

The New Risk Paradigm: Non-Financial Risk Management



Event Research Report

August 2020

Contents

03

Summary

04

Research Results

05

Conclusion

09

Appendix 1 – Research Results

10

Appendix 2 – About Participants

11

Appendix 3 – People Contributed to the Report

13

About Fitch

Summary

The prominence of non-financial risks in financial services is becoming more prevalent and is being recognized as the emerging key area of risk management. On 30th June 2020 Acin and Fitch Learning conjointly ran a webinar to a global audience of risk management experts and senior L&D professionals, interested in knowing more about this topic and learning how non-financial risk management is changing to a new paradigm.

This paper summarizes the interactive feedback from a series of polls taken at the time of the webinar - and sets the context for the transformation that is happening within leading firms in the financial services sector, highlighting the opportunity that this paradigm shift represents for the whole of the industry and how Acin, with its focus on data and data-driven insights, is helping to make the whole sector safer.



Research Results: The New Paradigm in Operational Risk Management Towards NFRM Data and Insights



“NFR has far reaching consequences and it goes beyond just one department or one function. It hits every part of the organization and it really is an all encompassing discipline.”

Rupal Patel, Data & Insight Director at Acin

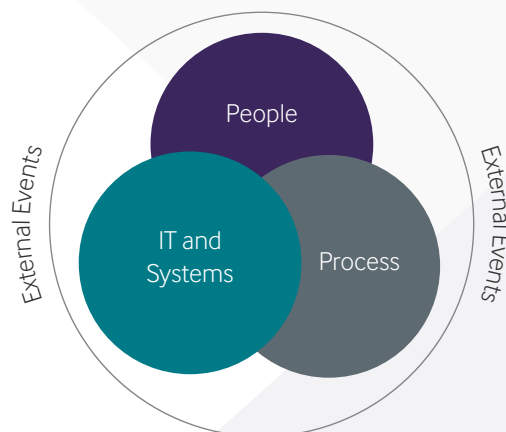
Introduction

The profile of non-financial risk management (NFRM) and operational risk within the financial market industry has changed significantly as a result of COVID-19. If the crisis of 2008 raised our awareness, what we are now facing has made us realize its far reaching impact and is driving the need for risk management experts to improve their understanding of it, to better manage risks and mitigate their effects.

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.¹

COVID-19, the current external risk event, has already had a big impact on three key organizational elements in many financial services firms, namely People, IT and Systems and Process, as illustrated in the diagram below:

- **People:** With staff forced to work from home, the exposure to conduct risk has greatly increased. Control environments have been weakened and management are not able to physically oversee staff. This also raises a longer-term issue of exactly how staff are going to be managed and developed.
- **Process:** Existing processes are being placed under extreme pressure with the shift to home working and then the application of new processes as staff return, given the need for social distancing and deep cleaning.
- **IT and Systems:** The need to purchase additional remote working equipment, often at short notice, and reliance on third parties for critical systems and support; you're only as good as your weakest link.



Also, with media focus on the role of the financial sector in restarting many economies globally, the reputational risk for any firm is heightened.

Now, more so than ever before, we need quality data and information, both internally and externally sourced. This will become key in the management and mitigation of the operational risks we now face.

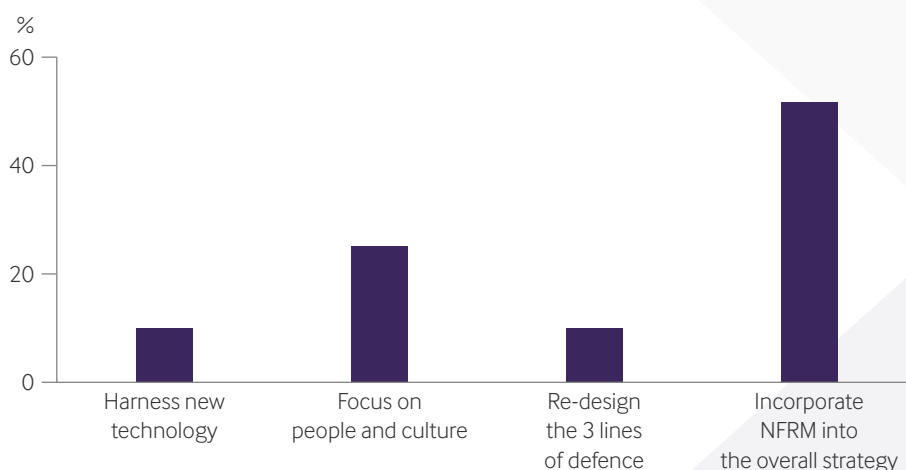
The NFRM and operational risk landscape has changed, and it will not be returning to the way it was; COVID-19 has started a revolution, and we need to evolve to meet the challenges and thrive.

