Building reputational resilience

in the Food, Agribusiness & Beverage sector

Empower Results®

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Executive summary

The food, agribusiness and beverage (FAB) sector has become relentlessly agile as it is constantly challenged to react to changes in consumer preferences, environmental awareness, legislation, global trade negotiations and digital disruption. An ability to look ahead and pre-empt emerging risk is core to its future success.

Analysis of where future risks lie requires more than economic knowledge or political insight. Having a strategic overview of a business and how it could be affected by a wide range of outside influences is vital – and enables organisations to put the right measures in place.

According to Aon's Global Risk Management Survey (2019), the top ten industry risks have been identified as:

Industry risk insights

"What severe yet plausible events could cause financial and reputational harm?"

Top 10 Risks for Industry

Looking ahead to 2022

CEOs and board members regularly list reputation as one of the company's most valuable intangible assets. Yet every month, a new reputational crisis makes the headlines, destroying shareholder value and trust with customers and stakeholders. While the sources of the crisis may vary, in many cases financial markets punish the companies, sometimes leading to a severe and sustained erosion of market value.

Why is risk increasing?

The increase in focus on reputational risk is due to several factors, including the global news environment and the growth in social media. Social media delivers opinions quickly and permanently and as companies have little control over the messages, it shifts the balance of power from companies to customers and other stakeholders.

Geo-political activity and macro external influences are also increasingly impacting the FAB industry. Complex and Just In Time (JIT) supply chains have increased the scale and scope of reputational risks as companies are less able to monitor business practices or anticipate emerging issues. Once a crisis occurs it's usually the large, visible company that gets the blame, even if the cause was further down the supply chain.

Expectations about business responsibility are also increasing. Customers no longer want companies to keep their brand promise but expect unblemished business processes across data protection, privacy and customer support. It's also becoming a prerequisite that companies align their business practices with social, ethical and moral standards - and in an industry where trust is absolutely critical – often on a level that exceeds legal or regulatory requirements.

> "It takes many good deeds to build a good reputation, and only one bad one to lose it."
> Benjamin Franklin

Understanding reputational risk

A company's reputation needs to be actively managed like any other core asset. Companies need to have a process to identify risks and while communication plays an important role, active reputation management should be integrated into business leaders' strategy decisions and holistically coordinated across an organisation.

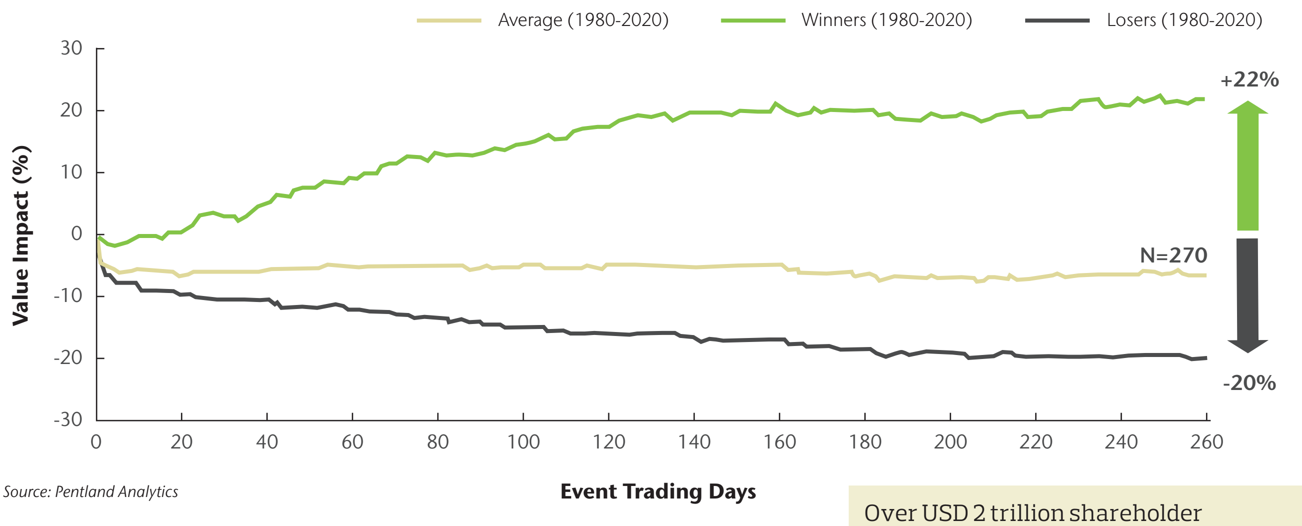
The intangible nature of reputational risk means that it is one of the more challenging risks to assess and quantify. Aon has recently commissioned Pentland Analytics to conduct independent specialist risk research and analysis that focusses on brand and reputational risk through an industry lens.

