
Proposal for the development of a Meta-Risk Index

Professor Michael Mainelli FCCA FCSI FBICS
Executive Chairman, Z/Yen Group Limited
michael_mainelli@zyen.com

Background

Globally, organisations are increasingly focusing on the management of risk. While organisations attend to the day-to-day work of improving performance and results, they are increasingly exposed to criticism for not controlling the volatility of performance, i.e. more consistent results. Globalisation plays a part in increasing volatility – more fluid capital markets lead to rapid adjustments in value, worldwide news affects perceptions of local firms, foreign political events change staff attitudes towards work abroad or investment. Risk management starts with information about risk, yet there is no widely accepted global risk measure or index.

Proposal

A global risk index would be used by organisations to provide an indicator of the likelihood and severity of potential change in various regions (probably regions within countries). The risk index would be an important input to investment or disinvestment decisions. It might also be an important input to decisions on suppliers, staff hardship allowances or perhaps even foreign aid. There are a number of risk indices, largely tailored to the type of decisions for which they might be used, e.g. oil or banking. Risk indices, in a broad sense this also includes rating agencies, are provided by organisations such as Control Risks, the Economist Intelligence Unit, Standard & Poors, Moody's and various insurers. However, it does not appear that any of these indices is widely used or highly regarded. One of the basic problems is that there has been no external confirmation of their predictive ability.

Z/Yen, the UK's leading risk/reward manager, believes that a meta-risk study might lead to a useful, commercially beneficial, meta-risk indicator. A meta-risk indicator would, rather greedily, consume almost any risk measure available from any credible source, weight them appropriately based on their contribution to predicting problems and then prepare an overall weighting for use by decision-makers. The beauty of a meta-risk indicator is that it can respond to mis-weightings and new information sources (e.g. a new corporate social responsibility risk such as "canopy grown coffee") without invalidating itself, unlike a narrow risk measure used only by the oil industry, such as "offshore development risk." Z/Yen has considered such a study for some time, probably using a proprietary multi-variate prediction tool, Auguri.

A meta-risk study might well be a first step to a meta-risk index.

Next Steps

This note is designed to initiate conversation. Z/Yen is interested in exploring these issues further with all parties. Please contact Michael Mainelli, Director, Z/Yen Group Limited, Michael.Mainelli@zyen.com