining how she navigates risk at Pitney Bowes. “We encourage each of the business units to be proactive in their own space and try to grow their businesses significantly,” she said. “But there was no one looking at it from a holistic point of view and saying, ‘Where are our real risks?’ And while we may have a significant risk in one business unit, it may not truly be an enterprise risk. We needed to understand our inherent risks in the business and what senior management didn’t yet know about.”

Schmitt puts risks on a timeline of what could impact the corporation in three timeframes: today, in 12 months, and in 18 months. But the framework is not so set in stone that it causes Pitney Bowes to miss out on opportunities. “The challenge for me has been to get people to change their behavior and start thinking, when they’re looking at opportunities in the business, what risk are they bringing into the corporation that we may need to have pieces in place to mitigate?” she said. “Or the interdependencies: if one business unit makes an acquisition in one area, what implications does it have for someplace else?”

“I’ve been very careful to make sure control is not in anything I say,” Schmitt added. “When I started to think about my approach, I didn’t want to be looked at as controlling, because the first thing that business units would say was, ‘Oh my God, here comes corporate again, telling me what I can’t do.’ So I wanted to make sure that I really partnered with them. I’m not going to own anything, per se. I’m just going to facilitate things so they understand the risks they’re taking on as they grow.”

Employees also need a culture in which people are communicating risks up the chain of command. But that alone is not the solution. “The problem with enterprise risk management is that you get a lot of garbage,” she said. “You get a lot of information—a lot of good information—but not all of it [pertains to what] is really high risk for the corporation. And there’s no way to easily manage all this information you’re taking in.”



## RISK AT THE INDIVIDUAL AND ORGANIZATIONAL LEVEL

The afternoon panel took on the cognitive biases that often get in the way of individual and organizational understandings of risk. Eamonn Kelly moderated a conversation on this subject with Ron Schouten, a forensic psychiatrist and crisis consultant, Harvard Medical School professor of psychiatry, and director of the law and psychiatry service at Massachusetts General Hospital; and GBN consultant Steve Weber, a professor of political science at U.C. Berkeley and author of *The Success of Open Source*.

“People’s cognitions are often influenced by an underlying fear; fear of failure, fear of doing something that will lead to harm or criticism...”

—Ronald Schouten,  
Harvard Medical School

As Kelly observed in his opening remarks, both cognition and emotions play important roles in our understanding of risk. “Our cognitive processes are subject to biases that we’re very often unaware of,” he said. “And we also bring emotional responses to issues that influence our perceptions and therefore our judgments. Risk is linked largely to perception, which is linked to the lenses through which we see the world, which is linked to the assumptions that we make—many of which are implicit and not well understood by us.”

Ron Schouten continued the discussion with an explanation of how our growing understanding of neuroscience and of how the brain works has illuminated the problem of risk management. “When we think about the brain, we think of it as divided into two parts,” he said. “There’s the neocortex, where all the higher function is, all the thinking, all those relationships. And then there’s the old lizard brain, the limbic system, which is really where the action is. As one of my old professors used to say, it’s the home of the four Fs: fighting, fleeing, feeding, and fornicating.”

Emotions always trump cognition, he said, at least initially. One of his big challenges in a crisis situation is to help people modulate between the two responses. If someone comes into his practice and is uptight and overly intellectual, he tries to get them to be more emotive and in touch with their feelings. If someone comes in who is so emotional they can’t intellectualize the problem, he tries to engage their intellectual defenses in order to deal with the real issues.

### The Psychology of Fear

Schouten outlined a series of common psychological defenses that seek to decrease exposure to fear and other negative events. These responses come into play because we are trying to make decisions but can’t handle all the information coming at us.

- Denial. “Denial is a psychological response where you just say, ‘Nope. Didn’t happen. Doesn’t exist.’” he said. “Most of us engage in it at a much higher level of intellectualization, and it’s career-ending.”
- Repression. “You’re aware, at some level, that the problem occurred, but you’ve just shoved it away: ‘That’s not a problem with these personnel. This problem will go away. Not a problem in the supply chain. We’ll just distance ourselves from it,’” he said.
- Magical thinking. “If I think it, it will be so,” he said. “And it’s surprising how often we encounter that in adults and in very responsible settings.”
- Response fatigue. “When you’ve been presented with a stimulus enough times, people get numb to it and stop responding,” he said. “We see this in compassion fatigue in first responders, EMTs, firefighters, and police in disaster situations. We see it in organizations where you’re constantly called to come in and do something about a problem and people just say, ‘OK, I’ve seen this,’ and they don’t respond at the previous level.”
- Seeking certainty. “We really intellectualize,” he said. “We go to statistics. We want to lock in.” In fact, studies of risk assessment and perception show that if someone gives a hard number versus a percentage, the hard number will be rated as a higher risk.

