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How a risk team adds value

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What would our successors do?
Andy Grove, Founder and CEO of Intel

Since 2008 the Joint Risk Management Section, sponsored in partnership by the Canadian Institute of Actuaries (CIA), Society of Actuaries (SOA) and Casualty Actuarial Society (CAS), has annually conducted a Survey of Emerging Risks. As the researcher for this project, I have asked open-ended questions thought to be useful to risk managers. Andy Grove noted the importance of viewing problems from an outsider's perspective. After a strategy he implemented had struggled, he hypothesized how the strategy would change if he was fired. This paper summarizes activities that are perceived as adding value by risk managers.

Each company is unique based on the skill set of the risk team and needs of the firm, many of which are strategic and can be fulfilled through well thought out scenario testing. These can be split into eight themes.

Provide input to risk committee

A fully functioning risk team will interact regularly with the risk committee and the board. The risk committee seeks out unbiased input to make decisions. Several respondents shared their experience, with some stating that they had been asked to provide detailed analysis on specific projects with others providing general input on all projects being contemplated. It was noted that recommendations are not always implemented.

Recurring risk reports

Some risk teams generate periodic sensitivity tests, along with other risk reports. These allow quicker response times when markets move or claims spike, improving resiliency even if the specific event was not modeled. Specific requests from external stakeholders may also be fulfilled by the risk team (e.g., detailing exposures following a hurricane or wildfire event).

Respond to board requests

Board members often request the risk team, independent from risk owners, to look at a broad range of issues. Projects have considered merger and acquisition opportunities versus internal growth and looking at competitive trends. Risk teams also ask broad questions; examples include the impact of low rates and how Brexit would impact operations in Canadian and U.S. subsidiaries.

Holistic ideas – endogenous

Natural hedges (where one risk diversifies another through negative correlations, without having to purchase a hedge or reinsurance) are a common analytical project for the risk team, sharing this knowledge with the business units, as is developing a common language and risk taxonomy. Proactively developing sources of liquidity, testing industry changes (e.g., old-age housing and financial solutions, policyholder behavior), and developing reinsurance strategies are other common themes.

Holistic ideas – exogenous

While holistically considering risks that are currently "owned" can lead to tricky relations with the business units, risk teams have been encouraged to do background research on emerging risks. Some of the topics worked on recently include genetic testing, artificial intelligence, interest rate risks (up or down), asset class risk, mortality/morbidity (including opioid issues), demographic shifts, climate change, public debt levels, international monetary policy, and capital market stability. Not all projects look at downside risk; one suggested that Long Term Care morbidity risk may have stabilized or even improve going forward.

Value investing/Bubbles

A subset of modeling holistic impacts is the risk team's search for assets/liabilities where the markets may have over-reacted, leading to mean reversion in the near future. Some of those identified could move up in price, while some could move down. While a few still advocated for efficient markets that make bubbles impossible, other respondents believe bubbles exist in private assets, collateralized loan obligations, energy subsidies, infrastructure subsidies (e.g., China's Belt and Road), auto finance, some Canadian housing markets, and general government financial subsidies.

Regulatory changes

The risk team is often tasked with managing and communicating potential regulatory changes as well as keeping track of regulatory metrics that change on a periodic basis. Expected changes often become part of a scenario set.

Orphaned risks/extra resources

Many risk managers manage specific risks due either to a temporary staffing vacancy or because the risk does not have a natural home. These could include business continuity, affiliation reputation risk, cyber security, severe weather, or other general risks. The risk team is also a candidate for special projects.

Conclusion

Risk teams are asked to do a variety of tasks. They are asked to produce company-wide scenario tests as well as look at the pros and cons of individual projects viewed using marginal impacts.

The risk team acts as the corporate owner of the risk process, so is accountable for sharing it with all areas. They also keep track of regulatory changes and help as needed.

These duties have been shown to work by fellow practitioners. By finding the ones that work best in your organization you can avoid finding out what your successor will do.

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