

Risk & Resilience Practice

Geopolitical risk: Navigating a world in flux

In a fast-fragmenting world, geopolitical instability has vaulted to the top of the CEO agenda. Here's what today's fraught global dynamics mean for leaders—and how they can begin grappling with geopolitical risk successfully.



In this episode of *The McKinsey Podcast*, senior partner Andrew Grant and global director of geopolitical risk Ziad Haider speak with global editorial director Lucia Rahilly about McKinsey's latest research on geopolitical risk, including how the geopolitical landscape is changing, implications for global players, and how leaders can move out of reactive mode and develop the resilience they need to thrive amid a fragmenting global order.

After, McKinsey partner Jennifer Stanley shares an early-career lesson on how to move past self-doubt and trust your experience—from our *My Rookie Moment* series.

The McKinsey Podcast is cohosted by Roberta Fusaro and Lucia Rahilly.

This transcript has been edited for clarity and length.

Transitioning to a multipolar world

Lucia Rahilly: The war in Ukraine has put a spotlight on geopolitical risk and on the very tangible disruptions it has caused in a wide range of areas: energy, food, supply chain, and so forth. The war has also put globalization under renewed scrutiny, as those same ties that tether us together now also present us with interdependency risks. Ziad, can you help us make sense of these changing dynamics in the geopolitical landscape?

Ziad Haider: We're in a transitional period from what used to be a more or less unipolar world to a much more multipolar world. From a military point of view, there is still the US's global preeminence. From an economic point of view, the US is still, of course, in a core position, but there's also the EU and China, so it's much more of a tripolar world. When we get to the political dimension, it is much more diffuse at a time when the global governance put in place after World War II is just not working. That's playing out most dramatically in two different theaters: Europe and the Indo-Pacific.

If we look at Russia's invasion of Ukraine, the word "disruption" doesn't do it justice when we think of the eight million people driven out of their homes and millions more without heat or electricity this winter. Companies are having to live with that shock, and at a human level it's deeply tragic.

At the same time, we have what's happening in the Indo-Pacific, which is the escalating US–China strategic competition. There are structural forces of competition at work, which is leading to a question that the Japanese prime minister posed eloquently in Singapore at the Shangri-La Dialogue: Today Ukraine, tomorrow East Asia? And by that, he's wondering if the instability we're seeing in Europe now might also occur in Asia, which is the engine of global growth.

Andrew Grant: I've been quite struck in the last couple of months by the number of corporate and global leaders who have made statements to the effect, "We live in a world now where geopolitics trumps capital markets." That's a very big call when you think of the life of a corporate leader, whose goal is to optimize around the capital markets, steward the value of their enterprise.

Risks beyond supply chain

Lucia Rahilly: Much of the discussion of geopolitical risk has focused on supply chain resilience. Say a few words about some of the other risks that are becoming more acute, and what leaders should do to prepare for them.

Andrew Grant: Two domains come to mind: capital and people. Global organizations typically think you would deploy capital very differentially based on country risk or different geopolitical risks. Do you actually deploy the amount of capital? Do you have different expectations around time frames? Do you think more about partnering and using other people's capital? Risks are not the only part of this that requires consideration. Companies must also reconsider their fundamental approach to allocating capital.

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Likewise with people. We have expectations that the talent working for organizations is very global. They want to be part of a connected global organization. We’re seeing that nationality is starting to matter a lot more. Leaders must work to hold their organization together when many of their employees are subject to much more nationalistic forces than they used to be. The leaders we speak and engage with are quite concerned about how to nurture a global culture in a world that is nowhere near as sympathetic as it used to be.

Ziad Haider: On supply chains, it’s also worth disaggregating the risks of maintaining a supply chain in a geopolitically challenging market. Many companies are doing this but need to use a lot more care and diligence to make sure there isn’t, for example, forced labor involved in that supply chain.

There’s a dimension of supply chain that is moving to less geopolitically challenging countries, or what some would call “friend-shoring,” be it India or Indonesia or Vietnam. There are regulatory and other challenges and opportunities there as well. There’s also a phenomenon of moving supply chains back home, which links into the themes of industrial policy we’re seeing. These three dynamics or facets of supply chains are all interacting at the same time.