Some people are more hard-wired than others to be risk-takers, because individuals have different patterns of dopamine receptors and produce different amounts of dopamine. These levels go up in people who successfully take risks. There is work in the securities industry to monitor things like heart rate variability to assess individuals’ propensity toward risk-taking.

Emotion is a powerful force, as well. “People’s cognitions are often influenced by an underlying fear: fear of failure, fear of doing something that will lead to harm or criticism,” he said. “When our emotions are actively engaged in a problem, we tend to ignore what our cognitive side says. We ignore what the data says with regard to probability.”

And people’s general temperament also greatly affects their perception of risk. “People who are very optimistic and have had positive life experiences will tend to overpredict good outcomes and underpredict bad outcomes,” he said. “People with negative life experiences will overpredict bad outcomes and underpredict good outcomes.” The greater distance a decision-maker sits from the front lines of a problem, the greater the level of disengagement with the emotional cues that are motivating people, often quite accurately, to act.

Schouten pointed to work in the fields of behavioral economics and decision sciences to classify the heuristics people use as “rules of thumb” when making decisions. One is availability. “When we can conjure up an image, a recollection of an event that’s similar to this one, we will predict a much higher rate of that incident happening,” he said. “People have a lower assessment of the absolute risk if they are familiar with the situation, they’ve seen it before, and if they have knowledge of how it works. Anxiety goes up with lack of familiarity and lack of knowledge. If you ask most people to assess which factor poses the greatest risk to us overall—an attack with conventional explosives or a biologi-



cal agent attack—most people would say a biological agent. In fact, if you look at availability and access and ease of delivery and the amount of damage that can be done, conventional explosives have a much higher risk of being used.”

A way to get around this common heuristic is to help people feel familiar with threats and implement control measures. Another is to “bind anxiety” with good information that’s honest and actionable, that gives people a feeling of control, and that lets them know when more information is going to be coming.

### A Look at Risk Aversion

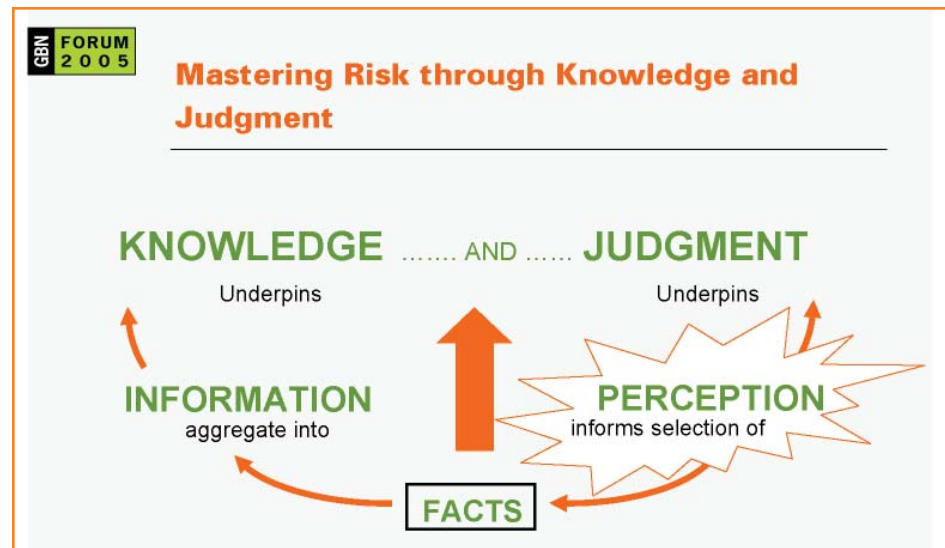
Steve Weber continued the conversation by detailing risk aversion and how it intersects with business strategy. “When we think about winning in markets or winning in crises, the kind of strategy that we need to overcome risk aversion is not going to come from brilliant individuals and it’s not going to come from the wisdom of the crowd,” he said. “Prospect theory is the notion that people are risk-averse in the domain of gains and risk-acceptant in the domain of losses, which, in simple English, means when you’re doing well, you buy too much insurance, and when you think you’re losing, you tend to place very scary bets. Even when you explain to people that this is what they do, they still do it.”

