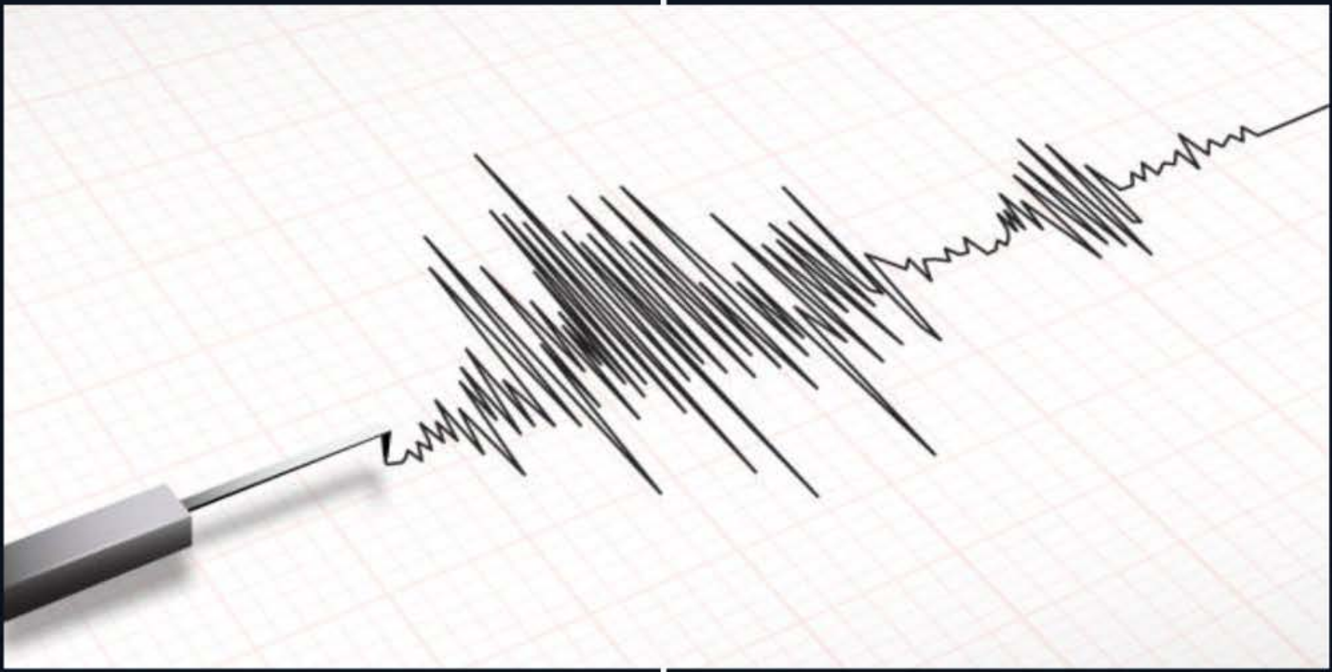
Leading Geopolitical Risk Management



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Impact of Geopolitical Risk

Geopolitical risk arises from actions or tensions involving state and non-state actors that disrupt established international relationships, particularly as the political and geographic foundations of those relationships evolve . The perceived intensity of geopolitical risk is increasingly influencing investment strategies and market behavior, as recognized by entrepreneurs, investors, and central banks . Organizations that systematically incorporate geopolitical risk management into their strategic risk management, business resilience, and business continuity planning are better positioned to anticipate potential impacts and implement proactive measures to mitigate adverse business consequences.

One of the defining features of the twenty-first century is the unprecedented level of connectivity among individuals, businesses, institutions, and states. This global interdependence means that developments beyond national borders, whether arising from trade and financial policy, geopolitical conflict, public health crises, or the rapid dissemination of information through digital channels, can disrupt domestic economic and social systems with a speed and scale unmatched than in earlier periods.

This interconnected world is the product of technological and institutional advances that emerged in the decades following World War II, including sustained periods of relative stability, the expansion of global trade under frameworks such as the General Agreement on Tariffs and Trade and its successor, the World Trade Organization, major improvements in transportation and logistics, and the advent of the internet. These developments delivered substantial gains in global living standards, as reflected in the long-term rise in per capita income worldwide.

Recent experience, however, has underscored that connectivity transmits not only economic opportunity but also systemic risk. Events such as the September 11 terrorist attacks, the global financial crisis, and the COVID-19 pandemic demonstrate how shocks can propagate rapidly across borders, amplifying their impact. In this environment, businesses can no longer treat geopolitical risk as external or episodic. Proactive identification and management of geopolitical risk is now a critical component of effective strategic planning, operational resilience, and business continuity.

Geopolitical risk manifests in several concrete forms. Macroeconomic shocks to the global economy, whether arising from cyclical downturns or more severe disruptions linked to financial or systemic crises, pose material risks to businesses and markets. Energy market volatility represents another prominent source of geopolitical risk, as fluctuations in oil and gas prices are often driven by geopolitical developments, including supply disruptions, strategic market interventions, and the effects of armed conflict on global energy production and distribution.

Cyber threats from both state- and non-state-sponsored actors continue to pose a significant risk to organizations. Cybersecurity threats illustrate how increased global connectivity and the speed of digital transmission, while enabling substantial economic and operational

[1] Dario Caldara and Matteo Iacoviello, "Measuring Geopolitical Risk," American Economic Review 112, no. 4 (2022): 1194–1225, https://doi.org/10.1257/aer.20191823.

