Executive Perspectives on Top Risks 2023 & 2032

Operational issues are top priorities for the Energy and Utilities industry group in 2023 and 2032

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The level of uncertainty in today's global marketplace and the velocity of change continue to produce a multitude of potential risks that can disrupt an organization's business model and strategy on very short notice. Unfolding events in Eastern Europe, changes in government leadership in several countries around the globe, escalating inflation, rising interest rates, ever-present cyber threats, competition for talent and specialized skill sets, continued disruptions in global supply chains, rapidly developing technologies … these represent just a sampling of the complex web of drivers of risks that may threaten an organization's achievement of its objectives. Uncertainty and risk are here to stay. Keeping abreast of emerging risk issues and market opportunities is critical to improving organizational resilience.

The need for robust, strategic approaches to anticipating and managing risks cannot be over-emphasized. Boards of directors and executive management teams who choose to manage risks on a reactive basis are likely to be left behind those who embrace the reality that risk and return are interconnected and recognize the benefits of proactively managing risks through a strategic lens. Those leaders who understand how insights about emerging risks can be used to navigate the world of uncertainty nimbly increase their organization's ability to pivot when the unexpected occurs. That can translate into sustainable competitive advantage.

In this 11th annual survey, Protiviti and NC State University's ERM Initiative report on the top risks on the minds of global boards of directors and executives in 2023 and over the next 10 years, into 2032. Our respondent group, which includes 1,304 board members and C-suite executives from around the world, provided their perspectives about the potential impact over the next 12 months and next decade of 38 risk issues across these three dimensions:[1]

- **Macroeconomic risks** likely to affect their organization's growth opportunities
- **Strategic risks** the organization faces that may affect the validity of its strategy for pursuing growth opportunities
- **Operational risks** that might affect key operations of the organization in executing its strategy

[1] Each respondent rated 38 individual risk issues using a 10-point scale, where a score of 1 reflects "No Impact at All" and a score of 10 reflects "Extensive Impact" to their organization. For each of the 38 risk issues, we computed the average score reported by all respondents.

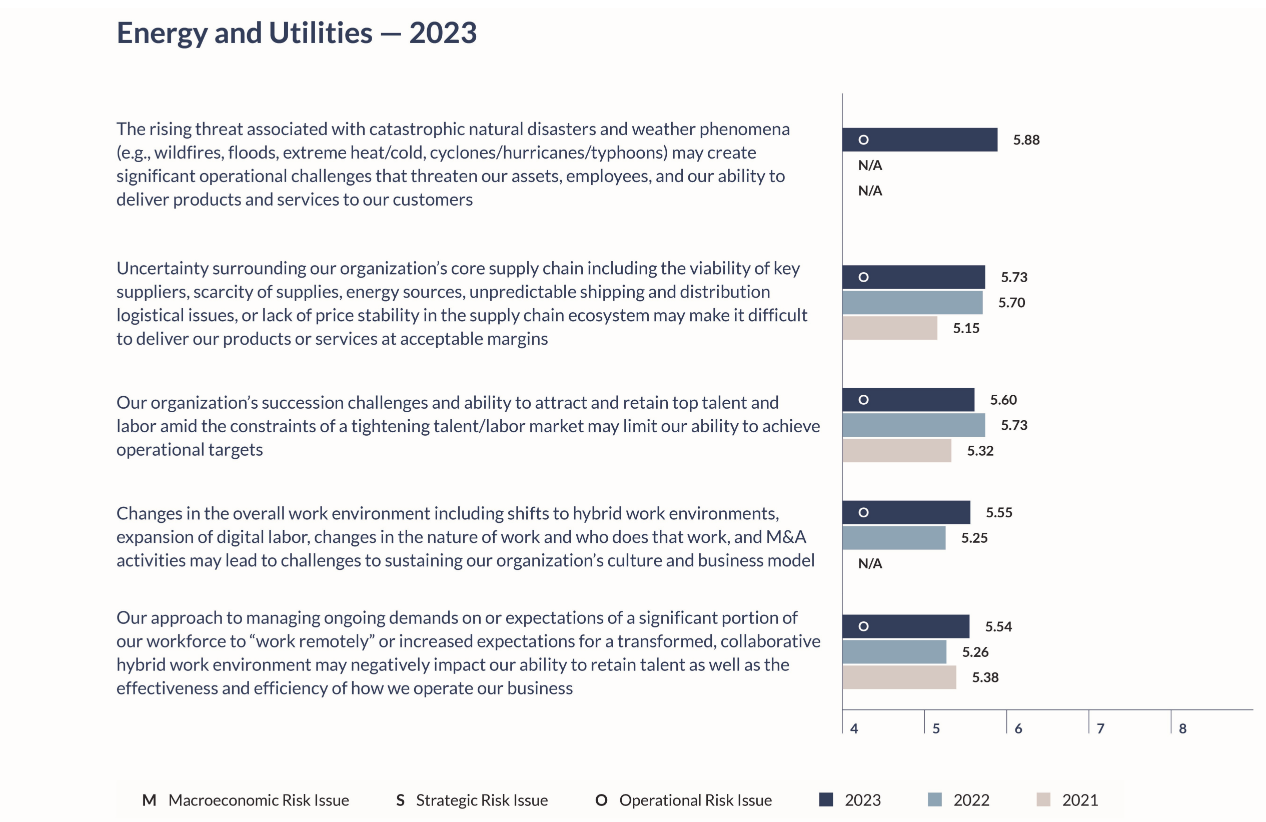
Commentary — Energy and Utilities Industry Group

