Is this the moment for emerging markets to prioritize integrity?

Global Integrity Report — emerging markets perspective

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Foreword

The pressure on emerging market economies has intensified over recent months, fueled by the COVID-19 pandemic which has hit business growth hard. Despite an increase in the number and strength of regulatory regimes and enforcement activities across many emerging countries and a greater focus by organizations on strengthening their compliance programs, EY's latest Global Integrity Report – emerging markets perspective highlights that fraud and corruption continue to be a major threat to the long-term success of business.

Regulatory scrutiny and remote working following the pandemic is only aggravating these issues. The survey of more than 1,700 employees from the board to shop-floor of large organizations across 21 emerging market countries provide timely and relevant insights into the myriad of ethical challenges faced. Nearly two-thirds of respondents (63%) believe that it is difficult for organizations to maintain standards of integrity in periods of rapid change or difficult market conditions.

Despite this, the research shows that businesses in emerging markets are making a concerted effort to reduce misconduct. More than half (55%) of respondents say their management frequently communicates the importance of operating with integrity and almost half (44%) say it has become easier for employees to report misconduct in the last three years (compared to only 34% in developed markets). While questioning whether this is the moment for emerging markets to prioritize integrity, this report highlights four key areas for organizations to prioritize in their integrity agendas, from putting corporate integrity high up the management agenda to addressing cybersecurity and third-party integrity issues.

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As organizations navigate the crisis and prepare for a ‘Great Reset’, corporate revival and recovery efforts should not get derailed by fraud, bribery and corruption risks. In the new normal, business leaders should cultivate a culture of integrity and trust amongst stakeholders, as these are vital pillars for building ethical and sustainable organizations.

Arpinder Singh
EY India and Emerging Markets Leader
Forensic & Integrity Services

01
Put corporate integrity high on the management agenda

02
Encourage employees to use whistleblowing channels to report misconduct

03
Increase the focus on cyber and data protection

04
Address third-party integrity issues

Key findings

63%

of respondents say it is difficult for organizations to maintain standards of integrity in periods of rapid change or difficult market conditions.

32%

of those surveyed say bribery and corrupt practices present the greatest risk to the long-term success of their business.

55%

of respondents say that management frequently communicates the importance of operating with integrity.

29%

of employees have not reported concerns about integrity for fear of their own personal safety.

35%

of businesses in emerging markets are very confident that their third-party partners operate with integrity.

Introduction

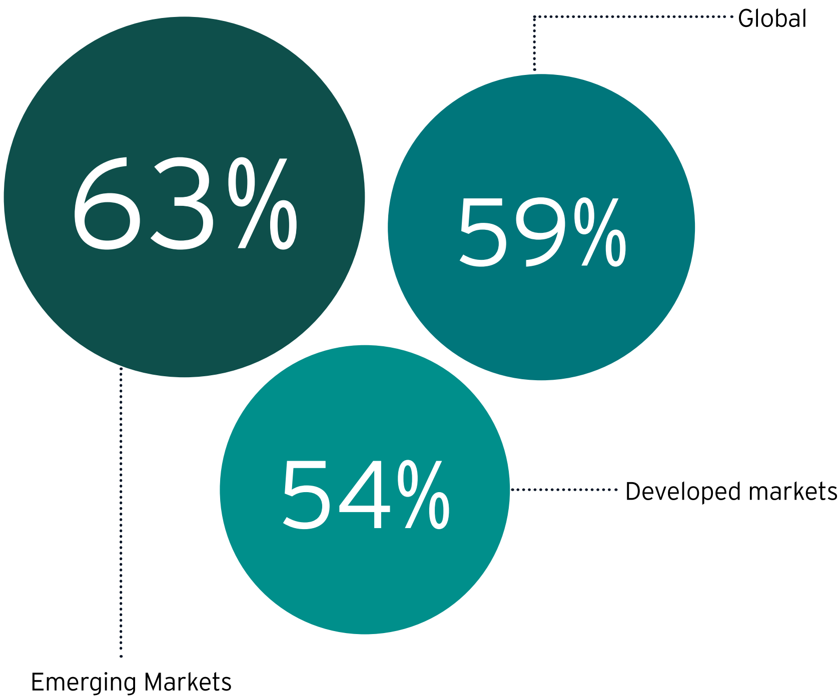
Creating long-term value – how can companies in emerging markets prioritize integrity?

An ex-CEO imprisoned for money laundering in Southeast Asia[1]; a senior business figure embroiled in bribery allegations in South America[2]; senior executives standing down during an investigation into corrupt practices in Namibia[3]. These are just three examples of the integrity challenges and breaches of trust that make business leaders anxious about investing and operating in emerging markets.