The problem is that when making tough decisions, most people don’t know whether they are in the domain of gains or losses. They also don’t know where the other players in the market are. Worse, they often don’t know their own risk thresholds, and those of their competitors, until they increase the risk to the point that it’s unbearable and one person swerves to miss the oncoming car in a game of chicken, so to speak. This lack of knowledge can create dangerous situations of competitive risk-taking like the Cuban Missile Crisis, as Nobel Prize-winner Thomas Schelling explored. As Figure 4 illustrates, mastering risk requires both knowledge and judgement.

“When we think about winning in markets or winning in crises, the kind of strategy that we need that overcomes risk aversion, is not going to come from brilliant individuals and it’s not going to come from the wisdom of the crowd.”

—Steve Weber, U.C. Berkeley

Figure 4: Mastering Risk



**TEXAS HOLD 'EM**

As the cards were dealt, the excitement and noise level mounted: GBN's Texas Hold 'Em Tournament had begun. In addition to learning this increasingly popular poker game, we also learned about our own risk appetite and the strategies of others? Among the comments:

- Everyone shares the uncertainties; it's how you manage them that matters.
- Go for the big bluff if you want the big payoff.
- Successful players don't just play the cards, they play the table, paying close attention to the externalities.
- While playing conservatively may get you to the final table, you're ultimately going to lose.
- Collaboration works to a degree—but is easily sacrificed when winning is at stake.
- If you stay in the game long enough, you're luck may turn; even with a weak initial hand you can win.
- Risk-taking is not only psychological but physiological (stick with the water, not the wine)!
- In order to win, you have to play.
- I'll keep my day job!

Weber cast doubt that the so-called wisdom of the crowd could help people get around their cognitive biases. People just aren't very good at managing risk, he said. You could somehow use the law of large numbers and random distributions to compensate for the worst excesses of individuals in assessing risk. "But where will this get you?" he asked. "It gets you exactly to the market price for risk, which guarantees mediocre performance. It never beats the market because it is the market. What you're going to get is broadcast TV, the S&P 500, the Chevy Impala, and Applebee's neighborhood restaurant. I don't think that's what the people who come to GBN meetings want. I think we want HBO; we want Legg Mason Value Trust; we want a Porsche Boxter; and we want Chez Panisse. And we're not going to get that from large numbers."

Instead, he made an "unfashionable proposal" that balanced the notion of using really smart individuals and using the wisdom of the crowd:

- Build a risk group—a small (8 to 12 people), highly trained, highly specialized group that is outside of all line responsibility and all day-to-day decision-making. And don't call it the "risk management group," but rather call it the "risk engagement" or the "risk ownership" group.
- Give the group access to the very best information from inside and outside the organization, and let it make decisions.
- Give it an in-house psychiatrist who consistently trains individuals to get better at understanding their own patterns of risk aversion and risk acceptance, so that they can step outside and see them for what they are.
- Give it a communications specialist to provide useful information inside the organization and usefully deceptive information outside the organization, in some circumstances.
- Track its performance and feed that information back to it as quickly as possible in real time. But don't punish it for failure.
- Analyze its decision-making to see if we can learn something about what we call "good judgment."
- Align the group next to a kind of skunkworks and let it race for 10 years. And then find out at the end of those 10 years who does better.

And with that modest proposal, Forum participants departed for dinner and an evening of Texas Hold 'Em, the ultimate laboratory for exploring individuals' perceptions and reactions to risk.

