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Behind the Boardroom Door: How public company directors manage risk

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Extreme weather events, supply-chain breakdowns, cyber-crime or other natural and human-made disasters pose challenges today for most firms and organizations. What are the best strategies for boards and managers to follow that will reduce the likelihood and impacts of these and other catastrophic risks? The National Association of Corporate Directors New England Chapter's Feb. 12 event in Boston will focus on this question with professor and author Howard Kunreuther, co-director of the Risk Management and Decision Processes Center at the Wharton School, University of Pennsylvania, and Kim Nelson, retired Senior Vice President of External Relations of General Mills.

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Howard Kunreuther

Kunreuther previewed key themes, also covered in his new book, "*Mastering Catastrophic Risk: How Companies are Coping with Disruption,"* coauthored with Michael Useem, below:

Overall, how well are U.S. corporations managing catastrophic risks today?

Companies are now preparing for low-probability, high-risk events more seriously than they did before. Firms that have an active dialogue internally about adverse events and systematically learn from the catastrophic losses of others are likely to improve their own operations. Many companies also have interactions with government officials and regulators making them more aware of actions they can take to reduce the likelihood and consequences of the risks they face.

What are the most common errors organizations make when it comes to planning for catastrophic risks?

The greatest errors are short-term thinking and overconfidence. Company leaders may perceive the likelihood of a disastrous event as so low that they treat it as below their threshold level of concern. To deal with this form of myopia, companies should stretch their time horizons: ather than framing the annual likelihood of a specific adverse event as 1 in 100, recognize that the probability of at least one of these events occurring over the next 30 years is greater than 1 in 4.

How can firms justify investing in risk prevention measures now given that it may be perceived as being costly and not worth the effort?

Risk management should be viewed as a long-term investment in staying competitive by creating sustainable value and protecting the firm and its reputation, rather than a short-run burden on the management's time and the company's budget. When a firm cannot purchase insurance against a given risk at an attractive price, it may opt to self-insure by examining its risk appetite and risk tolerance. In this regard the high price of insurance can be viewed as a market signal that the risk may not be worth taking in the first place.