

Augusto Pérez Arbizu

GRUPO TELEFÓNICA RISK AND
INSURANCE MANAGER

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In Telefónica, they share the view that the risk manager plays an important role, a function in which innovation is a key factor. The Grupo Telefónica Risk and Insurance Manager feels that “we should be in a position to provide imaginative solutions for the analysis, evaluation, mitigation and financing of new risk”.

Risk and Insurance Management (hereinafter, R&IM): How would you rate Telefónica's level of tolerance to risk?

Augusto Pérez Arbizu (hereinafter 'A.P.A.): The Company has a reasonable level of tolerance to risk or 'acceptable risk', understanding these concepts to be its willingness to assume a certain level of risk, insofar as this enables the creation of value and the development of business while achieving a suitable balance between growth, performance and risk.

To this end we have made a commitment to active management in the face of identified risks, always depending on the nature of the same, by taking comprehensive action on the impact and probability of them occurring.

R&IM: What are the main features of the corporate risk management model implemented in Telefónica?

A.P.A.: The participation of agents in the identification, evaluation, management and reporting of risk is a vital part of the risk management process in Telefónica, as this enables them to take full advantage of their knowledge in their respective areas of competence.

“We have made a commitment to active management in the face of identified risks by taking comprehensive action on the impact and probability of it occurring”

First of all, we have the Risk Management function (ERM) which is headed by Internal Audit from which the procedure enabling the generation of the Group risk registry and map is managed. And

then we have the Insurable Risk function which our Area represents. We apply a procedure for the identification, evaluation, reduction and financing of these risks.

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Even though the scope, and above all the methodology, of these two functions is very different, in Telefónica we feel that the feedback between both Areas is quite valuable, and so the degree of collaboration is excellent.

RISKS WHICH ARE MORE DIFFICULT TO MANAGE

R&IM: Risks of a Business, Operational, Financial, Global nature... Which of these risks are the most difficult to keep under control?

A.P.A.: Generally speaking, those risks which depend more on external factors and agents are more difficult to manage than those arising from the internal operations of the company itself, as is the case in areas like regulation or the macroeconomic and social environment of the countries where we operate.

For affairs which are of a more 'internal' nature, such as operational risks which may affect our infrastructures for example, although they may sometimes be rather complex, we have more mechanisms and information enabling us to deal with them effectively.



R&IM: In Telefónica, which units take part in the insurable risk management process both at the corporate and local level?

A.P.A.: Corporate Risk and Insurance Management comes under Telefónica S.A. Corporate Finances. Corporate Center), specifically within the Risk and Insurance Treasury Division. This Division manages a series of companies linked to the insurance area which provide us with the necessary resources for undertaking the function.

First of all, we have our surety reinsurance company, Casiopea RE, strongly capitalized and given an A rating by AM Best, which gives us a high capacity for the retention and mutualization of Group risks, as well as direct access to the international Insurance and Reinsurance market. This is an extremely important tool for designing Corporate Insurance

Programs, since it provides great flexibility for achieving optimum costs at each stage of the market cycle and for adapting coverage to Group requirements.

Furthermore, we have Pléyade Peninsular, our insurance and reinsurance broker, with its subsidiaries in four Latin American countries. A great team which enables us to undertake most of the activities corresponding to the Area and reach all the companies within the Group. Its activities include the following: the implementation of corporate insurance programs and policies, the need for local insurance, risk engineering, support for Casiopea in the design and negotiation of corporate programs, offering insurance for employees, etc.

“Thanks to Casiopea and Pléyade, a Risk Management unit can be converted into a unit with revenue and a statement of income”

Thanks to Casiopea and Pléyade, a Risk Management unit which is traditionally a purely cost center can be converted into a unit with revenue and a statement of income. However, revenue growth has never been sought at the expense of premiums paid by the Group, since the objective has always been to optimize value added in matters of Risk Management, which we measure every three years based on independent third parties.

R&IM: The Group has Multinational Insurance Programs. What are the main features of these programs?

A.P.A.: We have been using our surety to design our programs for more than 25 years. So over this long period of time we have accumulated maturity and experience, specialization and knowledge of

our risks, as well as a well-capitalized surety and a great capacity for retention. For this we can usually provide an excellent response to the market in order to follow Casiopea in periods of excess, when we can introduce new coverage and growth over that already existing.

Furthermore, we make maximum use of the potential and try to innovate continuously. Our programs are not static, but evolve constantly in order to adapt as well as possible to Group requirements and to be at the forefront of the insurance market or even one step farther forward.

Another feature of our programs is that they are multilinear. So for example, All Risk, Cyber and Crime coverages are grouped together in a single insurance contract for each subsidiary/country, the local insurance company assigns 100 percent to Casiopea and then we roll back to the reinsurance markets with different retentions. This considerably simplifies management with the Group's subsidiaries and enables us to be more flexible when assigning and distributing costs, while at the same time complying with internal policies and regulations with regard to transfer prices.