¹ <https://www.bis.org/publ/bcbs195.pdf> page 3

Research Findings

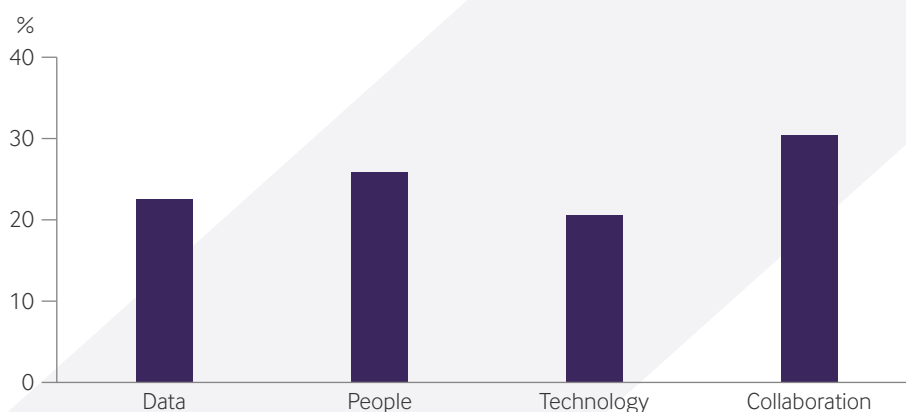
Incorporating NFRM into a holistic strategy is the best way to deliver on its risk management promise, harness technology, set the right culture and connect organizations. The level of collaboration expected and desired can be provided through adequate knowledge and use of technology, that is specifically designed to connect financial organizations via well defined, codified and comparable NFRM data (risks, controls and relevant attributes), generating harmonized data and data-driven insights.

Which of the following would you consider to be the most important factor to effectively manage NFR?



Source Fitch Learning survey, 30th June 2020: Out of over 150 people surveyed, 52% stated that they would consider incorporating NFRM into the overall strategy.

What do you think is the biggest influencer to accelerate and embed NFRM into your organization?



Source Fitch Learning survey, 30th June 2020: 30% of the people surveyed think Collaboration is the biggest influencer to accelerate and embed NFR into their organization.

Let's rewind ... how was NFRM put on the risk map (from 2008 crisis to C-19)

Operational risk and by extension NFRM rose to prominence in the aftermath of the 2008 financial crisis, following severe governance failures, conduct issues and risk management negligence. Basel II (the international capital framework) responded by highlighting the need to raise standards in banking and strengthen risk management practices to create a more stable banking system.

Financial organizations restructured their approach and strategy to control their business operations. Evidence of the measures put in place included new functions embedding the concept of the 3LoD,

considerable RWA set aside for operational risk and a continuous evolution of controls and mappings to risk frameworks often with external consultants. All of these were costly strategies, rigid in nature given their inherent foundational approach – i.e. policy/principle/people-based ('the 3 Ps'). They were built in a 'silo' by external consultants, or independent functions within a bank, with little consultation across the enterprise and with limited recognition of the sophistication risk and control fields required.

From Control Management to Risk Management

Meeting the continuums of regulatory requirements is integral to the management of risk, but adding controls to risk frameworks over time in a fragmentary fashion, without a risk lens, is equivalent to using plasters for a broken limb: its effectiveness is diluted, it creates a false sense of protection and silently increases risk

(e.g. control proliferation vs. genuine risk being logged causing the maintenance of NFRM data to become a mechanical, siloed process making it difficult to keep sight of risk management in a fluid manner).

Where do we stand now...?