The other risk, in addition to people and supply chains, is reputational risk. How do you maintain

a global footprint but be ready to answer the question about why you are in that problematic market? The bar for explaining where you are and why you’re there has gone up from external stakeholders, be it media or parliament, as well as internally, from colleagues. That’s something companies are having to balance. What you say in one market very quickly shows up in the other market, so you can’t get away with shading your messaging too much, either.

A changing world, a changing response to risk

Lucia Rahilly: We see in our McKinsey research that geopolitical risk is at the top of the CEO agenda. Business leaders know they need to act. But historically, at least in Western countries, leaders seemed more prone to address geopolitical risk in an ad hoc way, as specific crises or specific risks emerged. What’s the change in approach leaders should take now?

Andrew Grant: The first step is building a level of awareness and understanding about the issues at play and the implications for the organization. Second, there’s a level of professionalism and some critical new capabilities that organizations need to build in response to that awareness. A high level of professionalism is required to understand the legal and regulatory implications of laws from countries with extraterritorial reach.

Geopolitics is not born equal. It affects different countries differently. Leaders need to ask certain questions: How do I think about that? How do I categorize? How do I have a common language within the organization to understand and make decisions, and coordinate and bring along a global enterprise?

Ziad Haider: The world has changed, and that has forced companies to be more granular. If we look at the '90s, it was an era of US-led hyperglobalization. The US was facilitating China's entry into the WTO. We even had discussions at the Russia and NATO level. It's hard to imagine at this point. We've seen the arc change, and we now have a revival of almost old-fashioned major power competition between the theater in Europe and in the Indo-Pacific.

At the same time, within the US itself, these questions about its global role and the value proposition of unconstrained globalization have come under strain. And some of those are quite important and healthy questions. In the '90s, there was an idea that by immense multinationals going out to global markets, there could be this phenomenon of change through trade. You could transform markets, make them more open and more democratic.

Now, for many people coming off the Russia invasion of Ukraine, there's the question, "Does that hold?" Can you really be in some of these difficult markets and expect to change them significantly? Or do you need to be careful and clear eyed and not be in some of these places? And if you are in them, you must explain why. So that unconstrained idea of being a global multinational corporation has fundamentally been tested. Now the question is, how do you be global? And what's the right way to do it in this geopolitical environment?

A framework for resilience

Lucia Rahilly: Give us the high level on what leaders should be doing differently to plan for geopolitical risk and to become more geopolitically resilient. What are the broad categories they should consider?

Andrew Grant: There are countries that I would describe as having very localized geopolitical risks. Those are risks that are material for operations in just that discrete geography. However, one thing that we are finding for many global companies is they might be in 35 countries, 40 countries that have these local geopolitical risks. When you add those countries up, that's quite a significant portfolio of risk.

At the other end of the spectrum, arguably for the first time in recent history, we have two genuine geopolitical superpowers in the US and China. For corporates operating meaningfully in those two places, there are very real geopolitical considerations as a result of great power competition.

Then in between, there are countries that have genuine global military risks, defense and security risks, and those that have what I'd describe as human rights reputational risks that are quite global in their nature. Those countries in the middle are typically nations of genuine significance that figure very materially in the global operations of a global company. There are others, but for truly global companies we find that our framework is quite helpful.

We would also argue with regard to the US and China that the world has never seen two powers of this magnitude that are also so incredibly interconnected with each other. Clearly, there are dimensions like human rights that are very challenging and very problematic. But at the other end of the spectrum, the collaboration that has gone on between the US and China on climate is remarkable. It's a much more nuanced and considered framework that you need to have around an incredibly complicated, interconnected, dynamic relationship that also needs to be monitored and managed in a very active way.

Ziad Haider: Andrew really hit on it: the board's and leadership's focus needs to be much more granular. Every month, the board needs to look at the top five markets of geopolitical concern and create a clear game plan about what will be done to

manage those risks—and that starts with having a common set of facts.

