

The University of Texas at Austin McCombs School of Business Managing International Risk RM 395.7, FALL 2011 Unique Number 04310 M W 2-3:30 PM GSB 3.138

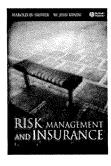
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Required Text: Risk Management and Insurance Perspectives in a Global Economy by Harold Skipper and W. Jean Kwon, Blackwell Publishing

Course Description

When we think of large risks faced by global companies, we often think in terms of natural hazards such as hurricanes, earthquakes, tsunamis, or tornados. Perhaps also manmade disasters come to mind—such as the terrorist attacks that occurred in the U.S. on September 11, 2001, or internet security breaches causing losses, or the BP Gulf oil spill, or the man-enhanced damages occurring in the nuclear power plant after the 2011 Japan earthquake and tsunami. Often overlooked however, are important systemic risk such as those brought dramatically to our attention by the financial crises, precipitated by the credit crisis of 2008. These types of man-made disasters have the potential to devastate the global marketplace and affect businesses worldwide. Losses in multiple trillions of dollars and much human suffering and insecurity are already tallied up, and some fear a slow recovery or even a double dip recession with the worst yet to come (although in fairness, some claim otherwise). Many observers consider this credit crunch, brought on by subprime mortgage lending and deregulation of the credit industry, to be the worst global financial calamity ever. Its unprecedented world-wide consequences have hit country after country, company after company—in many cases even harder than they hit the U.S. The world is now so fundamentally connected that past regional disasters can no

longer be contained locally. Risks are now intrinsically international. We can attribute the 2008 collapse to financially risky behavior of a magnitude never before experienced. Its implications dwarf any other disastrous events. The 2008 U.S. credit markets were a financial house of cards with a faulty foundation built by unethical behavior in the financial markets with ill designed risk management and reward structures. As we shall discuss, a basic lack of risk management (and regulators' inattention or inability to control these overt failures) lay at the heart of the global credit crisis. Companies and regulators ignored (and thereby increased) some major risks. The investment banking industry had inadequate risk recognition and management, and the impact was international. How was risk in this situation so badly managed? What could firms and individuals have done to protect themselves? How can government measure such risks (beforehand) to regulate and control them? These and other topics related to the management of international risks will be one of the subjects of this class.

This course will focus on considerations in, and influences on, international risk management. An important first step in this is the understanding of what we mean by risk and how people interpret it and make decisions in light of it. Accordingly, we will discuss basic risk and crisis management principles pertinent to multinational firms, including financial, legal and cultural cross-national differences that impact corporate risk management strategies; and specific multinational marketplaces (e.g., reinsurance markets, captive offshore insurance companies, foreign exchange markets, derivatives markets, etc.). These strongly affect the traditional US corporate structure and risk management process. Such topics as terrorism risk and security precautions will also be discussed from a business (as opposed to social) perspective. We shall consider the benefits associated with a firm having enterprise wide approach to risk management, as opposed to managing risks solely within functional area silos.

Briefly stated, there are five broad but integrated topic areas for this course.

- 1. The course will analyze the tasks, challenges, and obstacles facing the risk manager of a multinational firm or anyone else charged with obtaining a competitive "risk adjusted rate of return" on invested capital. In this we will discuss financial risk management as well as the quantification of risk and the psychology of risk.
- 2. We will examine the nature of risk management in different areas of the world, and the different nature of the risks faced in different areas.
- 3. The course is designed to provide awareness that economic, political, cultural, legal, and social systems affect the successful management of risks facing both people and organizations. This will entail discussions of such topics as political risk, terrorism risk, expropriation risk, export credit risk, differences in conditions insurance, foreign exchange rate risk, kidnap and ransom risk and insurance, and other risks.
- 4. Finally, as we have seen from the financial crisis, cross-border risk management is the future of the world faced by today's generation of managers. Particular attention will be give to the changing nature of risk management activities in an increasingly international arena, and the international nature of such risks as electronic security risks, financial risks, and environmental risk exposures faced by

- corporations. International economic concepts related to this goal will consequently be discussed. Outsourcing risk will be discussed here.
- 5. Financial concepts such as no arbitrage pricing and return on capital will be used to assess enterprise wide opportunities as well as enterprise wide risks. Enterprise risk management is the wave of the future, with AIG serving as the poster-child for what can happen when a company fails to implement risk management at the enterprise rather than the individual business unit level of operation (one unit of the company brought down the whole company).

