The journey and the rewards of Enterprise Risk Management

Imagine building a bridge without knowing which river it should span, or how wide the river is, or whether the environment has a history of flooding, or what kinds of vehicles need to cross it. Now imagine building a bridge that is fit for purpose. It is useful and appropriate for the surroundings. It is strong and resilient.

Enterprise risk management (ERM) done right is like building a bridge that is fit for purpose. An organisation’s ERM journey provides opportunities for clarifying business objectives and articulating risks, designing strategies for managing them and determining the organisation’s resilience and appetite for risk. Most importantly, however, is that ERM done well not only provides comfort to management but also enables risk to be seen as an opportunity towards pursuing the firm’s goals.

The challenge of risk appetite

In almost all organisations, risk appetite setting and articulation simply does not receive the airtime it deserves. For most, their risk strategy forms part of the business’s overall strategy but when it comes to risk appetite the same firms tend to get a bit “lost”. Putting pen to paper for clear articulation of risk appetite statements poses significant challenges. Partly this is because a clearly documented risk appetite necessarily implies accountability and a metric for evaluating performance. In addition, different board members will inherently have different risk appetites. A combination of these and a lack of experience in setting risk appetites means that this is usually a half-baked cookie for most firms.

Risk appetite statements are owned by the Board of Directors and board members are increasingly aware of the benefits of having well-articulated risk appetites that are used to run and manage the business. In our experience, the most effective way of defining your risk appetites is through a Board workshop allowing for deep discussion and with a view to agreeing and setting the appetites. An independent third party can facilitate at any point helping drive consensus more effectively, helping to clarify, providing data and benchmarks and developing a draft risk appetite document for discussion.

The best risk appetite documents are living documents and renewed or refreshed at least once every year, and they also inform business plans for future years. The operating environment will change and a third party can also help Board members and others to peer around the corner and anticipate changes that could inform risk appetite and, therefore, business strategy.

Organisations that set their risk appetite through an integrative process and articulate it clearly find that cascading it through the business is much simpler to accomplish and buy-in much easier to obtain.

But even the most specialised risk expert cannot individually enforce the risk appetite and the wider ERM framework without the explicit involvement of everyone from the Board of Directors through to support staff. Risk management is reinforced by the right risk culture, and that culture should instil confidence and reward staff and management for good risk behaviours. No one should be afraid to talk about risk.

Enterprise Risk Management is a journey

A final analogy illustrates the power of ERM. Imagine driving a car. The rear-view and side mirrors provide different perspectives; these perspectives could be informed by regulator risk assessments or potential risks that may arise. The car’s dashboard provides information
indicating oil level or battery charge or speed; these indicators tell you whether the car is safe to drive and if you can move forward.

Most importantly, you face the windscreen and your perception is real-time. Perhaps it is raining, or a cow crosses the road in front of you. There could be an accident ahead. Or the weather is bright and sunny. Risk management done right is like the windscreen: it gives you a real-time view of what is coming up ahead. Enterprise risk management comprises all of the different views and indicators that allow you to drive safely and strategically forward to reach your goals.

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