COVID-19 as the manifestation of a severe non-financial risk has shown us that NFRM has far reaching consequences impacting people, process, systems, internal and external to the organization; NFRM is like the sun's rays reaching into and enveloping all parts

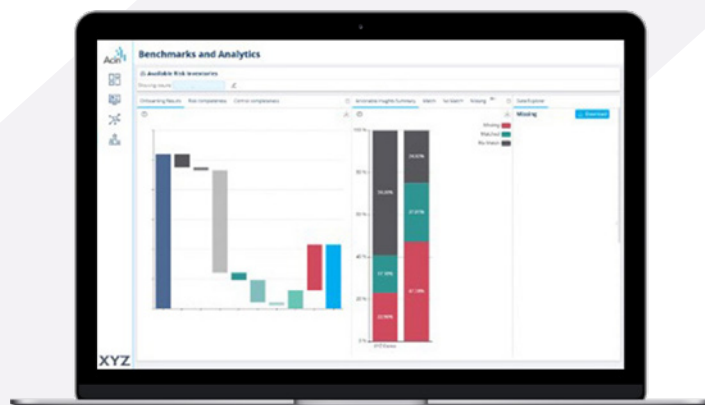
of the firm, it really is an all-encompassing risk pillar. We are all data inundated, but risk-starved and need the digitization of data to take center stage given the increasing demands on NFRM (shareholders, investors, regulators).

New levers for Risk Managers ... Data, Network, and Collaboration

NFRM is under rapid transformation, with financial organizations aiming to smart-manage non-financial risks with **data** curated through **Network** collaboration, and **technology-enabled**.

Firms now require an in-depth knowledge of data, analytics and intelligence, supplemented by systems with standardized items to deliver the relevant risk controls. As it has been observed, one firm's operational risk is another's credit risk; recognizing cross-risk pillar connectivity collaboration is pivotal to meet increasing demands and open the doors to competitive advantage.

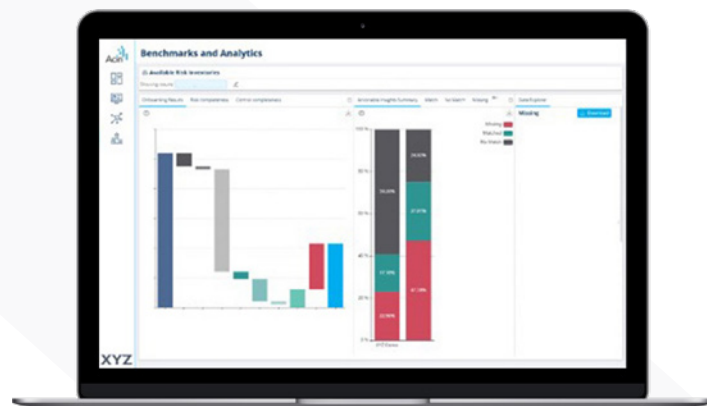
NFRM data is essential for risk management. Firms need to unlock the value in their data, too often ignored today, or not understood or valued, left proliferating or updated too infrequently for risk management use (e.g. annually).



Source Acin: The Acin Network, consists of a data-driven collaborative model using software as a solution to digitize NFRM and address current and incoming challenges (think Operational Resilience and regulatory regimes post COVID-19 as an example).

Data is the fuel to the NFRM engine. It is being standardized, organized and in time will be overlaid with meaningful real time sensors to create data lineage across the organization; a “NFRM pulse” eventually replacing and/or refining manual control processes to indicate where control testing is needed. Adopting this data-driven approach will enable a data catalogue within banks, shaped by a network of peers ... one that can be trusted and be given a voice to create actionable insights. Only once this has been committed can the second line of defense truly partner with the first line of defense and help them by providing assurance over controls that may not be strong enough, or by descoping assurance activities where controls are strong enough. In effect possibly merging the 3LoD abstract construct for a more fluid and data-fueled model.

Existing tools only enable internal data consolidation, reporting and warehousing, too often offering limited sophisticated functionalities for dynamic NFRM which forces resources to be allocated to ‘excel/spreadsheet management’ instead of NFRM management. Data consistency which enables internal coordination has been a struggle for most organizations as front to back controls continue to operate in silos regardless of attempts at enterprise wide risk