In this global world, even within an organization, there are different points of view. You must think about how the board will be educated around these topics. Is there a common fact pattern? How are you monitoring risks in an operational way, not just in an academic way?

We're seeing a lot of our clients invest in their classic corporate affairs capabilities, their legal teams, and, given the uptick in regulatory changes, their government affairs teams. We ask questions like, who are you talking to on the ground? What's your air cover? How are you developing that?

Other questions that are quite important to clients are: How do you think of your structural presence, be that your tech stack or your corporate structure in a market? Are there degrees of freedom to be created or risks to be managed if you have a separate tech stack in a country or if you have a separate corporate entity? On the other hand, at some point all accountability goes to the headquarters. So companies are grappling with the right footprint to have.

Last, the people side of managing geopolitical risk is quite critical. People have their own geopolitics. It's not so much their interest; it's just a point of view where they grow up. So negotiating those different points of view in an organization to keep it strong, unified, and acting in one way is quite important. How do you have a common world view? And if there are differences, how do you reconcile them to have a clear firm position on a topic?

Andrew Grant: One other point is the importance of mindset, and the mindset of the board and the top team. The mindset I would emphasize is humility.

Ziad and I had the privilege of meeting with the head of government relations for arguably one of the world's largest and most sophisticated companies. He made the statement that they have thrown more resources at the geopolitical challenge over the last year than they could ever

have imagined. They now understand the problems with incredible fidelity, with no great answers. Humility is a very important start.

No one has a monopoly on the right perspective. It's really important for global companies to understand that these are very three-dimensional problems that they should view from a truly global, not just national, lens. The right stance is rarely black and white. And even if it's black and white today, it may not be black and white tomorrow.

Lucia Rahilly: Are most companies moving in this direction already? Or only the biggest ones, as you just described?

Ziad Haider: Elements of this are definitely happening; geopolitical risk is not new. Companies in certain sectors, like oil and gas, have been dealing with these issues for many, many decades. But there are others—for example, technology—that have yet to face these issues. Think of your tech stack in a splintering world, with different regulations in different jurisdictions. These are novel issues. A lot of companies are having to grapple with those new facets.

Andrew Grant: Many large global companies feel they've invested a lot in this. A couple of weeks ago, a chief executive approached me to ask about a challenge they were facing, and said that for many years, "We've always understood what it takes to really earn a growth premium for a company." Their question was, "Is it possible to take these new things we're doing to approach geopolitical risk to make my organization sufficiently better and earn a resilience premium? Would people view me as a good fit for navigating and thriving in a world that is becoming more geopolitically risky?" That's a really interesting thought, but I don't think many, if any, organizations are there yet.

Weighing whether to weigh in—in public

Lucia Rahilly: Leaders have to focus on building resilience across their organization. But what role

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are they expected to play now in public discussions of geopolitical issues?

Ziad Haider: This is another thing worth disaggregating. Last year was seismic. When we look at 1,000-plus companies that have exited Russia, according to a tracker maintained by Yale University, a big part of those exits was also an expectation for the CEO and the company to take a position. We’re very proud of the position McKinsey took in that case.

Edelman puts out a Trust Barometer about the expectations of CEOs on different topics. Last year’s barometer reflects the clear expectation of CEOs to take stances on geopolitical issues in the wake of Russia’s invasion of Ukraine. Collectively, that means moving from a world where it’s not just about corporate social responsibility but talking about corporate political responsibility and taking a clear stance.

We see three different stances or positions. There are positions of courage that are not cost-free. There are positions of necessity that companies sometimes take because they’re being forced to weigh in on an issue, either internally or externally. And there are also positions of humility when companies make mistakes. Sometimes, as a leader, you have to say, “Look, we got it wrong. And here’s how we’re going to fix it.”

The expectation writ large of CEOs to speak on these social and political topics in the social-media environment has gone up. But I’d differentiate a bit about the different types of positions they may or may not need to take along the way.

Andrew Grant: In my view, the most important audience is your own people. Making sure that it’s authentic, real, and lived, and that your people believe it and feel that it’s an accurate representation of who you are and what you actually do.