The study has identified organisations who have faced a major crisis event and then tracks who has come out the other side as either a winner or a loser - in terms of impact on shareholder value.

Where a business doesn't have shareholders and is privately owned, the value can be measured by other metrics in terms of revenue, customer relationships, supplier contracts and earnings before interest, taxes, depreciation and amortization (EBITDA).

The table below demonstrates the impact of 270 reputation crisis events across all industries over a 40-year period.

The Impact on Shareholder Value



Source: Pentland Analytics

- The X axis = number of trading days post the crisis event
- The Y axis = the modelled impact on shareholder value

Over USD 2 trillion shareholder value destroyed from poorly managed Reputation crises

The beige horizontal line in the middle of the graph illustrates how companies would normally perform. There are eighty-seven winners demonstrating an average positive value impact of 22% which translates into a value impact of almost $1.3bn. In contrast, the one hundred and eighty-three losers had an average negative value impact of -20% which translates into a negative impact of -$2.1bn.

What does it take to be a winner after a major crisis?

Our research identifies the five key characteristics of winners and losers

	Preparedness	Leadership	Communication	Action	Change
Winners	A deep commitment to loss prevention and mitigation	Strong, visible, authentic leadership from the CEO	Accurate, honest and well-coordinated communication	Instant, global response and visible action	True remorse with a commitment to meaningful change
Losers	A failure to prioritise risk preparedness	Weak or delegated leadership, failure to take responsibility	Opaque, partial or inconsistent communication	Delayed, absent or limited action	Minimal, inauthentic or reluctant remorse

Source: Pentland Analytics

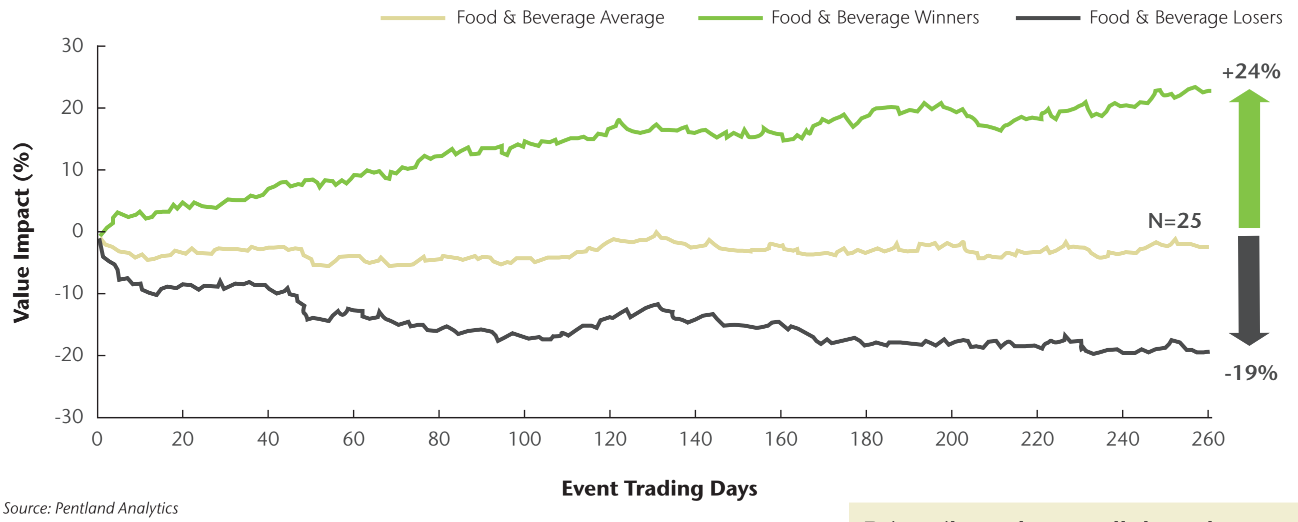
This emphasises the importance of risk preparedness and how those who are better prepared are more likely to emerge as winners from the crisis. As the COVID-19 pandemic has further illustrated, strong and visible leadership through a crisis is vital. The harsh reality is that very few CEOs remain in their role after a crisis, if they emerge as 'losers'. We see from the winners, that they are those who communicate clearly and honestly, with both authenticity and sincerity. They not only commit to taking action - but commit to meaningful change too.