[2] Ian Bremmer, The Geopolitical Risk Index, Eurasia Group, 2015.

benefits, have also introduced new and persistent vulnerabilities. The extent and nature of business impact from geopolitical risk vary by risk type, underscoring the need for organizations to tailor their risk assessment and response strategies.

Advocacy group initiatives and the actions of political and social activists are increasingly emerging as structural drivers of geopolitical risk. Their campaigns can accelerate regulatory change, strain diplomatic relations, disrupt cross-border operations, and exert sustained pressure on organizations navigating an interconnected and politically sensitive global landscape.

Organizational Leadership Approach to Geopolitical Risk Management

In a highly interconnected global landscape, geopolitical dynamics present material risks that can affect organizational performance, resilience, and long-term value creation. Organizations must therefore take a structured approach to understanding and optimizing these risks by addressing the following:

1. How likely are geopolitical risks to affect our operations and stakeholders?
2. What degree of geopolitical risk is acceptable in pursuit of our strategic objectives?
3. What risk mitigation, hedging, and resilience strategies should be implemented to manage potential exposures?

The following recommended approaches are designed to equip organizational leaders with the clarity, capabilities, and governance needed to effectively address these questions:

1. Geopolitical Risks Dimensions

Organizations should clearly define the dimensions of geopolitical risks and assess their implications for the execution of their strategic objectives. These risks should be systematically integrated into the organization's overall strategy and enterprise risk management framework, as geopolitical risks can materially affect strategic priorities, capital allocation, growth initiatives, human capital, operations, third-party relationships, technology, and more. Organizations should clearly define and align their geopolitical risk appetite with their strategic objectives, explicitly identifying which risks they are willing to accept to pursue value creation and long-term goals. The geopolitical risk assessment should be conducted multiple times throughout the year, driven by evolving global indicators, rather than confined to a rigid annual cycle.

2. Scenario Analysis & Simulation

Organizations should develop geopolitical scenario analyses grounded in the defined dimensions of their geopolitical risk assessments and informed by a clearly articulated risk appetite. Scenario analysis enables leadership to anticipate uncertainty, assess potential impacts, and make more resilient strategic decisions by illustrating how a range of plausible geopolitical outcomes could affect strategy, performance, and organizational resilience. By moving beyond single-point forecasts, this approach encourages leaders to visualize and evaluate multiple potential futures and their associated risks, strengthening preparedness and decision-making under uncertainty.

Scenario simulation goes beyond static scenario analysis by incorporating dynamic variables, interdeendencies, and escalation pathways, allowing leaders to assess second- and third-order effects. This approach supports more informed decision-making by identifying vulnerabilities, clarifying trade-offs, and strengthening preparedness before events materialize.

Organizations should implement geopolitical risk scenario simulation to dynamically assess how evolving geopolitical conditions could affect strategic objectives, operations, and financial performance, thereby strengthening decision-making, resilience, and preparedness. By running through a range of realistic geopolitical scenarios like trade tensions, tougher sanctions, regional conflicts, or shifting regulations, organizations can pressure-test their assumptions, see how strategies hold up, and explore response options before uncertainty turns into disruption.
Organizations should regularly test scenarios to validate preparedness and resilience against potential shocks.

3. Continuous Monitoring

Organizations should establish ongoing monitoring metrics to assess the impact of global threats on their operations and strategic objectives. These metrics serve dual purposes:

1. Help identify early warning signals and trigger mechanisms that allow leadership to preempt potential issues before they materialize.

2. Help with ongoing assessment to track and evaluate exposure to geopolitical risks once they occur.

Prioritizing metrics that enable proactive risk detection ensures that leadership is informed of emerging threats in real time, strengthening organizational resilience and decision-making.

4. Contingency & Response Planning

Organizations should develop robust contingency and response plans that convert risk insights, intelligence, and early-warning indicators into clear, executable actions. These plans should enable timely, coordinated decision-making when risk conditions change or materialize. This can be achieved by:

1. Developing structured playbooks and action plans aligned to predefined risk scenarios and trigger events, with clearly assigned roles, responsibilities, and escalation paths.

2. Establishing mechanisms that promote rapid activation, cross-functional coordination, and consistent execution, ensuring the organizations can respond effectively under pressure.

3. Utilizing advanced tools, actionable intelligence, and the right expertise to detect emerging risks before they materialize, empowering leadership to act decisively, strengthen resilience, and stay ahead of disruption rather than respond to it.

4. Embedding clearly defined risk appetite parameters into contingency and response plans to guide risk acceptance decisions, ensuring that exposure to geopolitical volatility is intentional, bounded, and aligned with the organization's strategic tolerance for uncertainty.

5. Governance & Oversight

Each of the organizational leadership approaches discussed informs critical elements of effective governance and oversight of geopolitical risk management.

Organizations should establish formal, clearly defined policies and procedures to govern the management of geopolitical risk.

These policies should articulate the organization's geopolitical risk posture and risk appetite; define the approach to identifying, assessing, and monitoring and mitigating geopolitical exposures and their implications; establish key metrics and reporting expectations; clarify roles, responsibilities, and decision rights; and specify the trigger events or market conditions that activate contingency plans and response actions. Supporting procedures should translate these policy expectations into actionable guidance, outlining how geopolitical risk management activities are executed consistently and effectively across the organization.

Geopolitical Risk Management

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