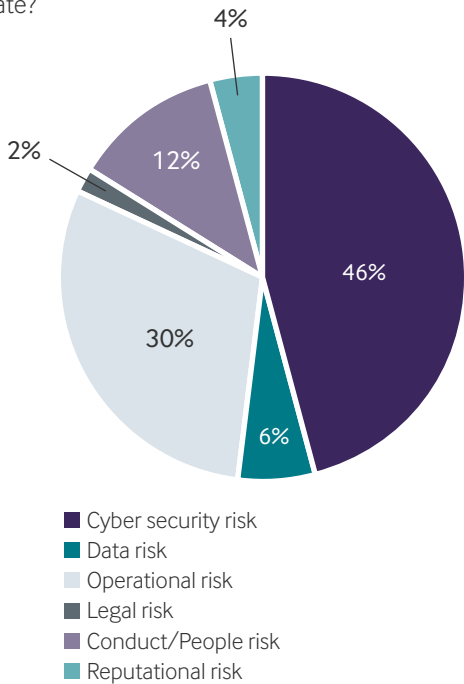
Source Acin: The Acin Network can deliver part of the solution (Network, Data, Technology), other FinTechs offer contiguous solutions (e.g. specialization on regulatory texts scrapping).

frameworks. A platform such as the one developed by Acin, the Acin Terminal, connects network members through their contributed data: mapped, processed, and analyzed to deliver on-demand risk intelligence and actionable insights. No opinion from external consultants, no judgment – hard data, turned into information intelligence and insight.

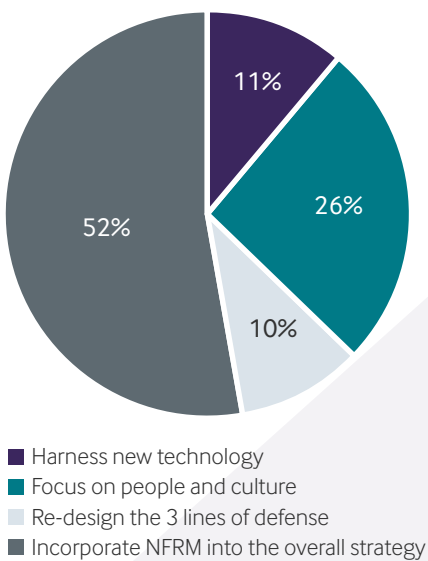


Appendix 1

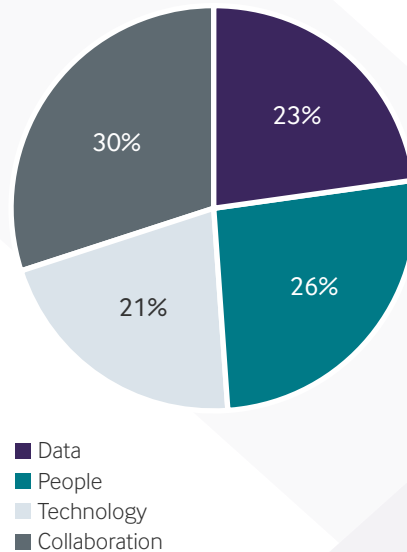
1 Which of the following non-financial risk categories do you consider to be the most important to focus on in the current climate?



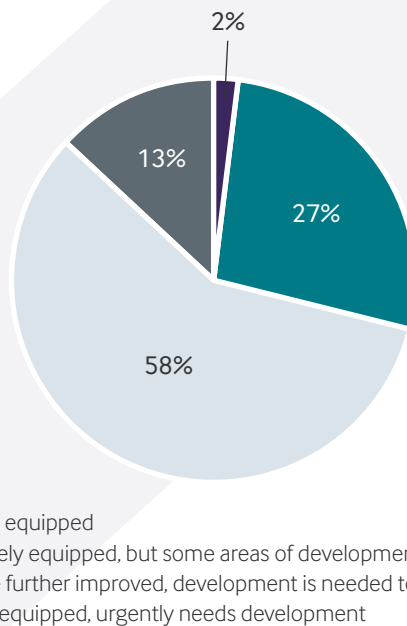
2 Which of the following would you consider to be the most important factor to effectively manage non-financial risk?



3 What do you think is the biggest influencer to accelerate and embed non-financial risk management into your organization?



