

**Deloitte.**

Implementing Risk  
Transformation  
in Financial Institutions:  
Strategy





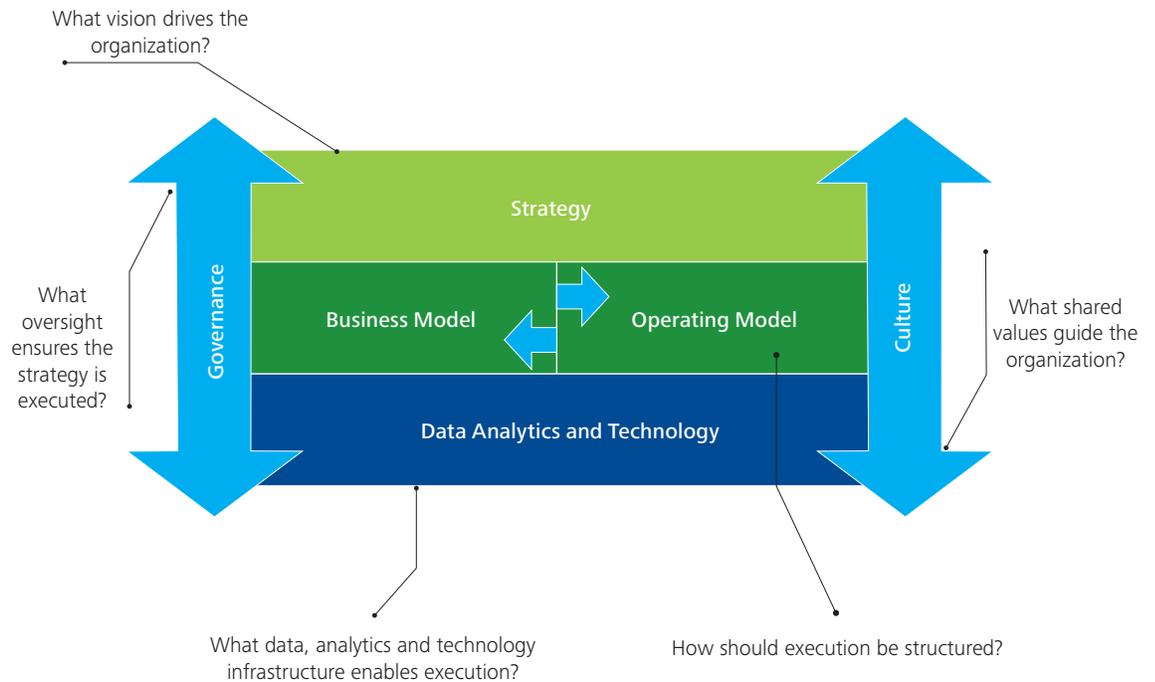
Risk transformation can enable a financial institution to elevate risk management from a functional capability to an enterprise responsibility that permeates the entire organization. When that happens, every business, function, and individual becomes responsible for, accountable for, and capable of recognizing and addressing the risks within their purview. Moreover, risk awareness and appropriate risk-related skills can become an integral component of every individual's responsibilities at every level. In these ways, risk transformation can enhance the organization's ability to implement business strategies and achieve goals while addressing risks and complying with evolving regulations.

This document is one in a series of four on the cornerstones of risk transformation (see Figure 1):

- Strategy
- Governance and culture
- Business and operating models
- Data, analytics, and technology

As explained in *Aligning risk and the pursuit of shareholder value: Risk transformation in financial institutions*,<sup>1</sup> when these cornerstone frameworks and capabilities are in place, risk management, risk governance, and regulatory compliance can be implemented in a more aligned and integrated manner.

**Figure 1: The cornerstones of risk transformation**



As Figure 1 shows, strategy is the overarching element—the vision that drives the organization. The organization's strategy (or strategies) are management's chosen means of pursuing the organization's goals. Governance and culture establish oversight and the environment in which strategies are implemented. Business and operating models, and data, analytics, and technology, enable the organization to conduct business, understand its risk positions, and manage risk.

Each document in this series focuses on a single cornerstone, in recognition that leaders can launch risk transformation initiatives across all four cornerstones or start with a single one. This document examines the importance and workings of strategy.

<sup>1</sup> *Aligning risk and the pursuit of shareholder value: Risk transformation in financial institutions*, 2013, Deloitte  
[http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/AERS/us\\_imo\\_grc\\_RiskTransformation\\_in\\_Financial\\_10152013.pdf](http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/AERS/us_imo_grc_RiskTransformation_in_Financial_10152013.pdf)

### Strategy as a transformational cornerstone

The Deloitte Touche Tohmatsu Limited network of member firms (Deloitte) defines strategy as an integrated set of choices that can position an organization to create superior financial returns and sustainable advantage relative to competitors. While various business units may require different strategies, management must reconcile and integrate those strategies and the board must approve and oversee them.