The latest EY Global Integrity Report – emerging markets perspective illustrates the extent of the problem. Approximately one-third (32%) of companies from emerging markets[4] say that bribery and corrupt practices present the greatest risk to the long-term success of their businesses, and just over one-quarter (27%) point to fraud. That's not all: nearly one-third (30%) believe that the risk of a cyber and ransomware attack is a significant threat.

It's not just endemic ethical issues that create challenges for firms operating in emerging markets – these regions have also been affected by the economic disruption and uncertainty caused by the COVID-19 outbreak. The World Bank expects developing economies to shrink for the first time in the last six decades as they count the cost of the pandemic[5], which has hit emerging markets such as Brazil[6] and India[7] hard.

Maintaining standards of integrity during rapid change is a significant challenge



Question: To what extent do you agree or disagree? It is challenging for organizations to maintain their standards of integrity in periods of rapid change or difficult market conditions – Global, Developed and Emerging? Percentage answering 'agreed'.
Base: Global Integrity Report 2020 (2,948); Developed (*1,218*); Emerging (*1,730*); India (*100*), Kenya (45), Malaysia (*100*), Nigeria (60), Saudi Arabia (75), South Africa (*100*), UAE (*100*)

Recovery from the global economic slowdown is expected to take as much as five years[8] and has led to far-reaching consequences worldwide in the form of spiraling revenues, job losses and economic unrest.

The EY survey shows that standards and best practice are most likely to slip when times are tough: 63% of respondents say it is difficult for organizations to maintain standards of integrity in periods of rapid change or difficult market conditions.

[1]Reuters, Former Garuda Indonesia CEO jailed for eight years for bribery, May 8, 2020.
[2]VOA News, Former Petrobras CEO Sentenced to 11 Years in Prison, March 7, 2018.
[3]Africa Times, Iceland firm's CEO steps aside in light of Namibia corruption reports, November 14, 2019.
[4]Emerging markets covered in this survey are included in the "About the Research" section at the end of this report.

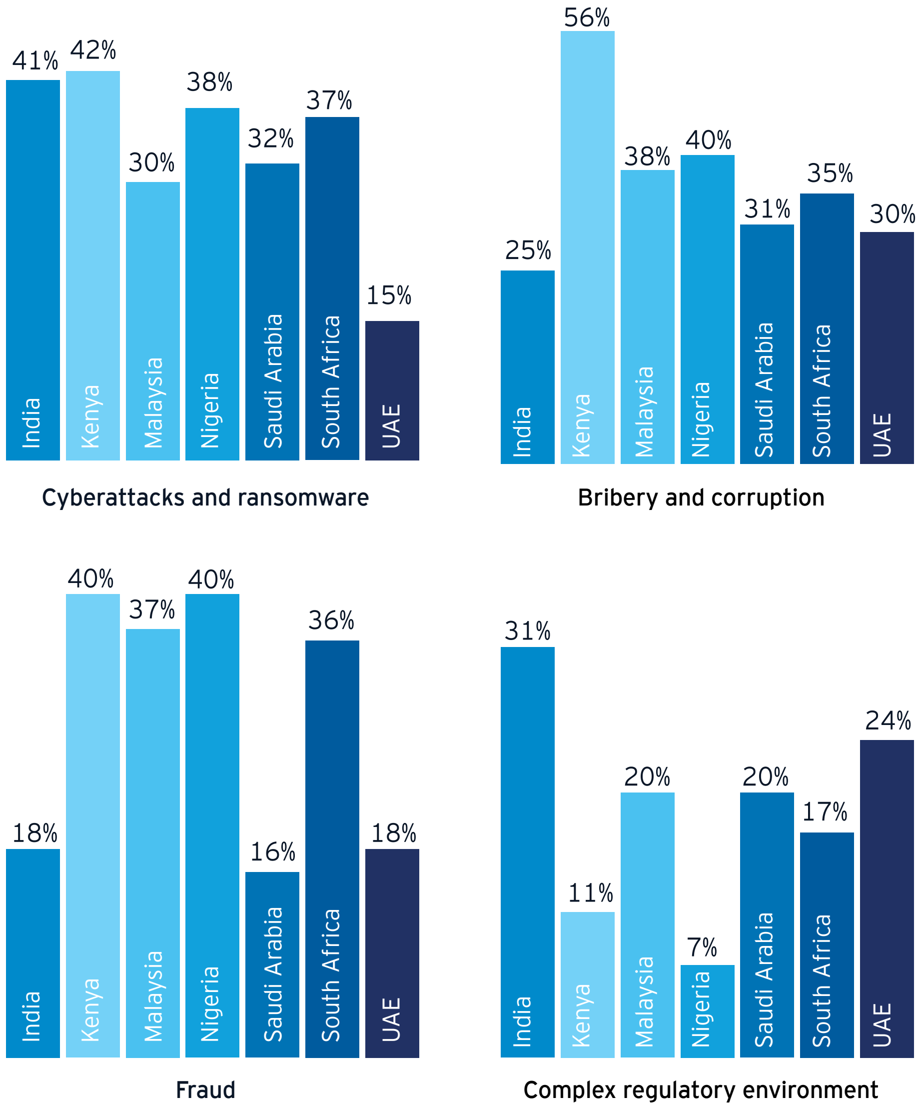
The survey reveals that businesses operating in emerging markets are more likely to be adversely impacted by the current disruption. For example, 45% of China-based respondents surveyed believe remote working provides a significant risk to ethical conduct, compared with 33% of respondents globally. In parallel, 35% of respondents based in India believe that ethical business conduct will suffer due to COVID-19, compared with only 20% globally.