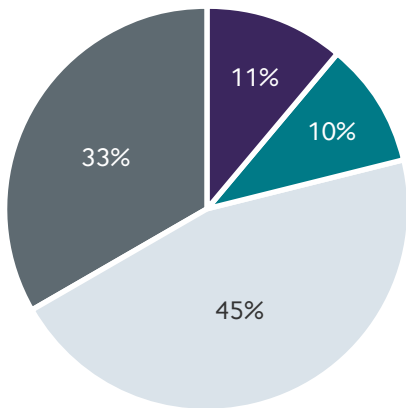
4 How well do you think the general financial services workforce population is equipped to deal with non-financial risk in the post COVID environment?



Appendix 2

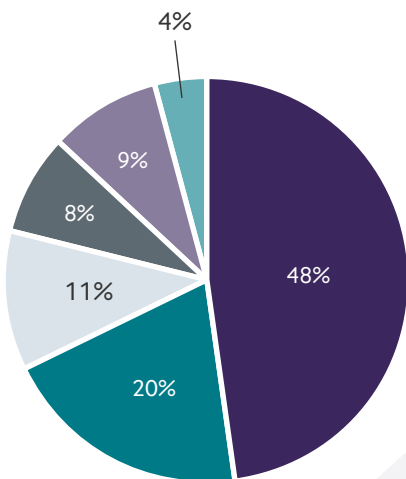
Key stats

143 attendees

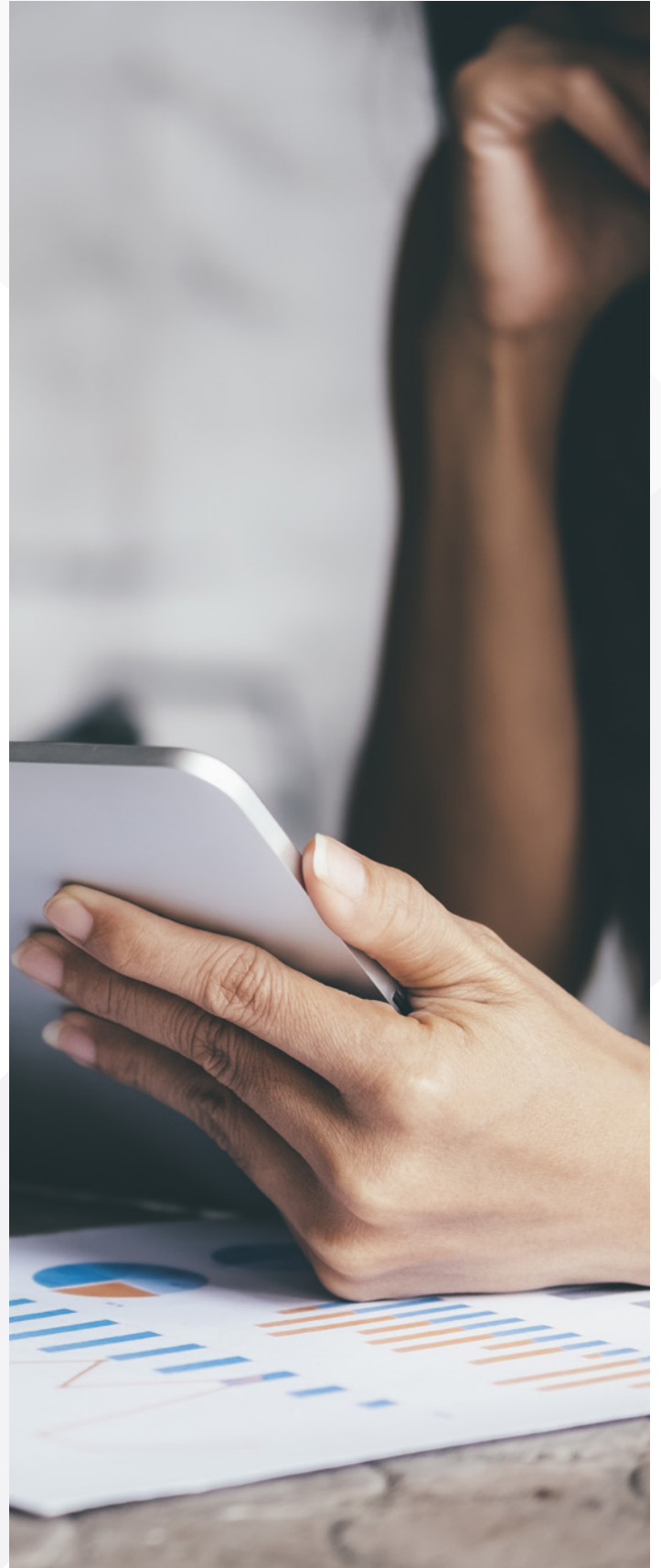


- Americas
- APAC
- Europe
- MEA

100 different companies attended



- Others
- Managers
- Director / CEOs
- Business Heads & Senior Executives
- Analyst
- HR