Operational issues are the priority focus for energy and utilities executives in 2023 as they seek to guide their organizations through a time of significant transition and growth for the industry. Many of these companies are under intense pressure to modernize their operations, amplify innovation — while still supporting existing programs and adopt new business models to meet the rapidly rising demand for energy services (including renewable energy solutions) driven by population growth, electrification and other trends.

Increased confidence about meeting regulatory challenges

In our 2022 survey, the top five risks for the energy and utilities industry were also operational. But the 2023 list is markedly different from the 2022 list with regard to regulatory risks. The 2023 results did not include risks related to governance and sustainability issues, which were among the top five in 2022. In fact, they don't even rank among the top 10. This shift is likely due to industry leaders feeling more confident that their companies can respond promptly and effectively to intensifying and evolving regulatory demands — at least in the near term. ("Regulatory changes and scrutiny" ranks seventh among the industry's top risks for 2032.)

Many energy and utilities companies have spent the past year, or even longer in some cases, looking inward to determine how they can be more resilient and agile overall. Improving management of regulatory risks has been part of that effort. We've also seen leading companies ramping up their monitoring and compliance efforts to meet increasing environmental, social and governance (ESG) demands. Those efforts have improved their ability to respond to future regulatory changes, including climate-related disclosures, and their executive leadership no doubt recognizes that.



Eyes on the sky: worries about extreme weather threats

Energy and utilities executives may be worrying less about climate change policies, regulations and expanding disclosure requirements, but they are very concerned about their companies facing operational challenges due to extreme weather threats. Ranking first on the list of top risks for the industry in 2023 and 2032 is a new addition to our survey: "The rising threat associated with catastrophic natural disasters and weather phenomena may create significant operational challenges that threaten our assets, employees, and our ability to deliver products and services to our customers."

While this risk isn't in the top 10 list for the overall survey results for either 2023 or 2032, it's understandable why it ranks as the number one concern for energy and utilities firms for the year ahead — and for the next decade. Extreme weather events around the globe are taxing, disrupting and, in many cases, outright destroying critical energy infrastructure, including renewable energy infrastructure. These events can impact energy companies' operations in other ways, as well, from preventing essential staff from reaching critical worksites to sidelining company communications.

Research shows that 83% of major power outages between 2000 and 2021 were attributed to extreme weather.[2] And 2022 delivered plenty of extreme weather events that disrupted the delivery of energy services to millions of people or otherwise strained energy supplies, including Hurricane Ian and its 15-foot storm surge in Florida, a powerful derecho that impacted nearly half of Canada's population, and a summer drought and series of heat waves in Europe.