Reputational risk in the Food, Agribusiness & Beverage (FAB) sector

Winning is difficult, but not impossible

Across the food and beverage sector the research looks at the impact of twenty-five crisis events where there were ten winners and fifteen losers. Almost half of these crisis events are product safety related with the other half a mix of governance failure, financial irregularities and marketing errors.

Food and Beverage



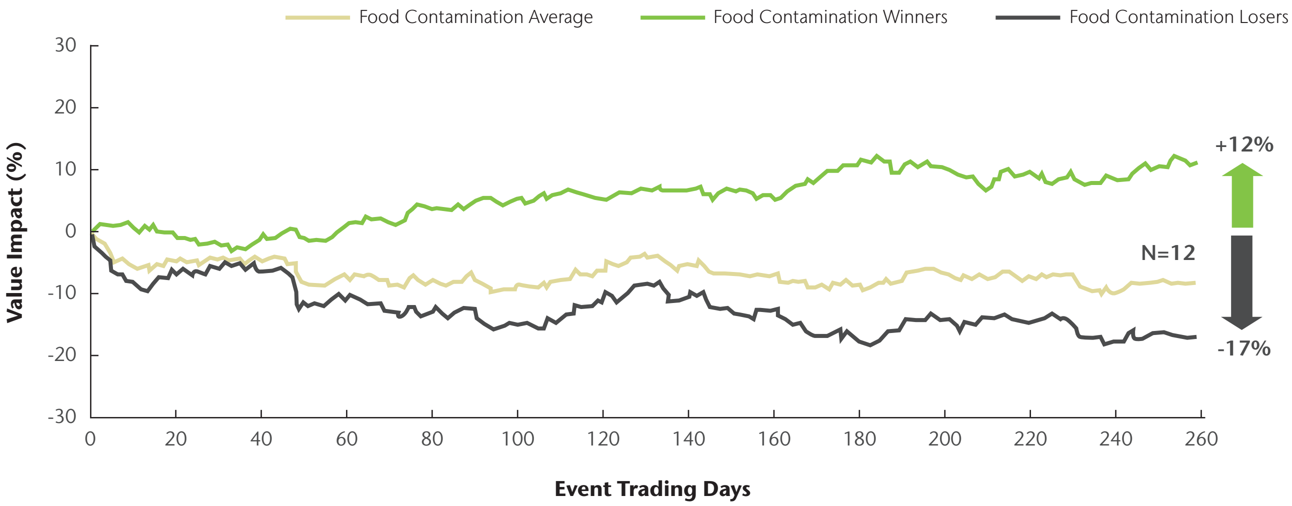
Source: Pentland Analytics

Primarily product recalls but other sources of risk well-represented

Value recovery is challenging in the event of a food safety crisis

Some of the more alarming food contamination cases in recent years have included melamine in infant milk formula, sabotage by a disgruntled employee putting needles in strawberries and pork products triggering miscarriages in pregnant women. In the social media world we now live in, judgement in the court of public opinion is instant and by the time the facts are established, consumers and investors have often moved on.

Value Impact of Food Contamination



Source: Pentland Analytics

Of the twelve cases (on the diagram above) there are eight losers and only four winners with three different types of contamination:

- Accidental contamination
- Perceived but no actual contamination
- Deliberate contamination

When a crisis happens, less than one third of organisations emerge as winners.