However, organizations operating in emerging markets are making concerted efforts to reduce misconduct by executing the following:

- Putting corporate integrity high on the management agenda
- Encouraging employees to blow the whistle on misconduct
- Increasing the focus on cyber and data protection
- Addressing third-party integrity issues

In this report, we explore how organizations are dealing with these areas of risk and offer practical ways for businesses to overcome the challenges they may face along the way.

Risks impacting the long term success of organizations



Question: Which, if any, of the following do you think pose the greatest risk to the long-term success of your organization?

Base: Global Integrity Report (2,948); Developed (1,218); Emerging (1,730); India (100), Kenya (45), Malaysia (100), Nigeria (60), Saudi Arabia (75), South Africa (100), UAE (100)

About the research

Between January and February 2020, our researchers — the global market research agency Ipsos MORI – conducted 2,948 surveys in the local language with board members, senior managers, managers and employees in a sample of the largest organizations and public bodies in 33 countries and territories worldwide. Of these, 1,730 surveys were conducted in 21 emerging market countries including: Brazil, China, India, Kenya, Mexico, Nigeria, Poland, Russia, Saudi Arabia, Singapore, South Africa, United Arab Emirates, Argentina, Chile, Colombia, Malaysia, Turkey, Lithuania, Latvia, Estonia and Peru.

A further 600 surveys in total were conducted in April 2020 using the same respondent profile across China and India, as well as Germany, Italy, the UK and the US during the COVID-19 pandemic.

[5] Financial Times, Emerging economies forecast to shrink for first time in 60 years, June 8, 2020.
[6] BBC News, In pictures: How coronavirus swept through Brazil, July 16, 2020.
[7] Times Now News, COVID effect: World Bank may project steeper contraction of Indian economy for FY21, August 20, 2020.
[8] The Financial Express, Global economic recovery may take 5 years.

01

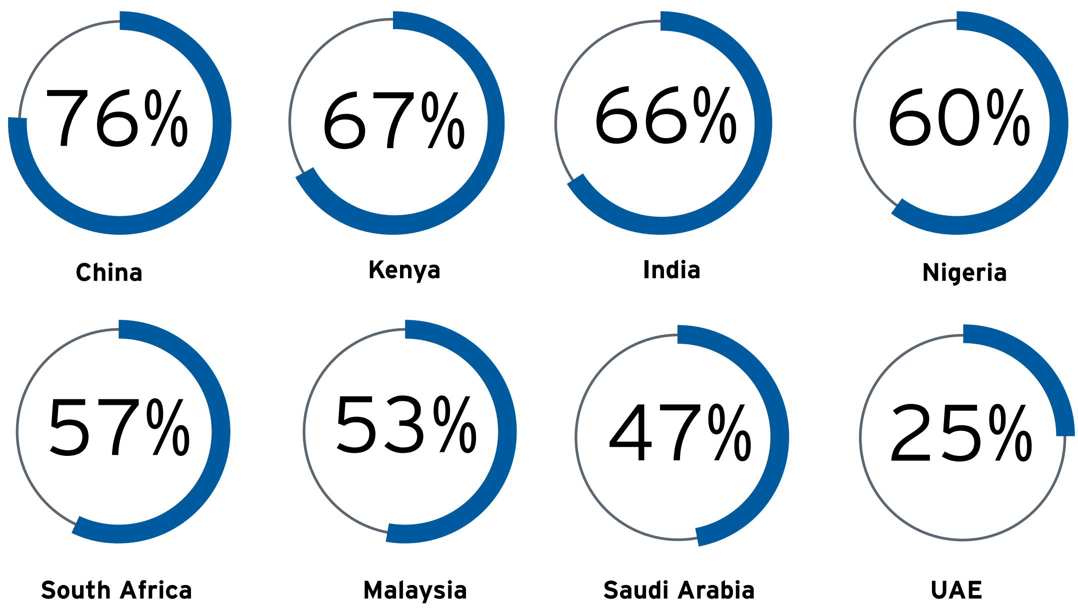
Put corporate integrity high on the management agenda