In response to regulatory pressure, financial institutions have been moving toward less capital-intensive businesses and increased capital efficiency. The need to make that migration would in itself present enough strategic challenges. However, coping with regulatory demands related to stress testing, scenario planning, capital adequacy, and data and reporting issues has rendered many chief risk officers (CROs)—as well as other senior executives, business-unit leaders, and board members—less than fully prepared to address strategic risks.

### Strategic risks: Not what you're thinking

A strategic risk is a potential event that can undermine implementation of a business strategy or achievement of strategic goals. Strategic risk events can invalidate the rationale of a strategic decision, threaten competitive position, and erode performance. But they can also point toward new opportunities.

Strategic risks may lack historical precedent or originate outside an industry (or both). Signals related to emerging strategic risks are often faint or intermittent, which can make them hard to detect, easy to dismiss, and difficult to interpret. Traditional tools cannot reliably locate and analyze them.

In addition, strategic risks may be:

- Unique to the institution, because the strategy, culture, governance structure, and business and operating models are unique to the institution
- Damaging to the entire institution, because a risk involving, say, reputation or access to capital in one part of the organization may affect other parts
- Easy to overlook, because they often seem irrelevant, unthreatening, or highly unlikely—and management may believe they are being monitored and managed when they are not
- Difficult to address with customary risk management methods

Strategic risks may arise from low-likelihood/high-impact “black swan” events. These events can escalate rapidly and render those who have not anticipated them confused, paralyzed, or prone to mistakes.

Although they may take the form of financial, operational, technological, political, or other familiar risks, strategic risks tend to be difficult to quantify and track. For example, the blockchain, an enabling technology initially designed to provide a secure record of Bitcoin transactions, was created anonymously and distributed freely, with no connection to visible institutions. Created for a single purpose, it could eventually prove to be disruptive in several major industries. Specifically, in financial services, blockchain architectures could provide the ability to facilitate global payments with greater speed and transparency and less cost than current methods.

Emerging technologies warrant continual monitoring as potential sources of strategic risks—should new or existing competitors harness them—and sources of opportunities. However, such technologies challenge conventional risk management methods when their source is unknown, distribution uncontrolled, and uses unanticipated.

Essentially, strategic risks can gum up, delink, or erode drivers of value. If ignored, they can become what Deloitte has separately described as “value killers” (see Figure 2 and sidebar: Beware of the value killers). On the flip side, strategic risks can present new drivers of value, suggest modifications to current drivers, or indicate the need to abandon existing drivers.

Figure 2: Value killer risks



### Beware the value killers

In 2014, Deloitte United States published *The value killers revisited: A risk management study*, which updated its 2005 study *Disarming the value killers*. The 2005 study defined “value killers” as risk events that destroy 20 percent or more of corporate value in one month relative to the growth or decline of the MSCI<sup>2</sup> All World Market Index in the same period.

The update identifies patterns in loss-creating risks of the Global 1000 in the decade before 31 December 2012. Value killer losses were experienced by 38 percent of the Global 1000, with a small subset of those companies seeing losses exceeding 50 percent of their corporate value.

### The 2014 study identified five key types of value killers:

- **High impact, low frequency risks:** These “black swan” events often catch companies by surprise, leading to rapid losses.
- **Correlated or interdependent risks:** Almost 90 percent of the companies suffering the greatest losses were exposed to more than one type of risk, which usually exposed a weakness that cascaded through the organization.
- **Liquidity risks:** Financial crises expose the dangers of liquidity risks, which have drawn intense regulatory attention and increased the cost of capital to institutions with high leverage and low ratings.
- **Merger and acquisition risks:** Business combinations may not only fail to deliver anticipated value, but can also, despite traditional due diligence, expose organizations to unexpected risks.
- **Culture and compensation risks:** Incentive programs that reward short-term performance may create unsustainable business models while inconsistent leadership or tone at the top can increase conduct risk.

Regardless of their classifications, value killer risks must be understood and addressed by the board and senior executives, who must also establish mechanisms for detecting and monitoring them.

### A necessary shift in perspective

Financial institutions manage risk as their core business. That, however, is partly why recognizing strategic risks may be challenging. Strategic risks can result from and amplify risks that the institution manages in the normal course of doing business, as well as other risks.

A shift in perspective is necessitated by post-crisis economic and regulatory conditions, and other developments (see sidebar: A (strategically) risky world). Indeed, ongoing developments create the need to monitor strategic risks continually, while maintaining a level of strategic flexibility unimaginable in pre-crisis times.

Generally, the following shifts in perspective would be useful:

- From a focus only on understanding traditional financial risks to a broader view of risk and the interrelatedness of risks
- From a mindset of pricing and managing known, fairly predictable risks to one of positioning the organization to detect and respond to unknown—and even unknowable—risks
- From a sense of mastery over risk to curiosity about risk
- From a focus on traditional risk reports to a focus on scanning for emerging strategic risks
- From an inside-out view of risk to a more outside-in view

Consider these questions:

- How might a new, technology-enabled business model disrupt a source of capital, revenue, or returns?
  - Imagine the potential impact of alternative payment systems and peer-to-peer (P2P) lending, continued stagnation in certain national economies, and investors’ periodic migration into index funds.
- Which internal and external cyber threats could put data at risk?
  - A new breed of hackers-for-hire can place customer data, account access information, and directors’ and senior executives’ personal information at risk.
- Where might risks to reputation arise, and how is the organization positioning itself to address and recover from them?
  - Risks to reputation can arise from customers or investors, interest groups, news sources, online ratings, blogs and social media, employee conduct, and legal violations, including those arising from ignorance of the law.