A tale of contrasting fortunes

The table below tells a story of contrasting fortunes for Perrier and Heineken.

Contrasting Fortunes

Source: Pentland Analytics

In 1993, Heineken recalled, destroyed and replaced 15.4 million bottles, because the necks of the bottles were vulnerable to splintering. At the time, they publicly stated 'we don't want to take any risk'.

In 1990, during some routine quality checks, North Carolina health officials tested some Perrier bottles and discovered elevated levels of benzene, and a media frenzy ensued. 160 million bottles were recalled from 120 countries.

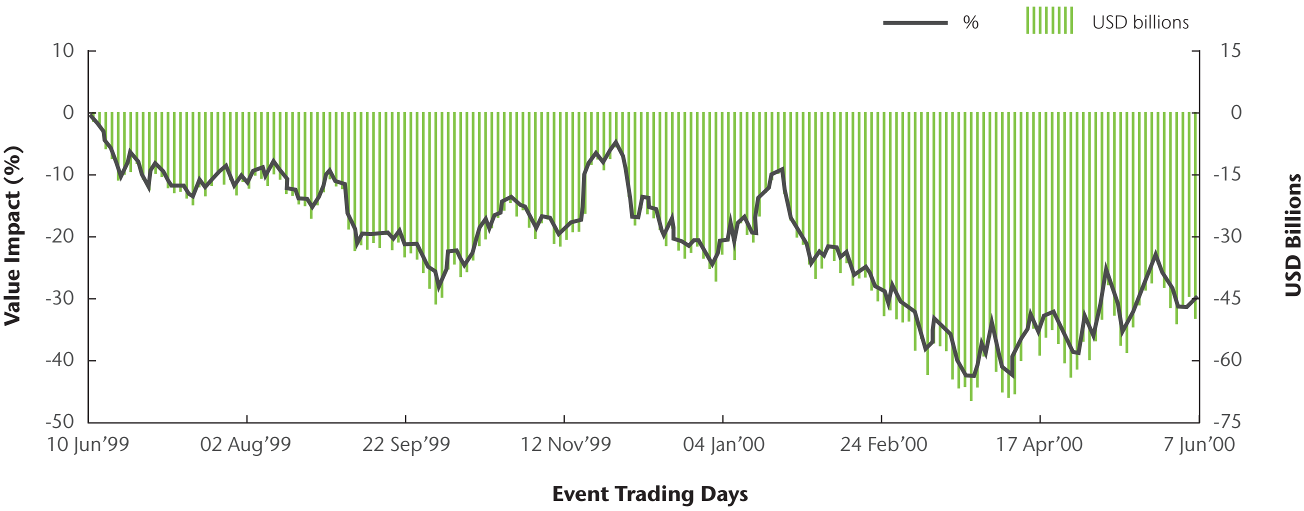
News headlines at the time used emotive language like "contaminated," "laced," and "tainted" with benzene. Benzene was described, not always accurately, as a "component of crude oil," "cancer-causing," and "flammable poison".

It's worth remembering that there were no injuries in either case. Heineken is still going strong. Perrier is now owned by Nestlé.

Perrier	Heineken
• Perrier estimated that "L'incident Benzene" had cost it USD262.9m: USD197.5m for recalling and destroying the bottles, USD47.7m on related advertising communication, consultants and financial charges, and USD17.7m on associated administration charges. • Perrier did not have product contamination and recall insurance. • USD620 million (approx. 23%) of shareholder value is destroyed over the post-event year and the Perrier Group loses its independence to Nestlé.	• At the time of occurrence, Heineken estimated the loss to reach USD10-50m. • It is unclear whether Heineken's product liability insurance policy would cover the losses. • Ultimately the glass manufacturer agreed to compensate Heineken for an undisclosed sum. • USD870 million (approx 22%) of shareholder value added over the post-event year.

Perception IS reality

Coca Cola - Perception is Reality



Source: Pentland Analytics

In the spring of 1999, dioxin was detected in poultry feed in Belgium. When the media reported on the dioxin contamination in May, consumers were understandably concerned about the ingredients in animal feed, and the consequential food safety impact. While it was later proven not to adversely impact human health, there were high profile political resignations, and seven million chickens and fifty thousand pigs were slaughtered and discarded.