Ziad Haider: I also think it’s important to think critically about the implications of taking a public position, like saying, “We’re exiting this market” or “We’re taking a principled view,” for your employees in another part of the world.

That’s an important piece because oftentimes these discussions go to headquarters, and a decision is made speaking to a Western audience or a certain set of audiences. But security and physical implications for colleagues in the impacted market can be quite severe. So when the next crisis comes, I do think a lot of companies are going to have to think about how, when, and how loudly they articulate a position when they absolutely need to or think they should.

When colleagues' views diverge

Lucia Rahilly: Diverging interests are inevitable within global companies. How should leaders prepare to navigate those conflicting geopolitical interests among their employee base before a crisis happens?

Andrew Grant: Companies need to be prepared and be thoughtful in advance and know that it will require some courageous, brave, and costly decisions. It's also important to consider what a global corporation looks like in a world that is very different from today's world. We need to rethink some significant aspects of how corporations will operate, in the same way that we rethought multinationals in a very meaningful and fundamental way after the fall of the Berlin Wall.

Ziad Haider: We tend to talk a lot about what an organization should be doing to manage the external environment. Three things come to mind. First and foremost, what's the mindset one brings to these conversations? If I actually want to try to walk in my colleague's shoes and understand where they're coming from, rather than come at it from the viewpoint, "I have a monopoly on the truth," that goes a long way in humanizing these discussions.

There's also how leadership signals. We see right now in some of these trickier markets that CEOs, for example, are opening to China. That's important signaling: Is leadership showing up? You could substitute China for any number of complicated markets out there.

The third thing is the forums you're creating in your own organization—the risk committees, the town halls. Are those aptly reflective of the global nature of your organization? Do people feel like their voices are being heard?

It's a basic point, but it's so important because very often these organizations move very quickly toward a few people in headquarters. The flip side is that there cannot be full transparency. Some of these topics are sensitive. So again, to Andrew's point, one has to be humble about this.

Navigating the nuances

Lucia Rahilly: We've spoken about responses to Russia's invasion of Ukraine. That was a cut-and-dried issue for various reasons for many leaders. But most geopolitical issues tend to be much harder to parse, more complex. Any recommendations for how to proceed in those instances?

Andrew Grant: My own view is that resilience is a bit like a muscle. There is good and bad; that's quite clear at some level but not at all levels. Therefore, you must make sure you are bringing the right approach and the right tools to the right problem and the right amount of moral courage, calling things human rights issues that genuinely are human rights issues.

If there are power, commercial, and national interests and national industrial-policy issues, let's call them that and not mix everything into, "We're the good guys, they're the bad guys." I do think there needs to be a level of sophistication and bravery but also appropriately tailored fidelity to the issues at hand.

Ziad Haider: Part of being able to deal with those gray areas is to have thought about them in advance. What many companies are doing is the exercise of classic scenario planning, looking at a range of scenarios. They look at the watch points to get a sense of which way it's going and to think about what positions they would take. That's exactly the kind of muscle we're talking about needing to build when these events and geopolitical spikes happen.

It can't take you all the way to the end, because you cannot anticipate every scenario or the speed of events. Russia–Ukraine is quite interesting because there was an extended Russian military buildup. We all saw something coming. But we also did not expect there to be a full-fledged invasion, trying to go all the way to Kyiv.

So there are questions of preparedness that many companies are taking from the experience of Russia–Ukraine, and they are already trying to apply them to the Asia context. Part of the answer

is essentially to think about that range of scenarios and not just protocols, but how you would respond. Would you put out a statement? Would you take a stance? That's part of developing a posture.

What's ultimately at stake

Lucia Rahilly: Leaders are navigating one of the most challenging operating environments in recent memory. And setting up an enterprise-wide approach to building this geopolitical muscle, as you described, Andrew, can be a big investment at a busy time. If you're talking to leaders who might be laboring under short-term pressures, what do you tell them is the number-one issue at stake for them?

