Implications for businesses: Energy

Ukraine: A conflict that changed the world

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The impact of the crisis on macroeconomic themes will be felt across all industries to varying degrees.

Inflationary pressures associated with supply chain issues, such as costs of materials, labour and logistics are mounting, with companies considering a number of solutions to maintain revenue and profitability. For instance, oil and gas producers and food manufacturers will be the most impacted by inflation, largely due to Russia and Ukraine having dominant positions as major exporters of key raw materials across these industries.

Other industries may need to change business models as a result of subtle changes in trading behaviours. As each nation becomes more focused on developing domestic production to avoid geopolitical risks, transportation and logistics companies will likely need to evolve to accommodate a lower demand for international trade but growing interest in national logistics solutions.

With ESG becoming an increasingly prominent topic on corporates' risk agendas, significant resources are being allocated to dedicated ESG teams across multinational corporations to develop risk management strategies. With increased awareness and potential scrutiny from employees, customers and stakeholders, businesses could incur significant costs to adhere to ESG standards.

In order to meet public expectations, thousands of companies have exited from or paused Russian operations. Those that continue to conduct business in Russia face potential reputational damage in the affected region, which could lead to economic repercussions (for example a. decline in business due to global boycotts). Corporates are also spending significantly more on due diligence and compliance reviews to ensure any direct or indirect relationships with Russia are identified and replaced.

Aon Global Risk Management Survey

Aon's 2021 Global Risk Management Survey illustrates today's traditional and emerging corporate risk portfolio. The Survey collates responses of over 2,300 risk managers from 16 industries, spread across varying territories and company sizes. In 2021 respondents selected and rated 10 top risks that their organizations were facing:

01	Cyber Attacks / Data Breach
02	Business Interruption
03	Economic Slowdown / Slow Recovery
04	Commodity Price Risk / Scarcity of Materials
05	Damage to Reputation / Brand
06	Regulatory / Legislative Changes
07	Pandemic Risk / Health Crises
08	Supply Chain or Distribution Failure
09	Increasing Competition
10	Failure to Innovate / Meet Client Needs

The following analysis breaks down the results of this survey by industry sector and considers how each sector's risk profile has changed as a result of the conflict in Ukraine. Risks highlighted in bold indicate risks that will be further amplified by effects of the crisis.

Overview

The following table summarises the implications of each of the market forces explored in this report to businesses over the short to long term. These are assessed in greater detail over the following pages for the different industry groups expected to be most impacted by the crisis.

	Cyber	Supply chain	Food security	Climate transition	Energy security	ESG	Public sentiment
Banks and financial institutions	Minimal	Minimal	Minimal	Minimal	Minimal	Significant	Medium → Significant
Construction and manufacturing	Minimal	Medium → Significant	Minimal	Minimal	Medium → Significant	Medium	Minimal
Energy	Medium	Significant	Minimal	Significant	Significant	Medium → Minimal	Significant → Medium
Food and beverages	Minimal	Significant	Significant	Minimal	Medium	Minimal	Medium → Minimal
Public sector and healthcare	Significant → Medium	Minimal	Significant → Medium	Significant	Minimal	Minimal	Significant
Technology	Medium → Significant	Minimal	Medium	Medium	Minimal	Minimal	Minimal
Transportation and logistics	Significant → Medium	Minimal	Medium	Medium	Significant → Medium	Minimal	Minimal

Key:
- **Minimal:** Market forces will have no or minimal impact on the industry
- **Medium:** Market forces will have an indirect impact on the industry
- **Significant:** Market forces will have a clear, adverse impact on the industry

Energy

Cyber	Supply chain	Food security	Climate transition	Energy security	ESG	Public sentiment
Medium	Significant	Minimal	Significant	Significant	Medium → Minimal	Significant → Medium

Global insurance premium: $43bn

Aon 2021 Top 10 Global Risks
(Risks in **Bold** are likely to be further amplified by effects of the Ukraine crisis):

01	**Business Interruption**
02	**Commodity Price Risk / Scarcity of Materials**
03	**Regulatory / Legislative Changes**
04	**Economic Slowdown / Slow Recovery**
05	**Environmental Risk**
06	**Cyber Attacks / Data Breach**
07	Accelerated Rates of Change in Market Factors
08	**Climate Change**
09	Cash Flow / Liquidity Risk
10	**Political Risk**

Refineries are currently enjoying a significant increase in profits due to price hikes that have been exacerbated by supply constriction pressures on top of demand surge as the world exited the pandemic. However, they remain conscious of the need to detach from Russian imports and restructure their businesses in order to incorporate renewable solutions. As such, as well as their partners across the value chain, they are mapping out their supply chains in detail and considering how to permanently disconnect from Russian business.

Short term: Several organisations across the West are reverting back to traditional classes of energy (e.g. coal) to meet short-term domestic energy demands. Consequently, there are reputational damage risks associated with ramping up thermal energy production in a pro-ESG environment.

Energy companies are benefitting from rising oil prices, experiencing a significant windfall in profits. While this can support efforts to transition to renewables, higher profits also lead to greater tax revenues for governments that will be looking to fund other elements of the economy, such as addressing the food crisis.

Energy (continued)

Medium to long term: As Russia and Ukraine are exporters of key materials needed for climate transitions, such as the nickel commonly used in battery storage devices, energy companies may have to look for alternative sources.

With an increased global focus on renewables – further spurred by the conflict – leading oil companies are looking to restructure their businesses to become energy giants. This will require significant costs and investment to mitigate new risks and recruit new and relevant expertise.

Case study: Sven is an oil refinery based in Berlin, owned by Russia and configured to Russian crude. The company faces challenge or must reconfigure to other sources of oil. Significant investment is required in infrastructure and the supply chain to remodel the business.

More likely scenarios | Less likely scenarios

01 Defensive push-back	02 Protracted conflict	03 Annexation	04 Collapse of Ukraine	05 Escalation
– Reform relationships with Russian suppliers in the long-term by investing into domestic and renewable energy solutions – Willingness to ramp up supply and procurement of new projects in Russia in order to alleviate supply and demand shocks – Companies tied to stricter regulatory requirements and greater costs associated to higher environmental standards – Greater profit margins from continuing high oil prices drive an improvement in business resilience	– Russia attacks one or multiple Ukrainian nuclear plants, leading to energy security, environmental and social risks – Reconsideration of energy importation from Russian allies	– Invest significantly in infrastructure redesign to accommodate other forms of crude and build relationships with suppliers outside of Russia; significantly invest in renewable energy and climate transition – Boycotting of Russian energy could lead to reduced profits and leave shareholders unsatisfied (exposed to class action)	– Higher oil prices lead to investors channelling more funds into non-ESG energy stocks – Expand supply chains beyond Russia and allies – consider developing LNG infrastructure to form stronger partnerships with US – Governments subsidise renewable energy projects and create favourable economics to drive the transition to net zero as oil/gas companies reinvest in renewable energy technology	– Social shift in attitude towards oil sands and ramp up of production; – Enter into a special agreement with OPEC to access sufficient energy – Disrupted systems for refineries and power grids may lead to the potential of loss of power for citizens and critical infrastructure – Destruction of renewable projects leads to increased dependency on oil & gas at inflated prices – Targeted Russian cyber attacks on power reactors in Ukraine, leading to supply disruption

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