**NAVIGATING THE MAZE**

Successful people take risks to learn. Moreover, those who learn well from experience take time to reflect on that experience, see what connections they can make to the “real world,” and begin to act differently based on their learnings, said Jimmy Carter, president of Effective Leadership International the moderator of the Maze experiential learning exercise on Wednesday afternoon. The Maze is a large, checkerboard carpet that a team tries to traverse safely without stepping on a wrong square (thereby earning a beep and a penalty). After a few minutes to strategize, the team has to discover—and remember—the safe path through this “unknown territory” without talking. And sometimes the safe path changes in the process! Is it better to be cautious or to make mistakes? How does being part of a team affect our risk-taking? And how might this translate into our organizational environments? In this spirit, participants reflected on the key insights they gained from playing the game:

- Elaborate preparations turned out to be useless. Until the game actually started we didn’t understand what our roles would be in helping one another.
- Effective strategy at the beginning focused not on how to get across the maze, but on how the group was going to learn an effective strategy.
- Teams self-organized into those who could remember how to direct people to the right squares. If you had eight traffic cops you were in trouble and if you had just one you were also in trouble.
- Knowledge was held by the group. No one could remember the entire path alone.
- We were faster because we couldn’t talk. If we had been able to talk, we would have stopped playing the game and debated the right strategy for half an hour.
- Once we understood the activity, a few minutes in the middle of the game to talk about strategy and course-correct would have been worth 10 minutes of preparation at the front-end.
- When the pattern changed, people suddenly had different kinds of information and could no longer support one another. Chaos ensued and the uncertainty level spiked. We sped up and panicked instead of slowing down and reflecting.
- No one sent around a person to learn from other groups.
- We took the most complicated path possible. We never stopped to simplify. We got stuck in the ruts of our own patterns.

**THE LESSONS FOR ORGANIZATIONS WERE CLEAR TO MANY PARTICIPANTS:**

- “Purposeful failure,” like the experimentation needed to successfully get across the Maze, is not entertained well in corporate America.
- In some organizations, making mistakes is more costly than in others. There are forgivable mistakes, from learning something new, and those that are less forgivable, because you’ve done them before.
- Many people fear groupthink. In some cultures, shared group intelligence is never allowed to go forward, because it’s so threatening to individual rationality.
- Unlike the real world, there was one goal and one understanding of the goal in the Maze. The problem in organizations is that we all think we have the same goal, but when we start talking about it, it isn’t the same goal at all.



“Risk management will be a kind of a threshold factor. It will not provide significant competitive advantage to any company or institution. The ones who win are going to be the ones who can both reduce the risk and increase the opportunity. That will provide the competitive advantage.”

—Ron Jonash, Innovation Management Inc.

## RISK AND REALITY

Each type of organization or industry has its own particular way of dealing with risk. We started the morning of the last day of Forum focusing on the risks facing six very different organizations that had volunteered to serve as case studies. The final session applied our insights from these—and all our prior—conversations into a broad, longer range context as we contemplated the risks ahead for all of our organizations.

### Risk: A Master Class

So how are world class organizations currently thinking about risk? Participants from IBM, The World Bank, PricewaterhouseCoopers, Pitney Bowes, Herman Miller, and Scottish enterprise discusses some of the big risks they were facing. We came away with a few key themes and insights:

- There is risk and opportunity in having a mission that is not fluid enough. We need a mission that responds to the opportunities in the world and helps us manage the risks.
- How you set up a problem makes a big difference. And once you’ve defined a solution, it’s helpful to step back, question your assumptions, and look at the problem again in an entirely different way.
- How do you tell a new story about an old song, one that will get people attracted to being there and to bring their energies?
- In new product development, when you’re trying to develop really innovative products, the biggest risk is not taking the risk in the first place.
- It’s not about the questions that you ask; it’s the questions you’re not asking that are really important.

### Navigating the Risks Ahead

The last panel of Forum was a question-and-answer session between Forum participants and a distinguished panel: GBN CEO Eamonn Kelly; Ron Jonash, head of Innovation Management Inc., a Monitor Group company; forensic psychiatrist and crisis consultant Ron Schouten; Denise Caruso, founder and executive director of the Hybrid Vigor Insititute and GBN Network member; and Raimondo Boggia, founder and managing director of C-Sights, a Milan-based consultancy specializing in strategic vision, and a GBN Network member. Some highlights of the wide-ranging discussion follow.

