

ERM Symposium

 **ERNST & YOUNG**
Quality In Everything We Do

ERM in Corporate Decision Making

April 25, 2006
J. Chris Karow

Risk in Corporate Decision Making

Where is Risk Relevant in Corporate Decision Making?

Simple answer is everywhere.....

- Strategic planning and decisioning
 - Business oversight and management
 - Line Business and operational management
 - Tactical daily decision making
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










Risk in Corporate Decision Making

- How can we embed risk in corporate decision making processes?
 - Where are the greatest gaps in considering risk in corporate decision making?
 - Where is the greatest value created?
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Risk in Corporate Decision Making

What is the role of risk in decision making?

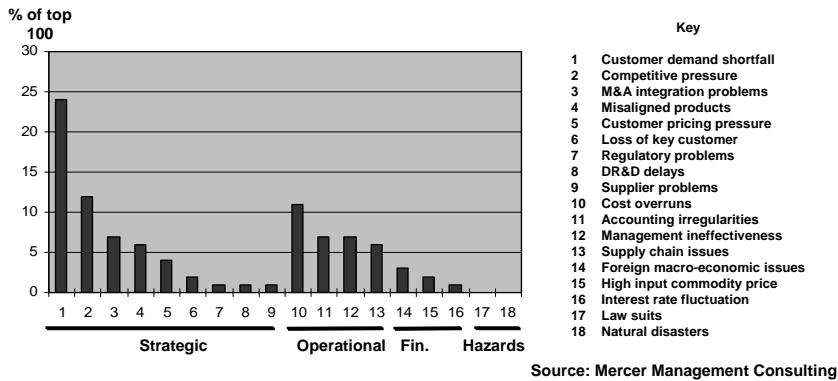
Examples

- | | | |
|--|---|---|
| <ul style="list-style-type: none"> ▪ Tactical business decision making <ul style="list-style-type: none"> • Pricing, • Product management, • Customer suitability, ▪ Line business management and oversight <ul style="list-style-type: none"> • Marketing and pricing • Business portfolio management • Operations and operational risk management • Performance measurement and people effectiveness ▪ Independent risk management and mitigation <ul style="list-style-type: none"> • Risk oversight and aggregate risk decisioning | 









 | <ul style="list-style-type: none"> ▪ Risk & return based pricing models ▪ Risk & return modeled product analysis ▪ Broker and Transaction monitoring ▪ Risk based pricing models ▪ Risk assessment, limits, scenarios, models ▪ Risk assessment, Limits and exceptions, scenarios Key risk indicators and KPIs ▪ Risk assessment, capital and risk & return models, KRIs, outcomes ▪ Risk assessment, limits ▪ Capital and risk & return models, ▪ KRIs, KPIs and outcomes ▪ Risk reporting and dashboarding |
|--|---|---|
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Why does risk matter in decision making

- Primary causes of severe stock drop

One hundred (10%) of the Fortune 1000 companies suffered a loss of over 25% of shareholder value within one month



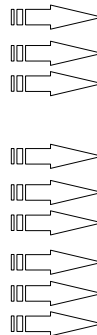
Causes

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Risk in Corporate Decision Making

What is the role of risk in decision making?

- Strategic planning
 - Capital investments,
 - M&A acquisition/divestiture,
 - Competitive & strategic business planning,
- Inflection points
 - New products, geographies, markets
 - New systems and infrastructure
 - New people and processes
- Extreme events and emerging risks
 - Catastrophic events
 - Natural disasters
 - New and emerging risks



Examples

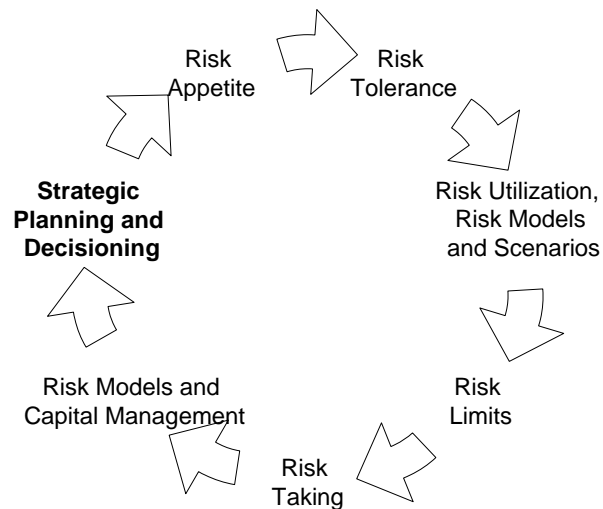
- Investment analysis?
- Economic capital models?
- SWOT, EC Models?
- Risk pricing models?
- New systems reviews?
- Internal audit, risk assessment?
- Catastrophic models, scenarios
- BCP,
- Risk assessment?

Risk in Strategic Decisioning

- Disconnect between risk and corporate strategic planning and decisioning processes
 - Why?
 - Lack of a structured process
 - Risk data and reporting is often times not oriented toward strategic decision making
 - Lack of involvement of risk management personnel in strategic planning process
 - Risk not viewed as opportunity, only as downside management
 - Risk processes often biased toward financial risks and do not focus on all risks critical to strategic decision making
 - Lack of focus on what creates and what diminishes value
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Risk Planning Lifecycle






- Risk appetite, tolerance and limits are not static
- They must be updated with changes in strategy, the environment and market expectations
- Ultimately, they should be a key element in driving risk taking and in turn in performance measurement



Risk in Strategic Decisioning

□ Where should risk be considered in strategic decisioning

▪ Risk as an input into strategic planning

- Capital budgeting and capital investment  Link Economic capital to strategic capital management activities (MCEV, EC, Stat Capital)
 - Capital structure and adequacy
 - Performance measurement
 - M&A/Divestiture
- Business planning and product pricing  Add scenario driven strategic risk assessment and link existing risk identification, assessment and measurement activities to strategic planning
 - Business priorities
 - Customer, Product, geographic focus
 - Concentrations and aggregations
- People, culture, capabilities and succession  Capability/capacity & succession
- New business, growth strategies  Add new business risk management process
- Extreme events  Add extreme events identification/assessment and mitigation processes

▪ Risk as a consideration in evaluating the viability of strategic decisions and managing implementation of strategy

- Strategy implementation activities  Add Strategy implementation risk assessment and mitigation plan

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