Against this backdrop of consumer nervousness, the integrity of food was high in Belgians’ consciousness. Increasing numbers of schoolchildren fell ill across Belgium, France and Luxembourg, and the one common denominator identified was the consumption of Coke. Bans followed around the world. 17m unit cases were destroyed at a total recall cost of an estimated USD250m.

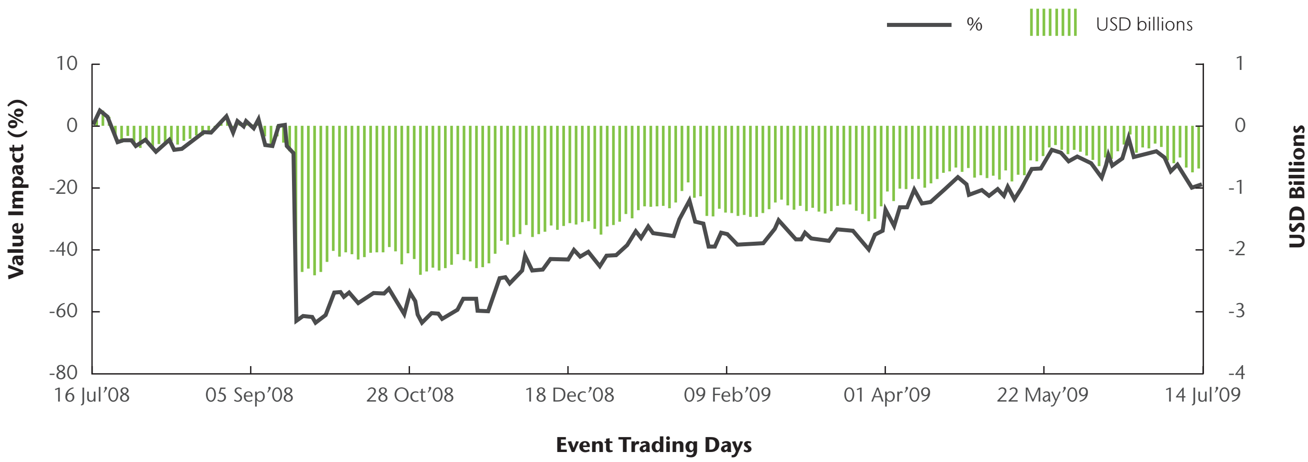
Ultimately, it was shown to be mass hysteria and there was nothing wrong with the product. But perception IS reality, and USD50 billion (over 30%) of shareholder value is destroyed over the post-event year.

Contaminating the innocent

There is no doubt that stories of deliberate contamination of infant milk formula products by a number of Chinese dairy companies sent shock waves around the world. In 2008, over 300,000 babies became ill, 54,000 were hospitalized, and sadly there were 6 deaths. The scandal involved milk and infant formula being adulterated with melamine in order to artificially inflate the protein content for quality testing.

Looking at China Mengniu, one of the companies involved in the scandal and given the profoundly shocking nature of events, it is not surprising that their shares nosedived 60% on the first trading day they were known to be involved. In the year post-event, USD700 million (approx 18%) of shareholder value was destroyed. A smaller rival, Shanghai-listed Beijing Sanyuan Foods - whose products tested safe - enjoyed a 52% rise in value over the post-event year.