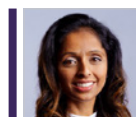
Appendix 3

The following people contributed to the report:

**JACOB WAI**

Director, Asia-Pacific, Fitch Learning

Jacob is Director of Fitch Learning Asia Pacific, focusing on delivering a professional learning platform in the areas of Credit, Risk and Finance and Fintech. Jacob is also working on growing the operations of our Asia presence through partnerships and implementation of the market strategy to complement the offering for clients from Fitch Group. He has over 20 years of experience in Finance and Technology field, with the last role being a Chief Risk Officer of a Virtual Bank applicant in Hong Kong, a Chairman of a standing committee on Operations & Data Governance in a regional bank and over a decade of Regulatory Risk Technology and Reporting management experience in large G-SIBs. He is the author of the risk textbook used in the Certified Bankers program and is also an Adjunct Lecturer of a local university in Hong Kong.

**RUPAL PATEL**

Data & Insight Director at Acin

Rupal is part of Acin's Data & Insight Directors specializing in Electronic Trading across financial Services.

She has extensive experience at Tier 1 Banks with expertise in Front Office, Finance and Operational Risk and has successfully tackled topics ranging from Supervision to regulatory questions on the design and creation of risk frameworks. Rupal is passionate about NFRM and has the experience, understanding and sensitivity to leverage Acin to solve client challenges across all functions. Rupal is also leading the Acin Network's 'Women in Control' initiative aimed at developing further female leaders in the NFRM industry.

**CHRISTOPHER J PENNINGTON**

Financial Trainer, Fitch Learning

Chris is one of Fitch Learning's leading senior trainers with over 15 years' experience in the classroom and the learning and development environment.

Chris draws upon a successful career in financial services that has spanned over 20 years. He began his career in securities services, where he gained a broad knowledge of financial markets, operational areas and the inherent risks. Chris progressed to client relationship management, where his expertise and knowledge was used to service a global client-base, often addressing and resolving operational risk issues.

Chris worked for leading global financial institutions including HSBC, Deutsche Bank and Thomson Reuters.

**GASPARD BIOSSE DUPLAN**

Head of Risk Insight at Acin

Gaspard is Acin's Head of Risk Insights and is playing a leading role in the industry transforming it to a network data-driven approach for NFRM.

He has extensive NFRM experience across all lines of defense in Investment Banking and Risk Consulting with expertise in Front Office, Market Risk and Operational Risk. He has a particularly strong track record in risk management for trading business ranging from control platform optimization and regulatory remediation, through to successfully managing day-to-day risk and control environments. This has provided Gaspard with considerable insights and knowledge of NFRM data and enabled him to play a key role in how Acin solves industry challenges through network data-driven insights. He previously held the position of Head of Market Risk Controls & EMEA Head of Market Risk Regulatory liaison at Barclays. He is a thought-leader on the transformation of Operational Risk and lectures widely on this topic and also contributes to leading publications and news outlets.

Our Business

Fitch Learning partners with clients to deepen knowledge, develop skills and enhance conduct, delivering positive business outcomes.

With centers in established financial hubs including London, New York, Singapore, Dubai and Hong Kong; we are committed to understanding complex client needs across fast paced Financial Markets, globally. Our learning solutions encompass expert faculty, e-learning, coaching and blended candidate assessments, improving individual contribution and collective business performance.

FitchGroup

is also comprised of:

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FitchSolutions



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FitchVentures

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www.fitchlearning.com

 www.fitchlearning.com/linkedin

 www.fitchlearning.com/twitter

Europe: clientservices@fitchlearning.com | T: +44 (0)845 072 7620

Americas: usclientservices@fitchlearning.com | T: +1 800 974 0394

Asia Pacific: clientservices@fitchlearning.com | T: +65 6327 1581 (Singapore) | T: +852 2263 9980 (Hong Kong)

Middle East & Africa: meclientservices@fitchlearning.com | T: +971 800 72489