Enterprise Risk Management’s Value Proposition

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Key message:

If you don’t seize market change by leveraging risk...

1. then somebody else will.
2. then you are at risk.
Perpetual uncertainty...

“Microsoft is always two years away from failure”

Bill Gates
People trends

Psychological mobility
Time pressures
Continuous learning
New working patterns
Electronic education
Cultural education
E-tutoring
Empowerment of individuals
Greater access to talent
Global mobility of talent
Technological connectivity
Alternative staffing models
Society trends

Civil protests as democracy
Terrorism & armed conflict
Anti-poverty
Influence of NGO ‘s
Cyber-terrorism
Organised crime
Media power and influence
Personal security
Shadow economies
Cosmetic surgery
Life expectancy
Ageing
Obesity, diets, nutrition
Customer trends

More consumers
Changing customer wants
Consumer landscape
Ethical consumption
Consumer activism
Anti-business sentiments
Consumerism
Health & wellness
Cultural diversity
Sensory
Green products
Demand for innovation
Complexity
Market trends

Regulatory changes
Political instability
Common & open standards
Manufacturing for the world
Global supply chains
Alternative manufacturing centres
Emerging economies’ strength
Growth of Middle East
China
India
Cheaper capital
Deflation
Deregulation
Consolidation
Capacity constraints
Demand for resources
Technology trends

Digitisation
Mobile computing
Leveraging technology
Technology convergence
Security threats
Cyber-terrorism
Cyber-crime
Security leap-frogging
Identity chip implants
Artificial parts
Biotechnology
Nanotechnology
DNA mapping
Financial Services trends

Marketing to female consumers
Growth of healthcare
Product design
Emerging markets
Payment cards
New payment technologies
Over-extended credit
New distribution channels
Consumer debt risk

Alternative investments
Self-directed investments
Worksite distribution
Depolarisation
Pension reform
Pension gaps
Failure of pension products
Alternative medicines
Medical aid alternatives
Self-managed healthcare
Critical illness products
## Today's Business Environment

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ability to identify and manage risks more quickly</td>
<td>59%</td>
</tr>
<tr>
<td>Improved corporate performance</td>
<td>39%</td>
</tr>
<tr>
<td>Cost reduction through reduction in duplication and identification of synergies</td>
<td>26%</td>
</tr>
<tr>
<td>Greater confidence among external stakeholders</td>
<td>24%</td>
</tr>
<tr>
<td>Ability to identify opportunities more quickly</td>
<td>24%</td>
</tr>
<tr>
<td>Greater confidence that key activities are not falling through the cracks</td>
<td>24%</td>
</tr>
<tr>
<td>Improved control environment</td>
<td>21%</td>
</tr>
<tr>
<td>Improved financial and non-financial reporting</td>
<td>21%</td>
</tr>
<tr>
<td>Ability to support business units more effectively</td>
<td>13%</td>
</tr>
<tr>
<td>Improved assurance environment</td>
<td>10%</td>
</tr>
<tr>
<td>Other, please specify</td>
<td>1%</td>
</tr>
<tr>
<td>None of the above – we do not consider greater convergence to be of benefit</td>
<td>1%</td>
</tr>
</tbody>
</table>

Source: *The convergence challenge*, Feb. 2010, KPMG in cooperation with the EIU
What value do you want from risk management?

- Risk Strategy
- Risk Identification
- Risk Governance
Strategic insights

Risk Strategy

- Take more risk?
- Reduce risk?
Typical risk management structure

- Board of Directors
  - Audit Committee
  - Risk Committee
- EXCO
- Divisional Management
  - Risk Assessments
  - Risk Controls
  - Risk Interventions
- Divisional Management
- Divisional Management
Typical risk management structure

Board of Directors

Audit Committee

EXCO

Risk Committee

Divisional Management

Risk Assessments

Risk Controls

Risk Interventions

Divisional Management

Divisional Management

“The goalkeeper model”
“Opportunity-focused” risk management structure

1. Customers
   - Customer Support
   - Sales & Marketing
   - Customer Retention & Acquisition
     - Customer Delivery
       - Management
       - EXCO
       - Board of Directors
“Opportunity-focused” risk management structure

Customers

Customer Support

Sales & Marketing

Customer Retention & Acquisition

Customer Delivery

Management

EXCO

Board of Directors

“The goal-scoring model”
Risk insights

Exposures

- Major
- Moderate
- Significant
- Minor

Likelihood of Occurrence

-1.0 -0.8 -0.6 -0.4 -0.2 0 +0.2 +0.4 +0.6 +0.8 +1.0

Opportunities

- Considerable
- Significant
- Moderate
- Minor

Impact on strategy and objectives

Downsides

- Considerable
- Significant
- Moderate
- Minor

Regrets

- Considerable
- Significant
- Moderate
- Minor

Opportunities

- Considerable
- Significant
- Moderate
- Minor
Top commercial risks

Initiatives to correct variances by seizing opportunities are selected.