Brief Summary of Lecture Topics

- 1. <u>A basic overview</u> of risk management and review of the history and importance of risk management activities to the global economy and corporate financial structure (Chapter 1, handout, and guest lectures).
- 2. <u>How the public perceives risk and risk communication</u> (Chapter 2, 4, and videos)
- 3. <u>Background on international economics & international trade concepts (Chapter 3)</u>
- 4. <u>The International Risk Environment</u>. This topic examines the settings that provide an opportunity for risk management services. Why an international perspective is important, major markets and international considerations are presented.
- 5. <u>The Structure of Risk Pooling and Insurance Internationally</u>. The nature and determinants of demand and supply for risk transfer internationally, the role of government and society. (Chapter 4)
- 6. Alternative Risk Financing Methods. (From Chapters 13, 14 and handouts)
- 7. <u>Governmental Intervention into Risk Transfer Markets</u>. Rationales for intervention, regulation, intergovernmental organizations, and taxation. New regulations in the aftermath of the financial crisis.
- 8. <u>Catastrophe Risk Assessment and Handling Catastrophic Risks.</u> This will include weather risk associated with global climate change, environmental risk, geological risks, and how to manage in preparation for and respond to such risks (From Chapters 5, 6 and handouts on crisis management)
- 9. <u>Global Risk Management for the Multinational Firm</u>. This topic examines the nature of risk management in a firm that operates in different areas of the world.
- 10. Enterprise Risk Management. (Chapter 12)
- 11. Political Risk (Chapter 17 and handouts)

Grade Determination

There are three major components of your grade, as shown below.

- Individual research paper—25%
- 2 Short answer and essay tests over lecture, assignments, guest lecturers material, and assigned readings—30% each
- Homework, class participation (15%). Attendance is part of class participation, and attendance will occasionally be taken. A (short) informal presentation of your research paper topic will be made in class.
- There will be no final

• Grades will be based on a plus-minus system using a curve. The curve in each assignment will be based on 100% minus the top actual score in the class. This amount will be added to each score.

Term Paper Description

The term paper will be on a topic of your choice related to managing risk in an international setting, or a comparison of risk handling in different international cultures or areas of the globe, or a case study in the management of international risk in an actual company or industry. The paper topic is not to be merely an "overview" or "encyclopedia" paper, but rather should address some issue of current interest or controversy (e.g., products liability exposure differences across the world and its impact on outsourcing viability, comparison of privatization of social security versus governmental based pension systems in developed countries, ethical issues associated with international contracting, the effect of intellectual property rights differences among counties and their impact on the competitiveness of the USA industries, risk related implications of the coming transition to international accounting standards, etc.). I have posted a list of potential topics to Blackboard, and I and will distribute examples of "A" papers from previous classes later in the semester. You may (and I encourage you to), however, choose a topic of your interest if you have one (e.g., you might choose kidnapping and ransom insurance if you have a particular interest in this, or the transition to international accounting standards (and the corresponding impact of this on risk disclosure) if interested in this, or pandemic risk management, or fraud detection, or military risk analysis issues).

The paper itself will be twelve to fifteen pages long (excluding the works cited page) with a minimum of eight references used and cited in the text. The bibliography must have majority of references which are from either academically valid journals or books, or from reputable newspaper magazines (Newsweek, Time, Business Week, etc., although these may be taken from the online versions). Unauthenticated internet sources are acceptable in some circumstances, but cannot constitute the bulk of your references, and it is your responsibility to check the truth of the statements found if not using a reviewed web-site.

Format, grammar and structure will count. There must be sectioning, paragraphs, etc. See a style manual such as MLA if you are uncertain as to style. The graduate writing center in Jester Hall or the undergraduate writing center in the Flawn Center will useful to you in completing this and I strongly urge you to use this resource.

Further Specifics on the Research Paper.

The paper should be written as an academic research paper, with titles, section headings, appropriate paragraphing, an introduction (stating your thesis), and a conclusion section. Margins should be reasonable (1 inch), and a 10-12 point font used. Look to your cited references for a format template. The *Journal of Risk and Insurance* format is a very appropriate format to emulate.

<u>Plagiarism will not be tolerated.</u> Any borrowed ideas, quotes or figures used in the paper must be referenced by authors' last names and year of publication. For example,

"RIDITs represent a very old idea and are closely related to distribution free methods" (Bross 1958, p19). If you turn in a paper without proper referencing, you will be severely marked down (at least one letter grade e.g., an A to an A-). The references in the reference section are to be listed alphabetically by last name of the first author. Examples are given below.

Books

One author:

Koerner, Joseph Leo. 1993. *The Moment of Self-Portraiture in German Renaissance Art.* Chicago: University of Chicago Press.

More than one author:

Cowlishaw, Guy, and Robin Dunbar. 2000. *Primate conservation biology*. Chicago: University of Chicago Press.

Editor(s) or compiler(s):

Panjer, Harry H., eds. 1998. Financial Economics: With Applications to Investments, Insurance, and Pensions. Schaumburg, Ill: The Actuarial Foundation.