Andrew Grant: If you really believe in a world where geopolitics trumps capital markets, then clearly that is your number-one priority. Leaders who recognize that geopolitics is their number-one issue understand that their point of view must be shared truthfully, and that they must put effort into expressing their perspective.

I also genuinely believe that there is an opportunity to create a more modern enterprise, an enterprise that is better evolved to the new geopolitical context. And there's a very significant prize around a resilience premium.

If you just hope that 2019 is going to come around the corner again, you're going to be sorely disappointed. It's a new world, and you will have to exercise new muscles. This will require real leadership attention and nurturing, and resource allocation decisions that are often quite brave. And there's a very significant competitive prize—those that do this most purposefully, most bravely, in an accelerated way, will be those that thrive in the next era.

Ziad Haider: Number one, if you don't focus on this issue, you potentially put your people at risk, depending on the market. Number two, you put your growth at risk, your presence in that market. And number three, you put yourself at legal risk if you're not across the different regulatory export

control and sanctions regimes. So there are real consequences, and a polycrisis, to manage here.

The one thing I feel every board should be doing in 2023 is to put the top five markets where they have the most geopolitical exposure on a piece of paper, look at them side by side, and discuss, "What do we need to do to better manage our position in these markets?" Many boards, from what Andrew and I are seeing, are gravitating toward the big questions around China—but not necessarily with the right level of detail.

And over here, coming out of Russia—Ukraine, we are seeing certain opportunities in terms of an accelerated energy transition. We are seeing something coming out of the tension in the Indo-Pacific about friend-shoring, which makes certain other geographies and countries more pivotal. So how do you position yourself?

Lucia Rahilly: Andrew and Ziad, great discussion. Thanks so much for joining us.

Andrew Grant: Thank you so much for facilitating such a fantastic conversation.

Ziad Haider: Thanks very much, Lucia. A real pleasure to be here with you.

Roberta Fusaro: McKinsey partner Jennifer Stanley was convinced her lack of business experience would prevent her from doing a good job on an M&A project. But, as her manager pointed out, she actually had the skills—just not the confidence. Hear more in an excerpt from our *My Rookie Moment* series.

Jennifer Stanley: The first time I was working on a project that involved a merger and an acquisition was frankly terrifying for me. I didn't go to business school. I had no clue what the term "due diligence" meant in the merger and acquisition world.

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—Jennifer Stanley

And here I found myself on a project where I was asked to do some modeling about a potential joint-venture partner for the client that we were serving. I truly had no idea how to start building the model, and I was frankly panicking a little bit because I knew that for something like this, the expectations were quite high.

What I did first to calm myself down was find a mentor who I had actually met while I was being recruited for my job here at McKinsey. And I just fessed up and said, “I’m really nervous. I’m actually not quite sure what I’m doing.” He asked me to describe what it looked like when I was at my best in graduate school, and I started to describe these statistical models, but in the social science context. And he said, “Perfect. You know how to build a model. You’re just using different kinds of data.”

My mentor then suggested that I go in and speak with my manager and write down a list of the

things I thought I could bring to the study that were strengths—things which would help out in the investigation that we were getting ready to do, and to be bold and ask him to align me to work streams that in some way, shape, or form matched things I was good at so that I could get some momentum. To my delight, what I thought was going to be a really difficult conversation, with me having to say, “I’ve never done this kind of a project before” was fine. My manager said, “Thank goodness. Now you know you know something that can be put to good use on this project.”

And the thing I learned is that if every time I’m confronted with a new problem or opportunity, if I ask for help from someone, and they talk me through it and we reframe the nature of the contribution I can make, I probably know more than I think I do. And there’s probably a way to build momentum and build my confidence and make a great contribution to the team and to the client.

Andrew Grant is a senior partner in McKinsey’s Auckland office, **Ziad Haider**, global director of geopolitical risk, is based in the Singapore office, and **Jennifer Stanley** is a partner in the Boston office. **Roberta Fusaro** is an editorial director in the Waltham, Massachusetts, office, and **Lucia Rahilly** is global editorial director and deputy publisher of McKinsey Global Publishing and is based in the New York office.

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