**Question:** *Regarding climate change, the amount of CO2 that we're putting in the environment is already enough to trigger some kind of event. If we start making the changes needed now, we won't be the ones who will benefit. As a society and as a people, we need to figure out a new way to act, respond, and think when we're in a situation where what I do doesn't matter to me. It matters to some people 15, 30, 100 years from now.*

Kelly: "One of the things I've been struck by in the Forum is how little we've talked about the time dimension to risk. We've talked about probabilities. But you can't talk about probability unless you put it into a timeframe. People are talking about a 20 percent probability of an avian flu pandemic, but if you take it out to 20 or 30 years, there's a 100 percent probability. If you take a long enough view of climate change and extreme weather events, these become inevitabilities. I think part of the challenge for us all is not just to expand our sense of oneness globally, but also to expand our sense of longevity in terms of the decisions and the choices that we're all making."

Jonash: "I've seen more and more organizations, more and more CEOs, being held accountable for the legacy they're going to leave behind. I'm actually more optimistic than I was three or four years ago about people being held accountable for that. The kind of excesses of the dot-com boom and Enron—we have learned a lesson, or at least some CEOs have certainly learned a lesson."

Boggia: "I think we are witnessing the death of the either/or syndrome. When you say 'either/or,' it means either I'm strategic and long-term-oriented or I'm cynical and make money at the bottom-line tomorrow. Who said that it is either/or? In risk analysis you can find cynical opportunity in the short run and have another mindset for the future generations in the long run. So the either/or syndrome is killing the ability of the organization to quickly adapt to change."

Schouten: "I think if we apply certain traditional economic notions that everyone's going to act to maximize their self-interest, we end up in a very grim place. But I happen to believe that there is such a thing as bounded rationality, as well as bounded self-interest. It has to do with how we identify ourselves. Are we citizens of just our organization, just our community, just our country, or the world? Do we have longer obligations? One of the great pulls on people is thinking about their legacy in their own family. So, not so much on the stick side, but on the carrot side, what are we going to do for the people who come after us?"

**Question:** *We've talked quite a bit about risk from many different levels, from the individual level to the organizational level to systemic risk. What do you think about how risk is changing within organizations themselves?*

Weber: "I think in a funny way the perfection, or move toward perfection, of hedging in the financial sector, and the ability to develop really sophisticated and quite advanced means of managing financial risk, has (as often happens when you get really good at doing one thing) allowed you to see how bad you are at other stuff. As we've gotten better and better at managing financial risks, lots of the other things have bubbled up to the surface and become more

important. Risk now becomes a core competence of any strategy organization, precisely because the financial stuff is easier to take care of.”

Kelly: “There is an elevation of the notion of risk and the ownership of risk from the risk management officer, or a risk management group or team, to a higher level in the organization, to the board level. My hunch would be that despite our brave efforts here to broaden the definition of the notion of risk into something that’s bigger than it’s been traditionally seen, that’s not going to happen in organizations. I think risk will remain associated with downsides, with mitigation, with avoiding danger and peril. Where organizations will significantly evolve in the next 15 years or so is in their treatment of this concept of uncertainty. Risk will be the language that gets attention in organizations, that will lead organizations to a much greater mastery of uncertainty, which is about acknowledging uncertainty, understanding and tracking uncertainty, and having an agility, an adaptiveness, and a different kind of leadership style that is attuned to a world of radical uncertainty. And risk will be a route into that.”

Jonash: “It will be interesting to see how a company like GE, Nokia, or another bellwether company handles this. If they do something differently, there will be a tipping point when everybody else starts to follow. I sense that risk management—in the sense of downside risk, risk mitigation, risk avoidance—will be a kind of a threshold factor. It will not provide significant competitive advantage to any company or institution. It’ll be a ‘must-do,’ whether it’s Sarbanes-Oxley or something else. And the ones who win are going to be the ones who can both reduce the risk and increase the opportunity, so that the whole curve shifts up in terms of how we’re managing risk and opportunity. That will provide the competitive advantage.”

Boggia: “Organizations should create a chief risk officer, with two reports: chief crisis officer and chief opportunity officer. And the same person has to report to the CEO giving the risk analysis—short-term, medium-term, long-term—of the crises we could face and requesting the money for that, as well as giving the opportunities on the short run or the long run that we can take out of it.”