Corporate integrity scandals can seriously damage the reputations of companies and their stakeholders. Research from Harvard Business Review shows that executives who have worked at scandal-hit companies suffer a 4% shortfall in future pay, even if it's clear that they were not directly involved in the scandal[9].

More importantly, integrity failures can also damage companies' relationships with their key stakeholders: investors, customers, employees and communities as well as compromising the long-term value of their business.

According to the EY survey, more than half (55%) of respondents in emerging markets say their management frequently communicates the importance of operating with integrity, compared with only 39% in developed markets. This proportion varies significantly across emerging markets, with 76% of managers frequently communicating the importance of integrity in China compared with just 25% in the UAE.

Significant country variation in management communicating the importance of acting with integrity



Question: In the last two years, how often have you heard management communicate about the importance of behaving with integrity? Percentage answering 'frequently'
Base: Global Integrity Report (2,948); Emerging (1,730); India (100), Kenya (45), Malaysia (100), Nigeria (60), Saudi Arabia (75), South Africa (100), UAE (100), (China 100)

[9] Harvard Business Review, The Scandal Effect, September 2016.

Talking about corporate integrity is a good start, because it helps to build a culture of trust and integrity across the whole business. Ultimately, however, actions are much more important. In particular, management should back up proclamations about integrity by setting visible examples and having clear measures and key performance indicators (KPIs) in place to measure the impact of their initiatives. Encouragingly, the majority (58%) of respondents in emerging markets say their standards of integrity have improved in the past two years. This is a positive sign, and it is important to recognize that these organizations have started addressing corporate integrity issues.

There are reassuring signs that companies across the private and public sector in emerging markets are taking note of the importance of integrity. For example, they are represented on international groups, such as the Business Twenty (B20), Group of twenty (G20) or African Union, to address fraud, bribery and corruption.

In addition, a number of emerging market countries have actively embraced The World Economic Forum's Partnering Against Corruption Initiative (PACI), in particular, the Future of Trust and Integrity project[10]. This initiative was set up to examine how to rebuild trust and integrity while simultaneously addressing corruption. In Argentina, where there was a renewed focus on tackling corruption to attract foreign direct investment (FDI), the World Economic Forum highlights that approximately 78% of business leaders perceived a drop in the level of corruption in the previous decade, and almost 90% anticipate further improvement in the next 10 years.

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> Management should back-up proclamations about integrity by setting visible examples and having clear measures and KPI's in place.
>
> **Ramesh Moosa**
> **EY ASEAN Forensic & Integrity Services Leader**

Building an integrity agenda is critical

Organizations must lead from the top on corporate integrity. The first step is to clearly convey why it's important to act with integrity: because it's the right thing to do and can differentiate the business, not just because local or global regulations require the business to act in this way. This must be supported by informal communications that help to encourage ethical behavior and raise knowledge and awareness among all levels of the organization beyond the tone from the top.

Second, formal programs, training, procedures and policies must be put in place by senior leadership and communicated clearly to the wider company. It is also essential for senior leaders to be seen to be following these rules themselves. The importance of "organizational justice" is key here, where everyone is perceived to be accountable for their actions, irrespective of rank or individual performance.

[10] World Economic Forum, "The Future of Trust and Integrity" 2018.

