

# Rebuilding Trust: Next Steps for Risk Management in Financial Services

A summary of a report produced by the Economist Intelligence Unit and sponsored by SAS

## Findings at a Glance

- Confidence levels are high, but there is a risk of complacency.
- The focus on regulatory compliance may distract attention from emerging risks.
- A clearly defined risk strategy is in place at most institutions, but significant areas of weakness remain.
- Financial institutions are filling gaps in risk expertise with investment in training and recruitment.
- The silo-based approach to risk management continues to pose problems.
- Financial institutions continue to struggle with data quality and availability.

The full report is available at [www.sas.com/ermresearch](http://www.sas.com/ermresearch).

## Overview

The Economist Intelligence Unit conducted a global survey on behalf of SAS to examine how the world's financial institutions are reinforcing their risk management capabilities in response to the global financial crisis. The online survey, conducted in February 2010, attracted 346 respondents – all executives with risk management responsibilities at banks and insurance companies around the world. A series of in-depth interviews with industry and risk experts followed the survey to form the basis of the EIU report. This document provides a summary of the report findings.

The financial crisis had many causes, but failures in risk management have been clearly identified as a contributory factor. Although there were technical shortcomings, especially related to risk models and metrics, a more widespread problem was a failure of governance, as risk managers' legitimate warnings went either unheeded or unnoticed. In the pre-crash credit bubble euphoria, a front office-driven culture too often rode roughshod over risk managers' concerns, and many CEOs were more focused on outperforming revenue and profit targets while paying little heed to growing risk concentrations.

The crisis changed all that. Across the industry, risk management has moved to the center of strategic decision making, and many institutions are revamping their entire approach to understanding and mitigating the risks that they face.

The 2009 report, *After the Storm: A New Era for Risk Management in Financial Services*, found that the majority of financial institutions have been conducting wholesale reforms to the way that they manage risk. If anything, the pace of change has accelerated since then, with institutions reappraising their corporate governance structures, risk functions, data, IT systems and software, and business processes and procedures.

Many banks and insurers have come a long way in their projects to strengthen risk capabilities. Discussions about risk have become a key part of the boardroom agenda, chief risk officers have a prominent seat at the top table, and there is renewed zeal for instilling a greater awareness of risk principles in the front office – the so-called “first line of defense.”

But despite this progress, weaknesses remain. The enthusiasm for large-scale risk projects has created human capital shortages as institutions scramble for the appropriate expertise. Data and IT systems remain significant impediments to an overall understanding of risk exposures, while regulatory uncertainty makes it difficult to plan for the long term.

The final report – *Rebuilding Trust: Next Steps for Risk Management in Financial Services* – includes the complete survey findings along with insights and analysis from industry experts and commentators.

## Report Highlights

### Confidence levels are high, but there is a risk of complacency

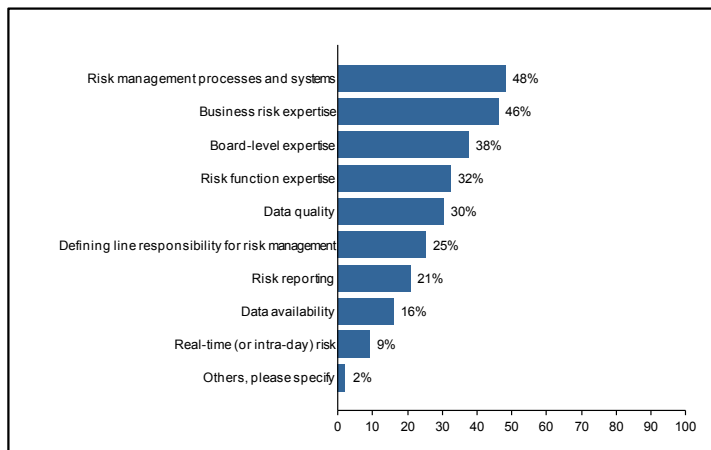
Compared with 12 months ago, financial institutions are feeling much more confident about the future. Around three-quarters of respondents believe that prospects for revenue growth over the next year are good, whereas 68 percent are positive about the prospects for profitability. These levels of confidence, which are around double the levels of a similar survey conducted last year, reflect a widely held view that the financial system has stabilized. There is a risk of complacency, however. As governments withdraw stimulus packages and liquidity support for the financial sector, revenues and profitability could yet fall.

### Focusing on compliance could distract attention from emerging risks

Around the world, regulators have stepped up their scrutiny of financial institutions. While few would argue against a tougher regulatory regime for financial institutions, survey respondents highlight uncertainty over future regulation as the main barrier to effective risk management. There is a danger that the focus on compliance could be “crowding out” day-to-day risk management at a time when formerly uncommon risks, such as sovereign debt crises, are becoming more commonplace.

### Most institutions have a risk strategy in place, but weaknesses remain

Investment in risk management is increasing almost across the board, with risk processes, data, IT and training being key areas of focus for most.



**From the survey: In which of the following areas do you think the most significant focus should be to address current shortcomings in risk management?**

Six out of 10 respondents now say that they have a clearly defined risk strategy in place that is updated regularly. However, this still leaves a worrying 40 percent who do not conduct regular updates or do not have a clear risk strategy in place.

### Investment in training and recruitment is filling gaps in risk expertise

Respondents recognize that gaps in risk expertise have been an important part of the problem in risk management. Asked about key focus areas to address shortcomings, respondents list issues related to expertise as three of the top four priorities. More than half say that they are increasing their investment in training, both of risk professionals and across the broader business, and a similar proportion say that they are spending more on recruitment.

### The silo-based approach to risk continues to pose problems

During the crisis, the separation of risk into separate departments led many financial institutions to underestimate risk concentrations and correlations.

Even now, less than half of respondents to our survey are confident that they understand the interaction of risks across business lines, and poor communication between departments is seen as a key barrier to effective risk management.

### Institutions continue to struggle with data quality and availability

An over-reliance on risk models, and problems with the data used to populate those models, have been widely seen as key failures in financial risk management. Today, financial services firms recognize that data quality and availability need to improve. Collecting, storing and aggregating data is an area of weakness for many institutions, with only 39 percent of respondents overall believing that they are effective at these activities.