A complex and persistent issue: supply chain fragility

Supply chain risk emerged as a top five concern for energy and utilities executives in our 2022 survey, and it remains firmly in the second spot on the 2023 list. As we noted in our previous survey report, the energy industry is especially vulnerable to supply chain risk given that its value chain is highly service-, feedstock-, parts- and equipment-oriented. Many organizations run lean inventories as a strategy to balance out operational costs. Increased globalization and reliance on third parties are also contributing factors to supply chain fragility for energy companies.

Additionally, there are lingering issues from the pandemic that hinder supply chain operations for energy and utilities businesses, including longer delivery times and constrained supplier capacity due to pent-up demand. Supply chains are also on the front lines when it comes to battling inflationary pressures. Moreover, partly due to the war in Ukraine, Europe is facing ongoing energy supply issues and is struggling to obtain essential supplies.

However, we have observed many energy and utilities businesses focusing on improving their supply chain resilience over the past year as part of their overall efforts to strengthen their operations. We see leading companies building formal supply chain capabilities, which is helping them to improve all aspects of their supply chain processes. Strategies include regionalizing and investing in cloud technology to enhance supply chain visibility.

The current emphasis on improvement and innovation to reduce supply chain risk exposure could explain why "uncertainty surrounding the organization's core supply chain" does not appear in the list of top five concerns for this industry for 2032.

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[2] www.wuft.org/news/2022/09/15/weather-events-caused-most-major-power-outages-in-the-past-two-decades/.

The need to adapt to the future of work

“Succession challenges and ability to attract and retain top talent” is the third-ranked risk for energy and utilities companies in 2023, moving down from the top spot in our 2022 survey and dropping slightly in score. That change is likely due to executives’ concerns about extreme weather threats and supply chain issues intensifying due to recent events, more than companies seeing any significant improvement over the past year in their ability to recruit and hold on to in-demand talent in a labor market that remains tight.

Energy and utilities businesses are still struggling to hire and train enough skilled talent to replace experienced personnel retiring from the workforce in growing numbers — and often earlier than expected. Many companies face an uphill climb in convincing younger workers that they can offer a rewarding career path. The need to secure highly specialized technical skills for jobs in areas such as renewables is another obstacle to energy companies overcoming critical staffing challenges.

Other trends are poised to exacerbate the energy and utilities industry’s “people problem” — as evidenced by the fourth and fifth risks for 2023. “Changes in the overall work environment,” which ranks fourth, includes shifts to hybrid work environments, the expansion of digital labor, and changes in the nature of work and who does that work. Ranking fifth is the concern that the organization’s “approach to managing ongoing demands on or expectations of a significant portion of our workforce to ‘work remotely’ or increased expectations for a transformed, collaborative hybrid work environment” could undermine the company’s ability to retain valued talent.

These risks are intertwined — and energy companies are certainly not unique in trying to decide how and if they can accommodate remote or hybrid work arrangements for employees for the long term. Also, like many businesses, they are finding out the hard way that taking an inflexible stance toward working remotely can worsen recruiting and retention issues. Realistically, many jobs in the energy and utilities industry can’t be performed from a home office. However, that doesn’t mean employers in the space can’t work with employees in these roles to create more flexible schedules or compensate them with other benefits such as more paid time off.

Looking more closely at the fourth-ranked risk on the 2023 list for this industry, another potential driver is around merger and acquisition (M&A) activities making it more difficult for energy companies to sustain their organizational culture and business model. M&A activity is rising as energy firms look to grow their business and/or jump-start or expand their interests in renewable energy. To prevent the loss of critical human capital due to post-merger “culture shock,” traditional energy companies aiming to acquire renewable energy startups will want to handle the integration process with great care, prioritizing communication and employee engagement from the outset.

Overview of top risk issues for 2032

As noted earlier, energy and utilities executives anticipate that “the rising threat associated with catastrophic natural disasters and weather phenomena” — from wildfires to floods to hurricanes — will be the top risk for their firms through the next decade.

