

Managing risk in turbulent times

Part 1: Getting the fundamentals in place

ADVISORY

Do you understand the risks your business is exposed to and how to manage these risks? Are there risks you may have overlooked?

Businesses with weak risk management fundamentals often find themselves vulnerable to unexpected surprises or to a turn of events. This is especially so during turbulent times where the horizon is still unclear. However, what is clear is the need to assess the fundamentals and priorities of your business and pool the required resources for charting the course to success.

Are you managing risks in silos?

The current economic crisis has illustrated how a systemic failure can result in multiple risk events occurring concurrently, due to their interconnectivity.

What this highlights is the need to assess risks in totality as a portfolio. While not a new concept, many organisations still manage their risks in silos instead of embracing a holistic approach to risk management. This prevents them from fully understanding the extent of their risk exposure.

When not properly mapped and analysed, the underlying correlation among different risks within an organisation may trigger unexpected surprises: this is something most businesses would not welcome in the current economic climate.

Businesses should take a hard look at their fundamentals and assess if new risks may be looming. Given the numerous competing priorities in these turbulent times, this may be challenging. However, businesses must remain vigilant and resilient. They should always balance downside risks with longer-term opportunities.

How risk-ready are you?

Risk management should be proactive in nature. A mature risk management framework complements this by being a strategic enabler in supporting an organisation's pursuit of its business objectives. A risk-managed organisation is also typically rewarded with higher valuations from financial markets, higher credit ratings and lower costs of obtaining capital.

A review of your existing risk management programmes should reveal the state of your business' resilience to adverse changes in the business environment. It may also provide the strength to rebound from any unforeseen setback.

Risk priorities and concerns of Audit Committees

Top Priorities

1. Risk management
2. Accounting judgments and estimates
3. IT risk and data security
4. Internal controls

Top Concerns

1. Recession-related risks
2. Risk intelligence
3. Increased risk of earnings management
4. Tone at the top, culture and incentives

Source: *The Audit Committee Institute 2007-2008 Public Company Audit Committee Member Survey*, KPMG International



"To succeed in turbulent times, businesses need to manage the interconnected network of risks holistically"

Irving Low
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Disparate and misaligned risk management programmes are often a sign of weaknesses in the corporate governance framework. This may be worsened by differing appetites and levels of tolerance to risk in an organisation, and by a generally reactive approach to risk management.

A formalised risk management programme should not hold back an organisation's pursuit for performance. Rather, it may be likened to the braking system in cars which serves to help ensure a safer journey to the final destination.

It is important for organisations to consider both risk and rewards. Proper measurements and responses with returns adjusted for risk exposure can help create longer term and sustainable stakeholder value.

Complete the 'health check' below - how many questions can you answer 'yes' to? The more questions you know the answers to, the better your organisation is likely to be equipped to manage risks.

| | |
|--|--|
| <input type="checkbox"/> Do you know the top risks your company faces? | <input type="checkbox"/> Are incentives to top-management affected when a risk event results in a loss? |
| <input type="checkbox"/> Does everyone in the company share a consistent view of the risks which the company faces? | <input type="checkbox"/> Is the person responsible for risk management programmes in your company a member of senior management? |
| <input type="checkbox"/> Is your company's risk profile constantly updated to reflect market trends? | <input type="checkbox"/> Is risk management integrated with your planning and budgeting cycle? |
| <input type="checkbox"/> Are one or more of the following programmes integrated into your company's overall Enterprise Risk Management framework? | <input type="checkbox"/> Is company performance risk-adjusted? |
| <input type="checkbox"/> Financial risk management | <input type="checkbox"/> Is a risk communication strategy in place to facilitate communication of risks to appropriate stakeholders at the right time? |
| <input type="checkbox"/> A comprehensive insurance programme | |
| <input type="checkbox"/> A business continuity plan | |
| <input type="checkbox"/> A crisis management plan | |
| <input type="checkbox"/> Are risks at the divisional / departmental, project, investment and subsidiary level considered part of your overall risk management programme? | <input type="checkbox"/> Are your board of directors and management clear of their roles and responsibilities for corporate governance? |
| <input type="checkbox"/> Is there a consensus amongst the board of directors and management on your company's risk appetite and tolerance limits? | <input type="checkbox"/> Is it business-as-usual for your company when adversity strikes? |
| <input type="checkbox"/> Are risks monitored closely enough to allow your company time to respond and react to increasing exposure? | <input type="checkbox"/> Does your company's risk management programme proactively engage the internal audit function in managing risks? |

Recognising all the 'connections'

Integrating the Enterprise Risk Management framework with the business and rationalising the risk management processes are critical in any attempt to steer a smooth course through the uncertain economic times ahead. The consideration of the relationships between various risks may also reveal a greater complexity in the operating environment than originally assumed.