China Mengniu Dairy - Deliberate Contamination



Source: Pentland Analytics

Not if – but when

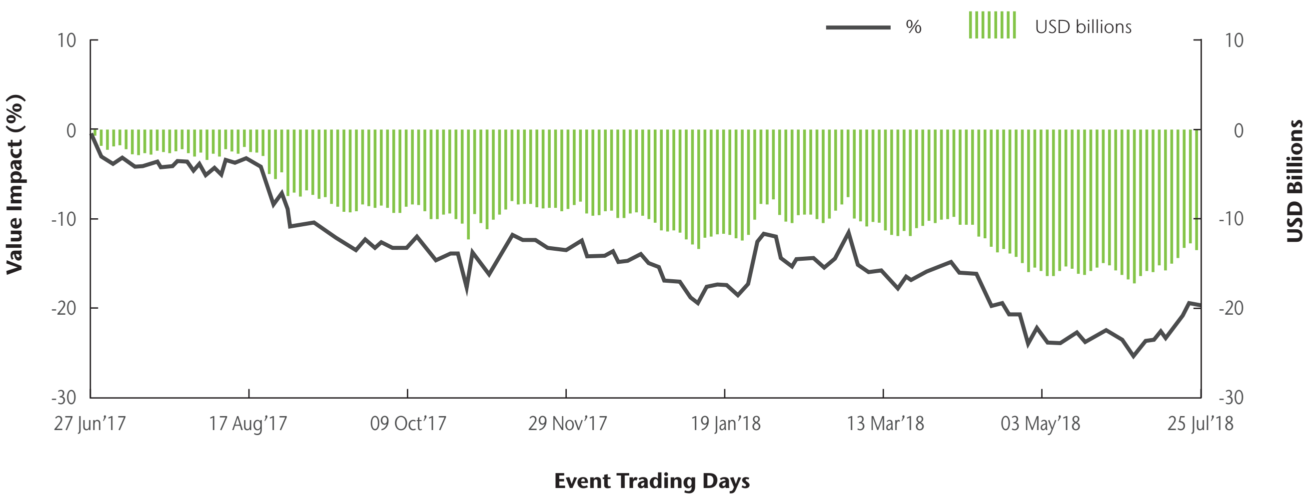
At Aon, our view is that cyber in the FAB industry more often than not manifests in the form of either a business interruption event or supply chain disruption and both of those feature in the industry top 10 risks, as identified by Aon's 2019 Global Risk Management Survey. As with any major risk event, there is invariably an impact on the company's brand and reputation.

Boards are continuing to increase their focus on enterprise cyber risk, wanting to understand what a 'bad cyber day at the office' looks like, how much it's likely to cost, how D&O and cyber are intertwined, and in some cases how cyber breaches have led to both investor and regulatory scrutiny.

The reality is that for organisations operating in the FAB sector, the cost of an Operating Technology (OT) breach is likely to be a multiple of the cost of an IT breach. The other relevant insight to consider is the law of unintended consequences – where very large global players such as Mondelez have been randomly attacked rather than specifically targeted – and this could happen to any company at any time.

Covid-19 has certainly forced the remote working agenda, and while the nature of the FAB industry means factories continue with production, there is no doubt that there is an increase in focus on cyber risk as some business functions (such as Finance, IT, HR and so on) moving to a hybrid working model.

Mondelez - Cyber Attack



Source: Pentland Analytics

Mondelez was one of several high-profile victims of a NotPetya ransomware attack in 2017, with court papers revealing that with 1,700 of its servers and 24,000 laptops were rendered "permanently dysfunctional". In the region of USD14 billion (20%) of shareholder value was destroyed over the post-event year. Mondelez are currently pursuing a $100m claim against Zurich in an Illinois court, and the world is watching with bated breath for the decision.

Horizon scanning for emerging reputational risks

Managing reputational risk is a journey of learning for any organisation and should be addressed as a corporate governance issue at board level. Pre-loss decision making together with constant vigilance should be employed to effectively understand and get ahead of emerging issues coming down the track.

The COVID-19 pandemic has amplified the need for food and drink companies to have a robust cyber risk strategy. Exposure to cyber risk is increasing on many levels particularly where there are complex food supply chains. We have seen the theft of sensitive intellectual property and random ransomware attacks with criminally motivated food fraud. The 'Just in time' (JIT) process is also heavily reliant on the use of new technology across multiple supply chains.

Environmental awareness, tied in with climate change and sustainability, is also growing quickly and in the FAB sector, there's been a conscious decision to shift to plastic-free packaging and the use of renewable fuels and anaerobic digestors, as examples.

Food safety remains an important issue and the COVID-19 pandemic has accelerated the way organisations need to reassure customers. The management and safety of staff remains paramount but an increase in costs to source PPE and install safety measures across production lines has been high.