02

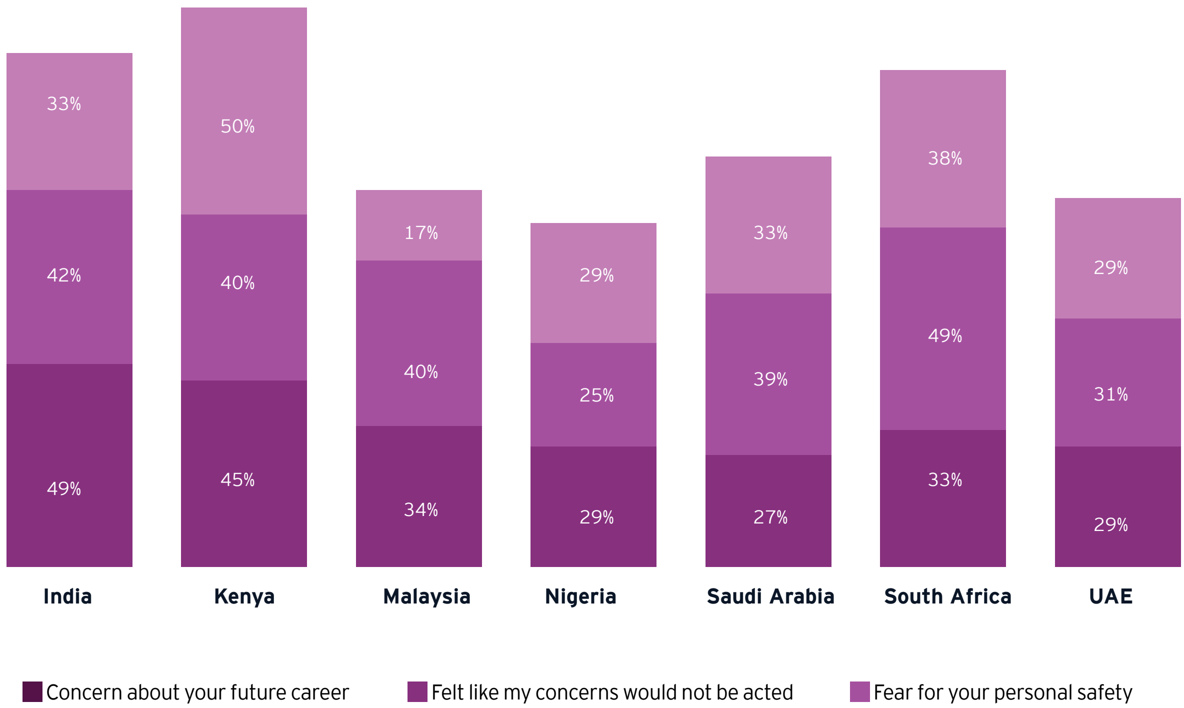
Encourage employees to use whistleblowing channels to report misconduct

It is critical that employees' voices are heard in the organization – creating a "speak-up" and "active-listening" culture is a vital indicator of how deeply embedded integrity truly is. Developing effective channels to avoid individual employees reporting issues directly to regulators, enforcement agencies or the media is critical.

Raising the alarm about misconduct or unethical behavior can be considered risky for individuals, who might fear reprisal – both professionally and personally. More than one-third (37%) of respondents in emerging markets say they haven't reported concerns about integrity due to worries about their career progression; worryingly, nearly 3 in 10 (29%) kept their concerns private out of fear for their own personal safety.

Companies in emerging markets are making efforts to facilitate whistleblowing. Almost half (44%) of emerging markets respondents say it has become easier for employees to report their concerns in the past three years (compared with only 34% in developed markets), and one-third

Raising the alarm about misconduct still an issue in emerging market countries



Question: Which, if any, of the following were reasons why you did not report your concerns?
Base: Global Integrity Report (*2,948*); Emerging (*1,730*); India (*100*), Kenya (45), Malaysia (*100*), Nigeria (60), Saudi Arabia (75), South Africa (*100*), UAE (*100*)

(31%) say their companies offer whistleblowers more protection than they did in the past.

This is partly driven by tightening regulation in emerging markets[11]. But it's also in corporates' best interest to make whistleblowing as easy as possible. If employees don't feel comfortable reporting issues to management, they may go directly to a regulator, the press or vent their grievances on social media. Having a strong speak-up culture also has the benefit of creating "psychological safety" among employees that helps to drive innovation, productivity and employee satisfaction.

37%

of respondents in emerging markets say they haven't reported concerns about integrity due to worries about their career progression.

> "Whistleblowing programs form a key pillar of the organization's corporate governance framework and management and board oversight will be crucial for its success.

Sharon van Rooyen
EY Africa Forensic & Integrity Services Leader

The importance of an effective whistleblowing programme

Businesses must make employees feel that they can safely report misconduct, that it is practically possible to do so and that it is in the best interests of the firm. For example, an online whistleblowing system will not be appropriate if many workers are in remote regions and do not have access to a computer or the internet, which may be the case for mining companies. Multiple channels for reporting concerns must be in place so that employees have the option to choose what they are comfortable with and that would be advantageous for them. Formal systems can work effectively and efficiently by normalizing processes, such as resource allocation, case management and clarity on speak-up processes. These must be taken as the minimum requirements when running the whistleblowing mechanism.

It's also imperative that companies should protect whistleblowers to minimize any possible retaliation; anonymous complaints should also be addressed by the stakeholders. The right governance setup must ensure independence and confidentiality. Training and awareness programs will be key to facilitating an open and transparent culture. Companies should consider how they can create a positive speak-up culture and maintain the psychological safety of employees, which needs to be driven by strong leadership.