**Question:** *It is not the case that there are some people who take more risks and other people who take less; rather, each of us distributes our risk quota differently according to different psychologies and different values. Comments?*

Weber: “I actually am a little pessimistic about changing people’s risk propensity. I think you can affect the incentives within which those risk propensities then play themselves out. There is something about those risk propensities that can be affected minimally, perhaps with education that may change people’s calculations a little. I don’t think it’s going to change them profoundly.”

Schouten: “We’ve been talking about how you label things and how you present information. If you call it ‘mad cow disease’ people get really scared. If you call it bovine spongiform encephalopathy, most people say, ‘I don’t know what that is. That’s some weird disease.’ But ticked-off cows, that worries people. So how do you present the information to people in a way that’s reliable, that’s actionable, but also gives them the best picture?”

**THE WORLD BANK:  
A CASE STUDY**

“Will the World Bank be the right organization and have the right people to deal with the changing needs and demands of developing countries in the future?” asked Enrique Rueda-Sabater. The Bank’s mission is to reduce poverty in the world in a sustainable manner. Traditionally that’s involved providing advice, technical services, training, and financial services once the central government has invited the Bank in. But now the client landscape is changing and the needs are broader and less specialized; turnover within the Bank is increasing as well. In the spirited discussion that followed, the group observed that reducing downside risks and creating new opportunities may hinge on articulating a new and different mission, a new story—and realigning incentives and measures accordingly.

**Question:** *How do you engage in discussions with senior people about risk in such a way that you don’t engage in the unintended consequence of compromising their decision-making capacity? In essence, I can compromise your decision-making capability if I put risks in front of you and drive that chemical response to the top. I’m being responsible by bringing you risk. In the meantime, I have the unintended consequence that I may be compromising your ability to make use of the whole brain.*

Schouten: “I don’t know that we need to worry about it that much, because presumably the people who are in these leadership positions can get past that moment. And I think the way we help mitigate that impact is by providing some familiarity, by saying, ‘This is a very scary thing, but here’s what we can do about it.’ So by providing those elements of knowledge and control and the basic facts, I think we can get those people out of the limbic system and back in the neocortex pretty quickly. But a scary situation is a scary situation, and I think we owe it to people to deliver the bad news. By not delivering the bad news, or not being able to hear the bad news, you really screw up the decision-making process. So I think you just have to lay it out there, but in a way that is direct and even-handed and factually fits.”

**Question:** *What is the risk to the organization when we, as corporate citizens, bring risks forward? In the new environment of compliance issues, are we putting a responsibility on that company to address that risk?*

Weber: “There are so many new moral hazards, and the carve-outs often come so late in the process that we see behavior that later looks to be incredibly dysfunctional from a societal perspective. We need to be more aggressively forward-looking. For example, we should have been asking the question, not today, but in 1998, ‘What do private organizations need in order to mitigation strategies around avian flu? We’re only having that conversation today. That’s way too late. I think the impetus for that has to come from the outside. It’s not going to come from inside the government.”

Caruso: “In my space, which is scientific and technological risk, you’re dealing with innovations where there’s no historical data. It’s going to change. There’s going to be something that you didn’t know today that you’re going to figure out five years from now. So why do we refuse to acknowledge the truth of that at the beginning of the product cycle and gain some idea of what it is we might do when something bad happens? Companies can’t do that right now. If they do that they’re liable legally, because they’re admitting that they knew something might go wrong. I think it’s really important to start thinking of legal, public policy ways to protect companies that want to be innovative, that want to solve big societal problems, and that, right now, have their hands tied about acknowledging the reality that things change.”

“It’s really important to start thinking of legal, public policy ways to protect companies that want to be innovative, that want to solve big societal problems and that, right now, have their hands tied about actually acknowledging the reality that things change.”

—Denise Caruso, Hybrid Vigor Institute

## Final Thoughts

Weber: “Having a disciplined conversation about the risk environment is an interesting and potentially rich way to get back to the question of what is this organization really about—to get back to the mission question from a slightly different angle. As George Orwell understood, what you fear tells you a lot about who you are.”

Caruso: “We can be, and often still are, passive before our tools and our models that assess risk. And there’s sort of a new religiosity around that that I would really encourage people to challenge. I’d also encourage them to really look at new methods for doing this kind of work. Pre-risk analysis, we were victims of fate; now we can often become victims of reason.”