Managing risk in turbulent times *Your guide to this three part series*

Part 1:

Getting the fundamentals in place

- Why risk should not be managed in silos
- Take the risk-readiness "health check"
- Tips to improve your risk-readiness in turbulent times

Part 2:

Staying the course

- How to stay centred during the good times and the bad times
- Focus your energies using "STAR Track"

Part 3:

Moving ahead of the times

- Becoming a more intelligent enterprise
- Creating your own 'risk clock'
- Why you should re-boot your risk management programme

Is risk management a strategic enabler or just a project?

If you answered 'yes' to almost all questions in the assessment, then risk management is likely to be already embedded in your business' day-to-day operations. It may also be playing a strategic role in supporting management decisions. A comprehensive view of risk is readily available for decision-making and there is likely to be a strong tone at the top in supporting the long-term governance and performance agenda in your organisation.

If you have less than the majority of questions answered, a proper review of your risk management might help you pinpoint areas for improvement. At the very least, risk management should be employed to help give stakeholders confidence that risks are effectively managed and that their interests are protected. Nevertheless, improving risk-mitigation strategies should still be considered to increase its relevance to the company and allow for better management of the uncertainties surrounding business objectives.

If you were not able to answer many of the questions, then a review of one existing risk management programmes should be considered to enhance the tools and applicability of the programmes. Your company should review its corporate governance and risk management capabilities to better prepare itself for adversity and to aid in making better informed business decisions. This should be done to help manage the expectations of internal and external stakeholders, and including any requirements of regulators.

Improving your risk-readiness in turbulent times

What are the steps available to your organisation to better deal with risks in these turbulent times?

• Re-examine your business assumptions

Before the crisis descended, many would have heard business assumptions such as: "Liquidity is a given, it's only a matter of the price", "AAA credit rating is a guarantee of the financial standing" or "We are decoupled and insulated from the contagion."

We may now know better. Market situations change. So can organisational behaviour. In managing risks, businesses should be diligent in evaluating any underlying assumptions to help ensure validity under different market conditions. The assumptions that businesses make should be regularly reviewed and updated to stand the test of time.

• Re-align incentives to risks

The compensation structure drives the risk appetite and business outcomes of any organisation. Balancing risks and rewards are key to effective risk management.

It is important that incentives are directed towards rewarding a more effective risk-conscious culture which underpins the long term sustainability of the business rather than just strictly focusing on returns

• Manage, don't just measure

"What gets measured, gets managed" is only a half-truth. Risk measurement is not risk management. Having in place a risk measurement model does not necessarily turn a poor manager into a good manager.

Risk management needs to be embedded as part of 'business as usual', and not relegated to a compartmentalised function performed by a select few. Make your risk management process a rigorous one. With the right fundamentals in place, you can be better prepared to survive any turbulent times.



Contact us

This is the first of a 3-part series which looks at managing risks during turbulent times. The next issue highlights the business areas that organisations should focus on and direct their resources towards.

About KPMG's Risk Advisory Services

KPMG's Risk Advisory Services is a leading risk advisory practice that has gained market recognition through its many successful projects with local and global businesses.

Our multi-disciplinary approach draws on the expertise and insight of our audit, tax and advisory practices within KPMG in Singapore and member firms around the world. We aim to help clients respond to the challenges of governance, risk and conformance in a way that enhances both their business performance and corporate reputation.

Managing in a downturn

The Financial Times in association with KPMG member firms have produced an exclusive four-part series entitled, **Mastering Management: Managing in a downturn**. The series provides a comprehensive guide to the latest research and ideas on how to manage in a downturn, featuring commissioned articles from the world's top business thinkers.

Part One: Surveying the damage

Part Two: Getting through the crisis

Part Three: Looking beyond the crisis

Part Four: The future business environment

To read or download the issues, please visit www.kpmg.com/succeeding

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