ET Now, Govt tightens audit reporting norms to check corporate frauds, February 27, 2020.

03

Increase the focus on cyber and data protection

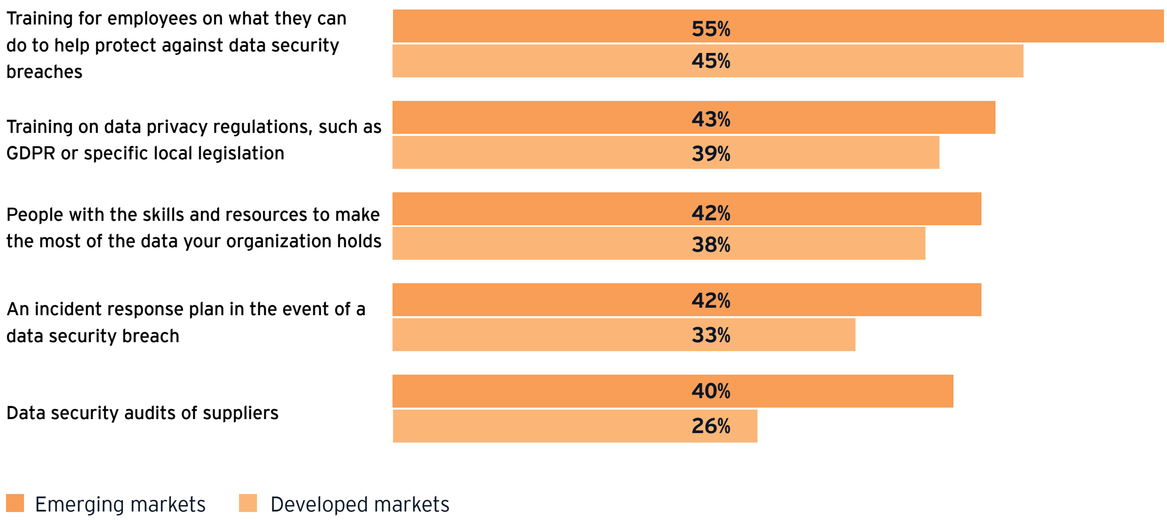
COVID-19 has heightened the risk of cyber breaches, given the increasing reliance on the internet and remote working by businesses. This increased dependency may lead to cyber criminals exploiting the vulnerabilities in weak networks and targeting unsuspecting employees. There was a spike in cyber and ransomware attacks in 2020[12], and cyber criminals have been reported to be even selling fake COVID-19 cures through phishing e-mails[13], as well as infecting networks with malware.

The consequences of a data breach may be adverse for an organization, resulting in financial as well as reputational damage. Research from Cisco finds that data breaches can also have a devastating impact on brand reputation[14].

Data protection has emerged as a priority and most companies operating on an international scale are implementing a number of data-protection practices and policies in line with applicable regulations.

Encouragingly, the EY report highlights that more than half (55%) of emerging market companies offer training to employees on how they can prevent data security breaches – compared with just 45% of companies in developed markets. In parallel, a significant majority (86%) of respondents in emerging markets say they are confident that they're doing all they can to protect the privacy of customers' data.

Emerging market countries acknowledging the importance of data protection



Question: Which, if any, of the following does your organization have in place? Percentage applies.
Base: Global Integrity Report (2,948); Developed (1,218); Emerging (1,730) % applies

[12]Checkpoint, Global Surges in Ransomware Attacks, Oct 2020.
[13]CNBC, Coronavirus fraudsters prey on fear and confusion with fake products, email scams, March 2020.
[14]Cisco, Securing What's Now and What's Next, March 2020.

Governments are taking steps to introduce legislation that outlines and clarifies companies' data protection responsibilities and the penalties for noncompliance[15]. This year, for instance, Brazil's General Data Protection Law has come into effect. It aims to unify 40 different statutes that previously governed personal data online and offline[16]. In India, meanwhile, proposals are in place for the Personal Data Protection Bill, a major new law to control the processing of citizen data[17]. Companies must, of course, not only adhere to local laws, but also international regulations such as the EU's General Data Protection Regulation (GDPR) and the California Consumer Privacy Act (CCPA) that also covers customers located overseas.

The EY survey results suggest that companies believe they are making progress in implementing data-protection policies and practices. The stakes in this regard are high. Many emerging market countries operate data centers for large organizations as they move their operations offshore. Cost-cutting measures during the COVID-19 pandemic will only exacerbate this situation.