Jonash: “We probably spend 90 percent of our time measuring and assessing the risk or the opportunity and only 10 percent of our time developing contingency plans and action plans for dealing with it. I’d like to at least get it to 50/50. And frankly, I’d give up half of the measurement of the assessment of risk to get the 50 percent on action. We’ve got to move to action, because that’s where everything falls apart.”

## Conclusion

The presentations, exercises, and conversations at Forum 2005 served to underline several of the dimensions of the new reality of risk for organizations:

- Risk is rising up the corporate agenda.
- Risk is an uncertainty that matters—that is relevant—and often lives in the relationships and interactions among multiple uncertainties.
- Risk must drive the agenda of “explorers” every bit as much as the program of “exploiters”; it must be understood as much as opportunity as threat, which requires the creation of a new dialogue (new language and tools).
- Risk is emerging faster than ever from uncertainties in the external environment and then creating new threats and opportunities in the market and organizational environment.
- Risks are also interacting with one another. Addressing one threat or opportunity creates another threat or opportunity, especially as you move from the contextual to the market environment. This requires a continuous dialogue.
- Changes in business models are exposing us to increased risks, e.g., by “thinning the membrane” (outsourcing, global distribution, etc.).

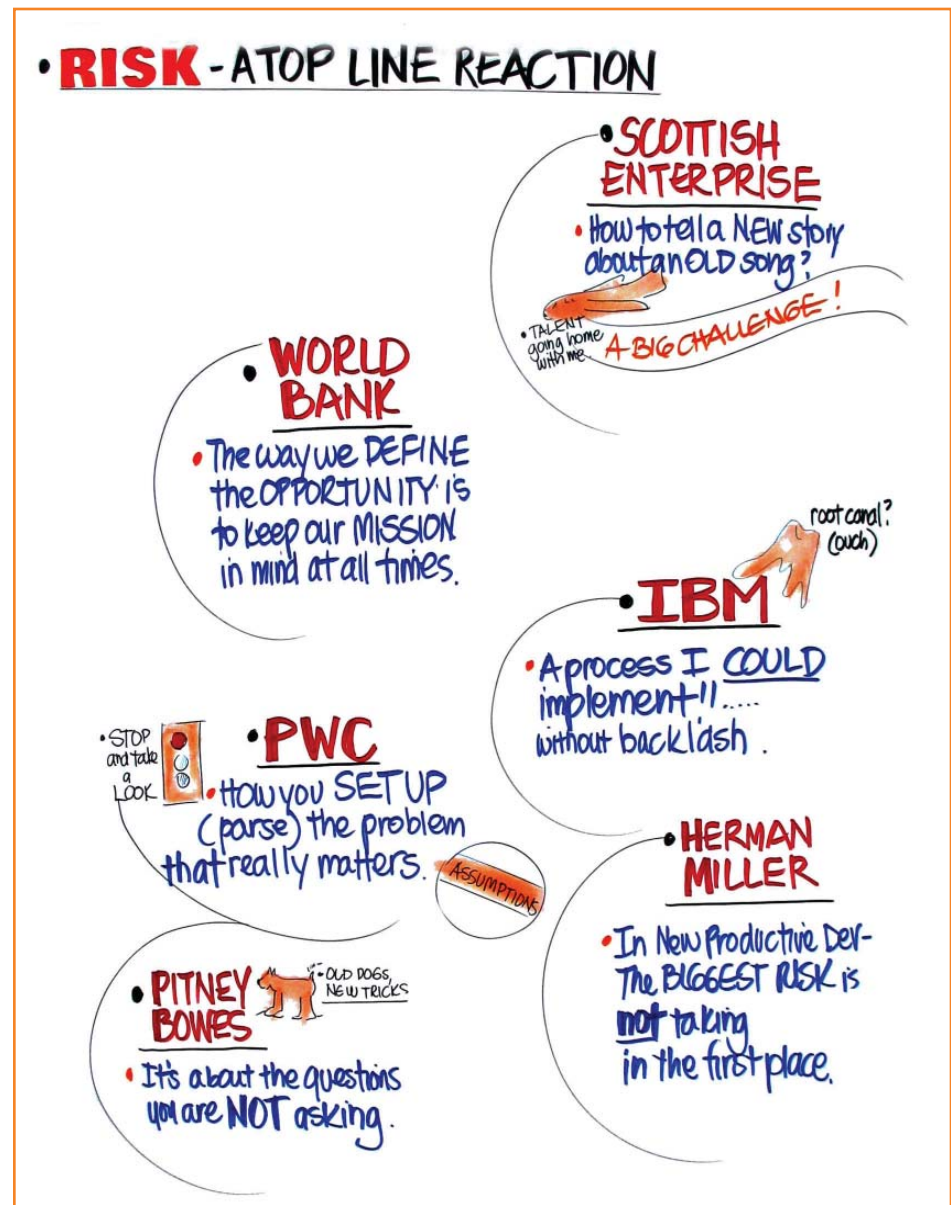
As this report suggests, the participants’ journey in Forum 2005 was a rich and involved one. Far more was said, done, and learned in the course of our time together than can be squeezed into a summary of this sort. Indeed, much of the most useful learning was personal—rooted in insights that the participants made as to how risk can translate into opportunity, and how they can broaden and deepen their approaches to risk management in their own organizations.