We've also seen a growing link between reputation and shareholder value around gender diversity at board level. When an organisation's most senior leadership is a collaborative and diverse team across age, background, gender and ethnicity as well as skills and experience it sends a powerful signal to both shareholders, customers and both current and future employees about the commitment to equality and inclusion.

Demonstrating a better understanding of other cultures has a direct impact on workforce productivity and revenue, as well as positive views held by consumers and shareholders. There's also a connection between diversity as part of an organisation's risk management procedures leading to the arrangement of more favourable insurance programmes.

> "Your brand name is only as good as your reputation."
> Richard Branson

How a crisis event can drive change for the better

We have seen in recent years how changes can be made for the better after a crisis, scandal or tragic fatality. The food safety landscape has witnessed an acceleration in changes from one that was focussed on unintentional or natural contamination to one that now requires food manufacturers to consider, control and prevent more unpredictable and sinister events.

Natasha's Law

The issue

In 2016 Natasha Ednan-Laperouse died after eating a baguette. She had a sesame allergy and wasn't aware that sesame seeds had been pre-baked into the bread as a visible list of the ingredients didn't have to be displayed.

The impact

This prompted a change in the law for the food industry. Natasha's Law has already bought about changes to food labelling on pre-packed for direct sale foods - but it will be law in October 2021.

The change

It's hoped this will prevent severe reactions and deaths caused by a lack of clarity and insufficient labelling on food products.

Horsemeat scandal

The issue

In Europe, the horsemeat scandal saw meat from horses entering the supply chain as beef and ending up being sold in consumer products.

The impact

Initially identified in Ireland the scandal revealed a major breakdown in the traceability of the food supply chain and resulted in market withdrawals of tens of millions of food products across Europe, millions of euros of lost business and multiple prosecutions. Consumers' trust in manufactured food plummeted and sales of frozen hamburgers and ready meals dropped by nearly half overnight.

The change

The British government commissioned a review which resulted in the creation of a food fraud crime unit and a range of other collaborative enterprises across Europe including special functions within the European Joint Research Council (JRC) and food-focussed operations by Interpol known as Operation Opson.

Reputational risk assessment

Many organisations do not believe that they've done enough to understand the risks to their reputation.

The debate on whether reputation is a risk or an impact can often prevent it getting the attention it requires. Risk professionals spend less time with CMOs / brand and category managers; the very colleagues tasked with building brand and reputation equity. Reputation is usually a qualitative measure in the risk register, often with the CEO as an "owner". As a result, we learn very little about reputation exposure through a traditional Enterprise Risk Management (ERM) process.

At Aon we are seeing a growing number of organisations doubling down on improving their insights on reputation risk by:

- Validating that they have understood their most significant reputation risk scenarios
- Evaluating those risks through the lens of stakeholder sentiment
- Understanding the potential costs associated with the most significant scenarios
- Ensuring that current risk control measures are effective, and that insurance provides coverage for the financial exposure

When organisations assess risk through the lens of corporate reputation, rather than pure financial loss, we have seen them generate much improved insights on the specific scenarios that are likely to be most damaging to them and also an appreciation of how their stakeholder network would respond.

When we evaluate reputation risk, we do so on the basis of how stakeholders would be likely to respond to an event and with what level of negative sentiment or impact on trust.

- Stakeholders can include customers, partners, employees, regulators, or analysts
- Brand values can include quality, safety, sustainability, security, reliability, or exclusivity
- Reputation risk scenario categories might include unethical behaviour, food safety, regulatory breach, environmental incident, recall, leadership misdemeanour, cyber or health

We've seen some common characteristics among the most significant reputation risk events:

- They threaten to compromise the values, standards and beliefs that underpin an organisation and are important to its stakeholders
- They can be traced back to the actions or behaviours of the company, rather than being an industry issue
- They trigger negative sentiment in multiple stakeholder groups
- They interest (social) media
- They are seen as avoidable or poorly managed
- They have the potential for staggered, time-lagged impacts

The end product of this type of risk assessment can be a reputation risk register, which is a useful tool to stimulate a better dialogue on risks to reputation with the organisation.