Company or organization as author:

Blue Cross and Blue Shield of Michigan (BCBSM). 1987. "Participating Hospital Agreement." Detroit: BCBSM. [Citation in text would read: (BCBSM 1987)] U.S. Prospective Payment Review Commission (ProPAC). 1991. *Annual Report to Congress*. Washington, DC: U.S. Government Printing Office. [Citation would read: (ProPAC 1991)]

Parts of books (articles in an anthology, chapters, introduction, etc.):

Twaddell, W. Freeman. 1957. A note on Old High German umlaut. In *Readings in linguistics I: The development of descriptive linguistics in America*, 1925-56. 4th ed. Edited by Martin Joos. Chicago: University of Chicago Press.

Journals

Brown, Robert L., Robin Damm, and Ishmael Sharara. 2001. "A Macro-economic Indicator of Age at Retirement," *North American Actuarial Journal* 5(2): 1-10.

• Magazines and Newspapers

With an author:

Cynthia Schreiber, "Overture, EarthLink Decline in New-Stock Selloff," *The Wall Street Journal*, 11 July 2003, Money and Investing section.

Without an author:

Euroweek. 1997. "CSFB, Winterthur Storm Swiss CB Sector with First Catastrophe-Linked Bonds," (Jan. 17): 5.

• Working Papers, Technical Reports, and Ph.D. Dissertations:

Amundin, M. 1991. Click repetition rate patterns in communicative sounds from the harbour porpoise, *Phocoena phocoena*. Ph.D. diss., Stockholm University.

• Personal Communications:

Rich, Colonel William. Interview by author. Tape recording. Boston, Mass., 3 March 2001.

Online References (use date citation was found):

Individual Life Insurance Experience Committee (ILFEC). 2001. "Report of the ILFEC: Mortality Under Standard Individually Underwritten Life Insurance

between 1990 and 1991 Anniversaries," *Transactions of the Society of Actuaries*. Online at http://www.soa.org/research/91ilreport.html.

Note: When quoting material from another publication, you must include the page number(s) of the quote in the citation (Smith 2001, p. 20). You must have references in the body of the paper. Every paper in the references should appear in the text, and vice versa.

I will check for plagiarism!!!

Academic Dishonesty

The McCombs School of Business has no tolerance for acts of scholastic dishonesty. The responsibilities of both students and faculty with regard to scholastic dishonesty are described in detail in the Policy Statement on Scholastic Dishonesty for the McCombs School of Business:

By teaching this course, I have agreed to observe all of the faculty responsibilities described in that document. By enrolling in this class, you have agreed to observe all of the student responsibilities described in that document. If the application of that Policy Statement to this class and its assignments is unclear in any way, it is your responsibility to ask me for clarification. Policy on Scholastic Dishonesty: Students who violate University rules on scholastic dishonesty are subject to disciplinary penalties, including the possibility of failure in the course and/or dismissal from the University. Since dishonesty harms the individual, all students, and the integrity of the University, policies on scholastic dishonesty will be strictly enforced. You should refer to the Student Judicial Services website at http://deanofstudents.utexas.edu/sjs/ or the General Information Catalog to access the official University policies and procedures on scholastic dishonesty as well as further elaboration on what constitutes scholastic dishonesty. If you use words or ideas that are not your own you must cite your sources. Otherwise you will be guilty of plagiarism. Plagiarism is considered to be academic dishonesty. Examples will be given in class.

Class Web Sites and Student Privacy

In order to keep you appraised of all course information easily, and so you can monitor your test results quickly, this class will use a Blackboard Website. To access the site, go to http://courses.utexas.edu. The site is password-protected. You will be asked to enter your UTEID to enter. Alternatively, enter UTDirect and follow the links for Academic Services and Course Web sites. The syllabus and project information will be posted to Blackboard, http://courses.utexas.edu/, under "Assignments". In addition, test grades will be posted to Blackboard so that at any point in the semester you can access your current grade status. Other site activities could include exchanging e-mail, engaging in class discussions and chats, and exchanging files. Class e-mails will also be sent to you through Blackboard to update any class information, including guest speakers. Therefore, it is very important that you maintain correct, current email information with the University, as it is your University information that Blackboard uses. It is your

responsibility to check your e-mails in a timely manner and check Blackboard for new postings. Your professors cannot update your UT e-mail. You must do that directly with UT, and if your e-mail is not current with UT centrally, you will not get updates and certain class handouts before class since class e-mail rosters are a component of the site. Students who do not want their names included in this electronic class roster must restrict their directory information in the Office of the Registrar, Main Building, Room 1. For information on FERPA related issues see

http://registrar.utexas.edu/students/records/ferpa/ The following link provides the complete University policy on the use of e-mail.

http://www.utexas.edu/its/policies/emailnotify.html.