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Businesses in emerging markets are increasingly acknowledging that data protection is a business critical issue.

Nader Rahimi
EY Middle East & North Africa Forensic & Integrity Services Leader

Strengthening cyber and data privacy frameworks

Businesses in emerging markets need to be leading the way in dealing with data privacy issues and not just strengthening controls and processes in line with developed markets. Organizations should consider building a data privacy and protection framework, with strong guidance and support from management and board. Regular communication and awareness should be conducted among employees, as well as third parties. They should also leverage the right technologies as part of their information governance frameworks, covering identification data, categorization, retention or disposal and consolidation of data.

Other leading practices include appointing a data protection officer and continuous monitoring through regular audits to minimize noncompliance with regulations, such as GDPR, that can potentially result in heavy fines and penalties.

The increasing sophistication of cyber threats coupled with strict regulation means that companies are raising the bar and implementing industry-leading practices to protect critical and sensitive data. Attacks can be triggered externally (e.g., cyberattack) or via internal breaches (e.g., data leakage or insider threats), and organizations need to adopt the latest technologies and tools to help identify issues and improve vigilance. This can be done by strengthening the virtual infrastructure, developing strong monitoring frameworks, diagnostics scans and incident response strategies, and raising awareness among all stakeholders to counter future cyber and digital risks.

[15] Comforte Insights, 9 Countries With GDPR-like Privacy Laws, January 17, 2019.
[16] GDPR, What is the LGPD? Brazil's version of the GDPR.
[17] Financial Times, India proposes first major data protection law, December 11, 2019.

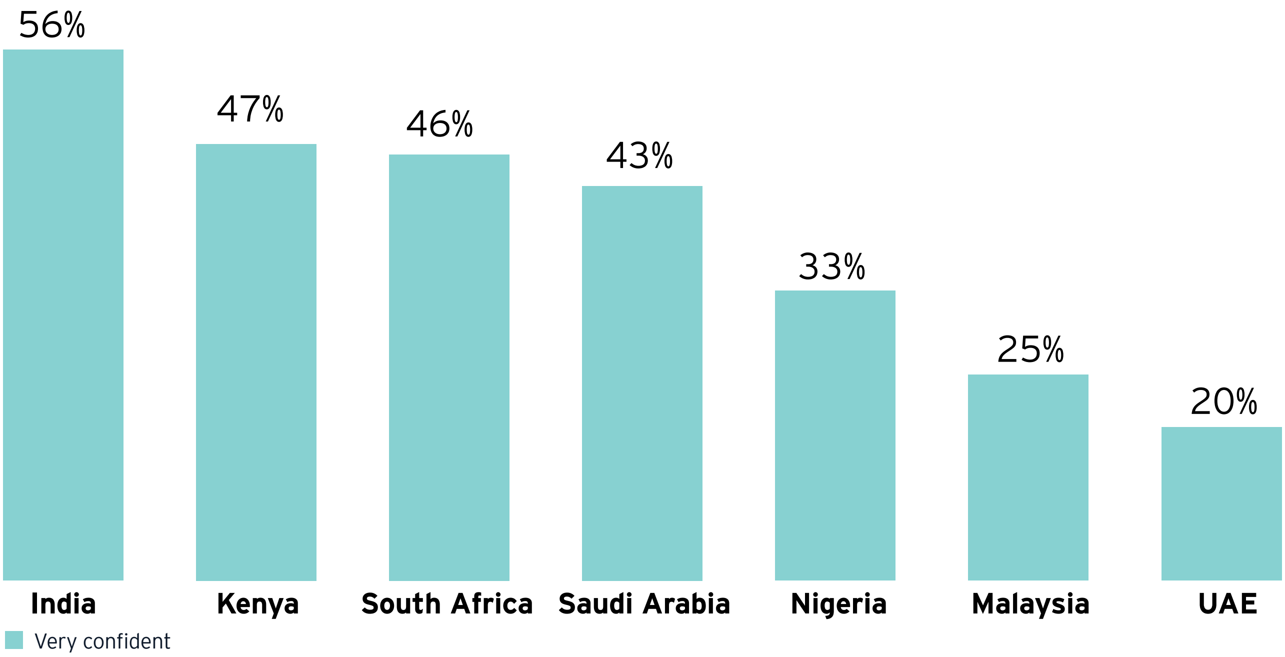
04

Address third-party integrity issues

Businesses' efforts to improve integrity will be undermined if their third parties engage in poor conduct. For example, the reputation of a retailer will likely suffer serious damage if one of its suppliers engages in unethical behavior or malpractice. Similarly, a third party may willfully exploit loopholes, pay bribes, employ child labor, create artificial stock-out situations, "piggyback" on slow-moving stock keeping units (SKUs), sell counterfeit merchandise or take kickbacks from distributors for favorable contractual terms. These acts can not only tarnish the reputation of the retailer, but also lead to financial losses and possible penalties if local or global laws are evaded. For US and UK companies operating in emerging markets, actions by a third-party can also have legal ramifications under regulations, such as the US Foreign Corrupt Practices Act (FCPA) and the UK Bribery Act and the UK Modern Slavery Act.