We have been delighted to learn in follow-up conversations that many attendees have already put the approaches and insights that they gathered at Forum to work in their organizations. (A few have also reported increased poker winnings from Texas Hold ‘Em.)

But we are even more gratified that these same people, and the organizations that they serve, are committing themselves to continuing the development of the new language and the new tools that they—and we all—need if we’re going to manage risk effectively in the uncertain future we face. We hope that the readers of this report will join us in that effort.

“Are we citizens  
of just our  
organization; just  
our community;  
just our country;  
or the world? Do  
we have longer  
obligations?”

—Ron Schouten, Harvard  
Medical School





## Acknowledgments

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### RECOMMENDED READINGS ON RISK

#### BOOKS:

*Against the Gods: The Remarkable Story of Risk* by Peter L. Bernstein (Wiley, 1996)

*The Essential Guide to Managing Corporate Crises: A Step-by-Step Handbook for Surviving Major Catastrophes* by Ian I. Mitroff, Christine M. Pearson, and L. Katharine Harrington (Oxford University Press, 1996)

*Fooled by Randomness: The Hidden Role of Chance in Life and in the Markets* by Nassim Nicholas Taleb (W.W. Norton & Company, 2001)

*Inevitable Surprises: Thinking Ahead in a Time of Turbulence* by Peter Schwartz (Gotham Books, 2003)

*Powerful Times: Rising to the Challenge of Our Uncertain World* by Eamonn Kelly (Wharton School Publishing, 2005)

"Understanding Risk: Informing Decisions in a Democratic Society, Committee on Risk Characterization, National Research Council, National Academy of Science," Paul C. Stern and Harvey V. Fineberg, editors (National Academies Press, 1996)

*When All Else Fails: Government as the Ultimate Risk Manager* by David A. Moss (Harvard University Press, 2004)

*Why Some Companies Emerge Stronger and Better From a Crisis: Seven Essential Lessons for Surviving Disaster* by Ian I. Mitroff (AMACOM, 2005)

#### ARTICLES:

"Business 2010: Corporate Views of How Firms Will Do Business Five Years from Now," *Economist Intelligence Unit* (January 25, 2005)

"FT Mastering Risk," *Financial Times* (Sept. 23, 2005)

"Emergent Risks" (research paper) by Peter Gerzon and Bryan Richardson (London: Institute of Risk Management, 2005)

"A Delicate Balance Between Risk and Reward" by Eamonn Kelly and Steve Weber, *Financial Times* (Sept. 9, 2005)

"A Risk Management Reality Check for RMCI 2005"(draft) by Robert Vaughn Jacobson (New York: International Security Technology, 2005)

"Hold or Fold? Sizing up Business Risk" by Eileen Shapiro, Harvard Business School Working Knowledge (May 9, 2005)

"Strategy Despite Uncertainty: Cutting Through the Fog" by Donald Sull, et. al., *Harvard Business Review OnPoint* (Sept. 1, 2005)

"Investors Order Private Opinion Polls on Companies" by Sundeep Tucker, *Financial Times* online (Aug. 21, 2005)

"Adam Davis: Eagle-Eye on the Ecosystems Economic Sector" by Chris Van Daalen in *Ecostructure Financial* (August 2005)