COVERAGE PROBLEMS

R&IM: Are you having any problems finding coverage for some risks?

A.P.A.: If you are referring to regular and traditional coverage, this is not the case at this time. We have no problem finding capacity in the market under competitive conditions. However, if you are referring to non-traditional coverage or new coverage for emerging risks then this is logically quite another story.

In these cases it is always difficult to find a response, as it was to get Cyber coverage for the Group in 2008 before supply matured. Three years ago

we managed a certain degree of coverage for reputational risk. We would like to extend it, but at the moment only one company is prepared to provide capacity in excess of the retention of the Surety: We have also been trying for some time to get Multiline Stop Loss protection for Casiopea, but so far without much success.

R&IM: Telefónica's international presence has enabled it to diversify its activity in different countries and regions... But how does this affect you in terms of risk? In geographical terms, where are the greatest challenges for your Department?

A.P.A.: We have a presence in 22 countries, in most of which we occupy first or second place in the market and the Operator has dozens of satellite subsidiaries. To be able to reach every single one of the Group's subsidiaries, Pléyade plays a vital role in Corporate Risk and Insurance policy. Pléyade Peninsular not only serves Spain, but also provides free services for Germany and the United Kingdom. In the other countries, brokerage provides a response, either through its Latin American subsidiaries (Argentina, Chile, Brazil and Mexico) or via agreements with local brokers.

One of the greatest challenges is political risk. We have a Political Risk Insurance Program, although with the exception of coverage for Political Violence and Terrorism, we understand that market response is not very significant for risk such as that of Telefónica. Furthermore, the strict regulation of the insurance industry is another challenge from the standpoint of our Multinational Programs. Logically, this affects us throughout the Latin American region.

Finally, other challenges are the maintenance of coverage for Natural Hazard Risk in certain especially exposed countries (Chile, Peru, Venezuela, Ecuador, etc.); and the risk of collective actions in countries like Brazil, Argentina and Chile.

R&IM: What is the role of Telefónica Insurance in the management of the Group's risks?

A.P.A.: Currently its role in the management of the Group's risks is practically non-existent. Telefónica Insurance was created in 2005, with the aim of providing an issuing service for our programs, first in Spain and subsequently in Europe, because in accordance with legislation in Luxembourg, which is where Casiopea Re has its legal headquarters, a reinsurance company cannot undertake direct insurance activities.

At that time we were unsure about the efficiency and capacity of the response the market could provide. After a few years we started to develop the insurance business for the Group operators' client base, especially the mobile insurance, and we soon discovered that underwriting all our operations in Europe via Telefónica Insurance made good sense and we opened branches in the UK, Germany and Spain to work in free establishment.

At the same time we were able to confirm that large, multinational insurance groups were developing a much more efficient and flexible response for the issue of multinational programs. In short, we realized that Telefónica Insurance added ever more value to the Group for the development of the insurance business and less as a direct insurance company for our multinational programs. Nowadays, Casiopea is concerned exclusively with corporate programs, while Telefonica Insurance does the same for the development of the Group's insurance business.

R&IM: In your opinion, how will Brexit affect the European insurance market?

A.P.A.: It is still a little too soon to forecast. In the worst case scenario, insurance companies domiciled in the UK may lose their European passport and vice versa, and we assume that the large multinational insurance groups will look for the quickest and most efficient solution in order to continue providing services for their clients, be that by working in reinsurance, or transferring underwriting undertaken in London to other subsidiaries within the EU. It has been suggested that Dublin could compete with the London market.

Nevertheless, I am more concerned with the difficulties that we could have in maintaining the activities of Telefónica Insurance's British branch, which has a current premium volume of nearly 100 million Euros in O2 UK Mobile Insurance. Finally, beyond the effect on the insurance market, the main concern about Brexit is regarding the impact it will have on O2 UK which is such an important asset to Telefónica.

NEW BUSINESS AND RESULTS

R&IM: In the line of developing new insurance business, you recently launched insurance covering cyberbullying and identity theft, how is this being received?

A.P.A.: Telefónica Insurance's strategy is indeed to develop the insurance business, not only via Mobile Insurance, but also via products which are innovative, digital and/or related to Telefónica's services.



From a commercial point of view it is still too soon to be able to appreciate the degree of acceptance. The pilot phase of the product has been launched and we're still finalizing the platform's optimum performance before undertaking a mass launch. We're also analyzing which will be the most appropriate distribution formulas and channels for this product (retail channel, wholesale distribution, bancassurance, etc.). We're hoping to be able to make some kind of interesting launch for the Christmas campaign.

R&IM: At a business level, are companies becoming more aware of the technological risk they are facing?

A.P.A.: Indeed they are. This isn't something new. Cyber risk already went beyond being an 'emerging risk' some years ago and it is now the subject of profound analysis in the risk map for any important company. It may well be that awareness of this risk has fallen behind to a certain extent in small and medium-sized businesses due to their limited resources, both at the system and information security level and that of risk management.