TOP COMMERCIAL RISKS

3 Loss of profitable clients
4 Insufficient new business acquired
7 Emerging competition
8 Downward pressure on price

RISK-TAKING ACTIONS

C1 Make an acquisition
C2 Sell more specialisation services
C3 Cultural matching of services
C4 Use new media to deliver services
C5 Sales strategy to switch providers
C6 Reputation enhancing services
Top commercial risks

TOP COMMERCIAL RISKS

3 Loss of profitable clients
4 Insufficient new business acquired
7 Emerging competition
8 Downward pressure on price
Strategic benefits: case studies

A mobile phone operator used risk information as the platform to shape its business strategy

A central bank combined its risk and strategy planning processes

An oil & gas company identified the top risks facing its new growth strategy

An airport management company integrated risk indicators into its balanced scorecard system
Strategic benefits: case studies

A security company conducts a country risk assessment to determine strategy and decided against market entry.

A retail group saved $$$ in a strategic decision to diversify supply chain risk.

A packaging group uses risk information as a predictive mechanism to track competitor and customer trends.
What do you want from risk management?

- Risk profile?
- Quantify risks?
Risk Profile

Top 10 Risks

1. Loss of building, together with key staff or technology infrastructure
2. Adverse changes in law and government affecting the company’s business model
3. Loss of market share or revenue through competition or regulation
4. Introduction of competing products and technologies by other companies
5. Inability to attract and retain key employees
6. Failure to develop global management and information systems
7. Exposure to litigation related to the company’s products/services
8. Deficient products/services provided, loss of reputation
9. Changes in legal, economic or regulatory environment
10. Changes in legal, economic or regulatory environment
What do you want from risk management?

- Risk Identification
- Quantify risks?
Potential impact of top risks on PBT

![Graph showing potential impact of top risks on PBT]

**TOP RISKS**

1. Hostile regulatory change
2. Loss of operating licence
3. Market maturity
4. Brand erosion
5. Increase in trade levies
6. Strike & labour disputes
7. IT infrastructure failure
8. Increasing middle-market competition
9. Growth of new entrant products
10. International ventures
11. Failure to capture targeted market
12. Major natural catastrophe
13. Online competition
14. Perception of customer safety
15. HIV and Aids

**Area of impact on corporate performance**

- Revenue
- Net Operating Expenses
- Impairment of Assets
- Finance Income
- Finance Costs
Potential impact of top risks on PBT

Value at risk: $3.3bn

Considerations:
- correlations
- aggregations
- timing
- indirect costs
- non-financial impact
- proportional exposure
- acceptability?
Quantification benefits

A cash-carrying company negotiated insurance premium reductions due to its risk management performance

A fishing company diversifies its income due to market volatility with the aid of risk insights

A transportation company implements risk processes to reduce losses

A public entity implements enterprise risk management as part of its turnaround strategy
Quantification benefits

A listed company is rated by analysts as a top ten emerging market investment proposition, in part due to good governance.

A hospitality chain implements enterprise risk management in response to shareholder activism.

A telecommunication company uses enterprise risk management to assist in securing government funding.
Risk appetite

Decision A: there is a 1% probability of 100 fatalities

Decision B: there is a 100% probability of 1 fatality
What do you want from risk management?

- Better risk governance?
- Assurance?
“Risk management must be an integral part of strategic planning and capital allocation processes…

…not just a passing agenda item briefly discussed during a board meeting.”
Visual Metaphor

GRC GUIDING PRINCIPLES

Technology

Governance, Organization & Infrastructure
  - Accountability and responsibilities

Enterprise Assurance
  - Continuous monitoring
  - Effectiveness and efficiency review
  - Integrated reporting

Risk Profile
  - Risk drivers
  - Emerging Risks
  - Interdependencies

Culture & Behavior
  - Motivation / incentives
  - Ethics and compliance

Business Processes

MISSION

- Strategy
- Values
- Business Model
- Value Drivers

RESILIENCE

- Compliance
- Performance
Governance benefits

A pension fund administrator uses enterprise risk management to implement organizational changes

A short-term insurance company used enterprise risk management to develop an internal control framework

A diversified manufacturer implemented a risk-based integrated audit process

A clothing company designed a joint assurance plan between Internal Audit and Risk Management staff
Governance benefits

A listed company initiated audits of suppliers after an enterprise risk management review

A mining group holds governance and risk training for its board of directors

A petrochemical group prevents a product recall through an enterprise risk management intervention

A provincial government used enterprise risk management to improve its governance processes and enhance reputation
How did the case-study companies succeed with ERM where many do not?

1. Intelligent design

2. Business planning is centre-stage

3. ERM is a catalyst for value
Thank You!