Once we understand the most significant scenarios, we can use traditional bow tie methods to build out more detail on cause and impact. The fact that we are assessing reputation risk gives risk professionals an opportunity to model a wider range of data, such as sentiment analysis – i.e. tracking the volume or type of sentiment published about similar organisations following the defined peril.

The scenario itself can be costed out, using traditional Business Interruption and liability cost categories, as well as indicators more specific to a reputation event, such as crisis management, regulatory fines, contractual penalties and long-term erosion of market share. In our experience, risk assessment through this lens not only generates better insights on reputational risk events but often higher Maximum Foreseeable Losses (MFL's). This can help to focus the minds of executives on the value of pre-event risk mitigation, the importance of crisis preparedness and any gaps in existing insurance coverages.

A structured approach leads to positive outcomes

This case study shows how gaining a clearer and more in-depth understanding around the financial and stakeholder impacts on reputational damage can better equip an organisation to manage the risk.

Case study - major drinks manufacturer

The issue

Our client wanted to better understand the damage to their reputation and the impact it could have on their organisation. In particular, they were keen to undertake a deep dive into key causations, that could lead to severe reputational damage and financial exposure.

Our approach

We used our Reputational Risk Analysis methodology to help understand the organisation's key concerns. The approach consisted of the following stages;

Stakeholder Mapping

- Mapping the stakeholder landscape to understand how each risk could impact the organisation's critical stakeholders and identifying those which could lead to severe reputational damage

- Developing a foundation reputational risk register which would provide a list of causation risks that could lead to reputational damage and financial exposure

Bow-Tie Analysis

- From identifying the critical risks, we worked with the organisation to build a suitable scenario to identify the triggers and evaluate the breadth of impact

- We analysed multiple media platforms and social media channels to understand media coverage and consumer sentiment

Financial Costing

- To help quantify the costing scenario, we considered the impacts associated with risks materialising from a financial, operational and regulatory perspective – with the level of each impact categorised into a loss category

- Using the scenario impact analysis we were able to quantify the potential financial exposure, using Aon's Reputational Risk Costing Framework to assess all exposures across the loss categories

Result

The value of this approach enabled the topic of reputation to be discussed and managed in a structured way. From the initial engagement with us, the organisation gained a greater awareness of the impact of reputational risk on their organisation. They better understood the financial exposures and more importantly, gained a clearer and more in-depth understanding of where and how they could restructure their capital and investments to support the mitigation and management of reputation risk.

How Aon can help

We live in an era of unprecedented volatility. Trends around economics, demographics and geopolitics – combined with the rapid pace of changes in technology are converging to create a challenging new reality for organisations. This creates operational issues but also presents new and exciting directions to be explored.

Here at Aon, we recognise and understand the challenges you face. Our leading industry experts have worked in the FAB sector from small, local family-run firms to global manufacturers and across all links in the supply chains. We'll help you identify and mitigate risks in your business and if you do suffer a loss, we can help protect your reputation and get your business back up and running with the minimal amount of disruption. As a global risk partner, we work with insurers across existing and emerging markets to find innovative and seamless solutions.

We also support organisations to 'prepare for the unexpected' by reviewing and evaluating solutions that safeguard critical operational needs – along with the development and implementation of risk management and business continuity strategies. We can assess potential financial volatility as part of a risk review and explore specific business-related risk exposures not typically covered by traditional insurance programmes.

Our EMEA Food, Agribusiness and Beverage Industry vertical is a team of 40+ senior colleagues across the region, specialising in industry risk, including insurable, uninsurable and emerging risk. At Aon, we connect the capital to the risk by working with our clients to identify, assess, quantify, finance and manage risk.

About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

About Pentland Analytics

Pentland Analytics provides advanced analytics and advisory services to the executive management of the world's leading companies. The firm converts puzzling business questions into mathematical models and translates the output into clear, practical recommendations. The results inform strategic decisions and help to build clients' resilience, reputation and long-term owner value.

This paper constitutes information only and is not intended to provide advice. Professional advice should always be sought regarding insurance coverage or specific risk issues.

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