Another operational risk, “resistance to change,” holds second place on the top five list for 2032. That isn’t surprising, given that this risk is typically in our top five and holds the sixth spot for 2023. A macroeconomic risk — “the adoption of digital technologies” — which also ranks second on the 2032 list of top risks for this industry, provides insight as to why leaders of energy and utilities firms are concerned that resistance to organizational change may restrict their company’s ability to make timely and necessary adjustments to its core operations and business model.

Energy companies are under pressure to transform their operations and take advantage of technologies like artificial intelligence and natural language processing to increase efficiency and decision-making. Given that workers with these skills are in short supply in the labor market, energy businesses will need to upskill and reskill existing employees to work with these new tools to fully realize their value proposition — and not all staff will welcome that change or be able to adapt to it. Also, as organizations automate more processes, some jobs will become obsolete or change dramatically. All of these dynamics, if not handled well, can impact organizational culture negatively and hinder companies’ efforts to transform.

Two risks that share fourth place on the 2032 list are closely tied to “the adoption of digital technologies” risk. One is operational in nature — “the inability to utilize data analytics and ‘big data’ to achieve market intelligence, gain insights on the customer experience, and increase productivity and efficiency.” The other is strategic: “Rapid speed of disruptive innovations enabled by advanced technologies and/or other market forces may outpace our organization’s ability to compete.”

Clearly, energy and utilities executives are worried that their businesses — and their workers — will be unable or *unwilling* to keep pace with technological change in the coming decade. That, in turn, can prevent these companies from deploying advanced technologies effectively to create sustainable competitive advantage, and to help drive transformation in the energy industry as a whole.

However, these leaders can take some comfort in knowing that executives in other industries foresee similar challenges for the future, as four of the top five risks for energy and utilities companies in 2032 appear on the top 10 list of risks in our global survey.

It’s an exciting but daunting time of transformation, transition and growth for the energy and utilities industry. The risk environment is high, but there is also tremendous opportunity for forward-thinking leaders to evolve their operations so they can create a future-forward workforce, increase operational output and deliver new energy solutions.

Energy and Utilities — 2032

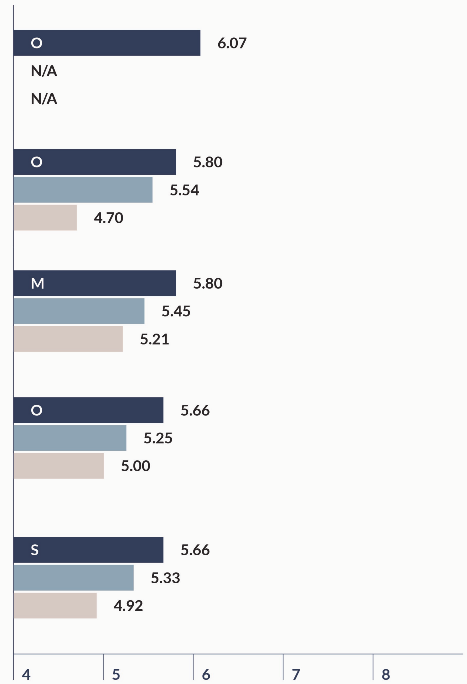
The rising threat associated with catastrophic natural disasters and weather phenomena (e.g., wildfires, floods, extreme heat/cold, cyclones/hurricanes/typhoons) may create significant operational challenges that threaten our assets, employees, and our ability to deliver products and services to our customers

Resistance to change in our culture may restrict our organization from making necessary adjustments to the business model and core operations on a timely basis

The adoption of digital technologies (e.g., artificial intelligence, automation in all of its forms, natural language processing, visual recognition software, virtual reality simulations) in the marketplace and in our organization may require new skills that either are in short supply in the market for talent or require significant efforts to upskill and reskill our existing employees

Inability to utilize data analytics and “big data” to achieve market intelligence, gain insights on the customer experience, and increase productivity and efficiency may significantly affect our management of core operations and strategic plans

Rapid speed of disruptive innovations enabled by advanced technologies (e.g., artificial intelligence, automation in all of its forms, hyper-scalable platforms, faster data transmission, quantum computing, blockchain, digital currencies and the metaverse) and/or other market forces may outpace our organization’s ability to compete and/or manage the risk appropriately, without making significant changes to our business model



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