Quite another matter is the demand for cyber-risk insurance by companies which in my opinion is holding back more than expected, in spite of the fact that supply in this field is already quite abundant. I

believe that in this area there are still some barriers which the risk manager needs to overcome. In short, the areas involved in the management of this risk need to be aligned (Systems, Information Security, Legal, etc.) and the company's Senior Management convinced of the need to establish a budget for the purchase of this new coverage.

“Demand for cyber-risk insurance by companies is holding back more than expected, in spite of the fact that supply in this field is already quite abundant”

Nevertheless, I am in no doubt that this trend is unstoppable. Companies depend more and more on digital assets, systems and networks for undertaking their activity and traditional insurance covering material assets will have less significance for the protection of their equity and their statement of income.

R&IM: In June you were appointed Chairman of IGREA for the next three years. What do you hope to achieve during your term of office?

A.P.A.: The Board of Directors has had a period of reflection on what will be the upcoming challenges for IGREA and we have some idea of the direction we would like to take. IGREA would like to progress in another of the objectives defined in its statutes: to become a representative body for companies in their capacity as risk managers and insurance purchasers before institutions and the insurance market.

For this purpose, it has been decided to create a consulting Advisory Board for the Association's Board of Directors, made up of prominent professionals with a long, productive career in the exercise of Risk Management and who to date do not hold a management position in one of the companies within the sector. This Board will issue non-binding rulings on whatever matters are submitted to them by the Board of Directors.

R&IM: What position do risk managers currently hold in companies and what will be their place in the future?

A.P.A.: I believe that the status of risk managers in the company is in excellent health. The dramatic acceleration in change which we are now experiencing due to multiple factors: new technologies, globalization, climate change, economic cycles, geopolitics, etc. means that this profession is more dynamic than ever. The lifecycle of companies is becoming ever shorter and our profession may be able to play a key role in their survival and even become part of their competitive advantage.

“The dramatic acceleration of change we are now experiencing makes the risk manager’s job more intense than ever”

In the case of Telefónica, we confirm daily that it is becoming more and more important to explain to the Telecommunications Regulator, the Stock Market Commissions in the countries where shares are quoted, in M&A processes, etc., the risks to which the company is exposed, together with the risk control and management mechanisms, logically including the insurance programs currently in force. This environment means that Risk Management is becoming more and more important in companies. A trend that will continue in the future.

“As telecommunications is a strictly regulated sector, the greatest challenge is political and regulatory risk”

In recent years we have also witnessed the birth and consolidation of the ERM in most of the companies quoted on the Stock Exchange. However, for risk managers and the insurance industry to maintain this important role, innovation is vital in order to respond to the ongoing growth of risk for companies, companies whose activity depends more and more on intangible assets like branding, workforce talent, change management, etc. Between us all (risk manager, insurance companies, brokers, appraisers, etc.) we should be capable of providing imaginative solutions for the analysis, evaluation, mitigation and finance of new risks. ■

“THERE ARE ALWAYS NEW RISK MANAGEMENT PROJECTS ON THE TABLE BEFORE US”



Augusto Pérez Arbizu joined Telefónica in 1997 as Corporate Business Manager for Pléyade Peninsular, the Telefónica Group Insurance Brokerage. He already had previous experience in the insurance industry as Regional Technical Supervisor in the Vitalicio Group and in Baloise. He soon began to extend his responsibilities beyond attending to the business of the Group's subsidiaries in Spain, with frequent trips to Latin America and a greater participation in the Group's multinational programs.

In 2005 he was appointed Corporate Programs Manager, taking full responsibility for these programs, which meant not only the design and negotiation of coverage with the market, but also for the policy for underwriting and retention in reinsurance surety. Three years later, he took a further qualitative step forward after the decision to implement a new line of activity: to sell insurance to third parties, given the potential of the client data base and the Group's distribution capabilities. He thereupon became the Insurable Risk and Product Development Manager.

Finally, in 2014, he was appointed Corporate Risk and Insurance Manager. In addition to the aforementioned technical, operative and business development responsibilities, he was now also responsible for the management of different insurance companies within the Group. He is currently on the Board of Directors of Casiopea Re, Telefónica Insurance and Grupo Pléyade.

After nearly 20 years of involvement with Telefónica's Risk and Insurance Area, Augusto Pérez Arbizu still has a role to play, because “the risk management function is so intense and dynamic”. “Furthermore”, he adds, “Telefónica gives great importance to this matter, as shown by the volume of resources it allocated to this end. These resources, together with the confidence shown and the freedom of action the company has always given me, enable us to be very creative and innovative in the design and structure of our insurance programs. We are not restricted to simply renewing the programs. There are always new risk management projects on the table before us”.

We should also highlight the Telefónica Insurance's great potential. “We are currently working on some very interesting projects, some of which you'll be finding out about over the coming months”.

“Our insurance programs are not static, but evolve constantly to achieve the best possible adaptation to the Group's requirements”