Students With Disabilities

The University of Texas at Austin provides upon request appropriate academic accommodations for qualified students with disabilities. For more information, contact the Office of the Dean of Students at 471-6259, 471-4641 TTY.

Cell Phones and Computers.

Cell phones must be put away during class and computers may be used only for note-taking. Students who use gizmos for non-class related activities may be marked absent and asked to leave for the remainder of that class as the class discussion is an important component of the learning experience.

Religious Holy Days

A student who will miss classes or other required activities, including examinations, for the observance of a religious holy day should inform me as far in advance of the absence as possible, so that arrangements can be made to complete any missing assignment within a reasonable time after the absence.

Managing International Risk Day by Day Schedule Dr. Patrick L Brockett RM 395.7

Fall 2011

You are to have prepared the assignment listed below for a given day prior to coming to class (except for the first day). You may be called on at random in class discussion and there will be occasional in-class group discussions. All assignments for a given day are due at the start of class. Please read the textbook material before coming to class, so you will have a frame-of-reference for the in-class discussions and material.

NOTE: The following schedule is subject to change depending on circumstances (e.g., guest lecturer availability on certain days)

DATE	LECTURE TOPIC	ASSIGNMENT
Wednesday, August 24	Introduction to the Course, Hand out the syllabus. Very short class	READ Chapter 1 and "Risk History Primer" for next class period
Monday, August 29	Guest Lecturer: Risk Management Professor Patricia Arnold, The nature of risk, introduction to Risk Management techniques and practices, steps in the risk management process	READ Basics of Risk Management paper posted on Blackboard. Start work on the future of risk in property insurance handout assignment (posted to Blackboard)
Wednesday, August 31	Guest Lecturer: Risk Management Professor Patricia Arnold, More on the nature of risk and risk management techniques and practices	Continue working on the future of risk in property insurance handout assignment. Start investigating what topic to choose for your research paper
Monday, September 5	No Class September 5 th — Happy Labor Day!	Read Chapter 4 p. 101-108, Read p. 281- 283
Wednesday , September 7	No class. Use this time to do research related to two things: Answering the Assignment questions, and selecting a research paper topic for your class research paper	Do internet research on the two assignment questions concerning the social medial impacts on the future of the property and casualty and financial services industries, and to do research investigating what term paper topic to select. Please email me with any questions
Monday , September 12	Perceptual Dimensions of Risk: how the public perceives risk. Discussion of Research Paper. Discussion of cyber- risk for corporations, social media risk and m-commerce risk	READ Chapter 3. Select a topic for your research paper. Read handouts on cyber risk management for enterprises and on m-commerce risk
Wednesday, September 14	Background on International Trade and International Economics	TOPIC OF RESEARCH PAPER DUE IN CLASS AND BY EMAIL

Monday , September 19	Causes and Perceptions of the Global Economic Crisis and its Impact on International Risk.	READ Chapter 5
Wednesday , September 21	Catastrophic Risk Assessment: Natural hazards	READ Chapter 6
Monday, September 26	Catastrophic Risk Assessment: Human risks:	READ Chapter 15
Wednesday, September 28	Managing Catastrophic Risk	Study for Exam 1 (covers all material up to end of class 9/29)
Monday, October 3	EXAM 1	READ Chapter 12
Wednesday, October 5	Go over exam. Introduction to Enterprise Risk Management	READ Chapter 13
Monday , October 10	Enterprise Risk Management- Internal loss financing	Abstract of paper and 5 reference citations due in class and by email. READ Chapter 14
Wednesday, October 12	Enterprise Risk Management- External loss financing	READ Chapter 17
Monday, October 17	Political Risk, expropriation and nationalization risk	READ handouts on political risk and kidnapping and ransom insurance
Wednesday, October 19	More on political risk, kidnapping and ransom insurance	READ chapter 18
Monday, October 24	Intellectual property and technological risk	READ Chapter 19
Wednesday, October 26	The role of insurance and risk pooling in the global handling of risk	READ Chapter 23
Monday, October 31	Reinsurance, and global insurance market brokers	READ Chapter 24
Wednesday, November 2	Government Regulation of Risk and Insurance	Study for Exam 2 (covers all material up to end of class 11/3)
Monday, November 7	EXAM 2	
Wednesday, November 9	Supply Chain Risk Management	READ Chapter 25
Monday, November 14	Financial Services Integration	Finish research paper
Wednesday , November 16	RESEARCH PAPER DUE. Student Presentations of Research papers	
Monday , November 21	Student Presentations of Research papers	
Wednesday, November 23	Student Presentations of Research papers	Happy Thanksgiving!
Monday, November 28	Student Presentations of	

	Research papers	
Wednesday, November 30	Course Finale & Wrap-up The Future of Global Risk Management (Required Attendance) Happy Holidays!	NO FINAL EXAM Happy New Year!