

Emerging Risk: An Integrated Framework for Managing Extreme Events

Dr. Kathleen Locklear, MBA, DM

Presented at the:
2011 Enterprise Risk Management Symposium
Society of Actuaries
March 14-16, 2011

Copyright 2011 by the Society of Actuaries.

All rights reserved by the Society of Actuaries. Permission is granted to make brief excerpts for a published review. Permission is also granted to make limited numbers of copies of items in this monograph for personal, internal, classroom or other instructional use, on condition that the foregoing copyright notice is used so as to give reasonable notice of the Society's copyright. This consent for free limited copying without prior consent of the Society does not extend to making copies for general distribution, for advertising or promotional purposes, for inclusion in new collective works or for resale.

Abstract

Today's complex, interconnected global environment has created borderless risk capable of rapidly spreading across geographic, societal and organizational boundaries. In this environment, extreme events compel greater attention due to their potential for generating expansive and catastrophic harm. One source of extreme events is emerging risk, which, as defined in this paper, is new (novel) risk that has not existed previously. Akin to the Black Swan as proposed by Nassim Taleb, emerging risk falls outside our customary cognitive and decision-making frameworks. This paper begins by exploring cognitive and behavioral theories that can be applied to explain why emerging risk is often overlooked, downplayed or ignored. The existing literature is also examined to identify approaches (including systems theory, scenario planning and anticipatory management) for enhancing our capacity to understand, identify and handle emerging risk. Finally, this paper proposes an innovative framework for managing emerging risk within an overall enterprise risk management (ERM) program. The suggested framework provides a practical approach for meeting the challenges of emerging risk, including the need for alternatives to traditional quantitative and predictive tools.

Keywords: Emerging risk; extreme events; trans-boundary risk; enterprise risk management.