The survey data reveal that businesses operating in emerging markets are aware of this threat: only 35% of businesses in emerging markets are very confident that their third-party partners operate with integrity; in Malaysia, that figure reduces to 25%. Businesses should not just be concerned with the integrity of their partners in their supply chain. Third-party risk can come from a much broader range of stakeholders, including joint-ventures partners, distributors, consultants and contractors.

Confidence in third-party conduct varies significantly across emerging markets



Question: How confident are you that …? Our third parties, including suppliers, vendors, partners or consultants demonstrate integrity in the work they do.
Base: Global Integrity Report (2,948); Emerging (1,730); India (100), Kenya (45), Malaysia (100), Nigeria (60), Saudi Arabia (75), South Africa (100), UAE (100)

31%

of companies in emerging markets have processes or training in place around third-party due diligence.

Despite the challenges, there are some promising signs: 31% of companies in emerging markets have processes or training in place around third-party due diligence.

With remote working, restricted operations and limited mobility, COVID-19 has made it harder to assess third-party risk. Nationwide lockdowns imposed during the pandemic have caused significant damage to supply chain networks, with many companies either overlooking misconduct or lapses, possessing limited control and oversight over current vendors, or engaging new vendors without conducting adequate due diligence. In person site visits have become difficult; internal reference checks and informal discussions to identify issues or gaps may not be possible.

Challenging times such as these require businesses to rethink how they assess third-party risk. As a starting point, they should prioritize evaluating their most important third parties and ensure robust screening is undertaken in proportion to the increased risks, while not forgetting any additional risks arising from subcontractors used further down the supply chain[18].

Implementing a robust third-party due diligence program

Conducting adequate due diligence before onboarding a third-party vendor is critical to mitigate long-term risks and comply with enforcement standards. These checks should typically cover information gathered from publicly available sources to ascertain negative reports, involvement in litigation, loan defaults, bankruptcy, regulatory noncompliance and criminal activities. They may highlight potential areas of concern, such as omission of key directors or shareholders, limited information or history available, and irregularities in processes. Organizations should make third-party due diligence a periodic exercise and not just a one-off activity, as the nature, type of risks and regulatory ambit will continuously evolve with time.

Third-party onboarding processes should be looked at from a risk perspective through a proper contract, with appropriate contractual audit rights. It's also vital for businesses to provide ongoing training to third parties about which laws and policies they must adhere to, including compliance certifications in their jurisdictions.

Technology and digital solutions can be enablers to bring efficiency into the third-party due diligence process. For example, automated dashboards can be deployed to streamline some monitoring processes, and data analytics can be used for automated risk scoring and to spot issues that may require deeper investigation.

[18] EY, "COVID-19: Four key steps for managing integrity risks in supply chains" May 20, 2020.

Conclusion

Now is the time to create long-term value through integrity

Businesses will always face risks to their integrity. Managers under pressure may be tempted to bribe. Cyber threats have the potential to expose personal data and are becoming more complex, rampant and harder to spot. And the growing ecosystem of third parties creates further points of vulnerability.

The survey data demonstrates that companies operating in emerging markets acknowledge the scale of these challenges and are moving toward taking positive steps to address them.

But there is much more work to do. New laws, stricter enforcement of existing regulations and tougher penalties mean it is now imperative to focus on improving corporate integrity. In doing so, businesses should not just focus on the traditional aspects of integrity, such as fraud, bribery and corruption, but also on new measures including environmental, social and governance (ESG) criteria. Importantly, business leaders must convey to the entire organization that improving integrity is vital not just because regulation requires it, but because it is the right thing to do. There is also a strategic and financial incentive. Increasingly, customers will only purchase from and employees will only work for businesses with ethically sound practices.

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Business leaders need to champion a culture of integrity and good governance, and take practical steps to evaluate and address fraud, bribery and corruption risks. An effective, sustainable integrity and compliance program with commitment from the top management is critical.

Rajiv Memani
Chair, EY Global Emerging Markets Committee, EY India Chairman and Regional Managing Partner

For more information, visit ey.com/emergingmarketsreport to explore further EY insights on this topic.

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