<sup>2</sup> Morgan Stanley Capital International

- How might future regulatory and political developments impede innovation or undermine business strategies?
  - While regulatory actions ideally should not dictate strategy, they strongly influence it—as regulators intend. Yet as events unfold, things will change; therefore, strategies should be flexible as well as sustainable.

From the risk management standpoint, strategic risks pose challenges because of their complexities and potentially high stakes. Therefore, new methods of addressing them are needed, now and going forward.

### Addressing strategic risks

To detect and address strategic risks, companies may wish to consider whether they could benefit by investing in one or more of the following areas:

- **Identifying potential “black swans”:** Building on their own and other institutions’ experiences, leaders can brainstorm potential low-likelihood/high-impact events and identify ways in which the institution could recognize and assess them.
- **Sensing capabilities:** Technology can now enable institutions to monitor numerous variables in real time—from a huge range of credit indicators to the likelihood of storms and droughts—that may be precursors to a risk event (see sidebar: Risk sensing—monitoring emerging risks).
- **Modeling and stress testing:** Given the role of interrelated risks in strategic risk, stress testing scenarios with multiple risks can provide a clearer picture of the likely impact of risk events.
- **Response capabilities:** Not all risks can be anticipated; however, simulating responses to risk events and developing response plans can help improve the institution’s response capabilities.

Transforming strategic risk management goes even further. It includes broad and deep risk analysis, scenario planning, and both mandated stress testing and stress testing for planning and capital allocation purposes. It examines risks generated by a strategy as well as risks to the strategy. It considers potential strategic risks in decisions related to market entry or expansion, product initiatives, M&A activities, compensation plans, new hires, and talent management. At the same time, it fosters awareness of strategic risks across the institution.

In addition, big data scanning tools and sophisticated analytics can help institutions gather and analyze the vast amounts of information now available in cyberspace. Activities include monitoring news feeds and blogs for developments among competitors and following—and even influencing—evolving consumer tastes and business needs. But these activities must be sustained, and conducted within a framework that identifies what to seek, where to look, and how to monitor developments.

### A (strategically) risky world

Conditions are such that senior executives must consider a broad range of potential threats to the institution’s business strategies.

- In its paper, *Financial system impact of disruptive innovation*,<sup>3</sup> the New Economics Foundation (NEF) identified several potential disrupters. Notable among them were disintermediation of capital markets and payment systems, new forms of credit creation, and innovations in economic and financial policy.
- Specifically, P2P lending could change the world of consumer lending, as reported by *The Financial Times*. In a sign that P2P lending may be truly entering the mainstream, these loans are now being securitized and resold.<sup>4</sup>
- That same report noted that insurers, pension funds, asset managers, hedge funds, broker dealers, exchange traded funds, and money market funds all engage in activities once performed by banks.<sup>5</sup>
- In addition, structural changes in commercial lending could pose strategic risks for traditional lenders. In particular, the move by small and medium-sized enterprises from bank-originated lending toward the bond markets may herald still more disintermediation.<sup>6</sup>
- The dangers of using the past to forecast the future continue to be documented. A Thomson Reuters article points out that the old model of using historical data to predict the future has proven time and again to be unreliable. They also state that even with better technology, more judgment is required.<sup>7</sup>

Risks posed by these developments extend beyond the “normal” risks financial institutions face in the course of business.

<sup>3</sup> *Financial system impact of disruptive innovation: A working paper for the United Nations Environment Programme (UNEP) inquiry*, 2014, UNEP <[http://www.unep.org/inquiry/Portals/50215/Documents/Disruptive%20Innovation\\_Inquiry%20Working%20Paper\\_%20NEF.PDF](http://www.unep.org/inquiry/Portals/50215/Documents/Disruptive%20Innovation_Inquiry%20Working%20Paper_%20NEF.PDF)>

<sup>4</sup> “Alternative finance steps out of the shadows” by Patrick Jenkins and Sam Fleming, 10 December 2014, *The FT’s Year in Finance*, *The Financial Times* <<http://im.ft-static.com/content/images/ff107cee-7f74-11e4-b4f5-00144feabdc0.pdf>>

<sup>5</sup> Ibid.

<sup>6</sup> “SMEs Embrace The Bond Markets” by Peter Dollé, 27 February, 2013, *Forbes* <<http://www.forbes.com/sites/insead/2013/02/27/smes-embrace-the-bond-markets/>>

<sup>7</sup> “What’s next in disruptive technology and innovation in financial services—Download from Davos” by David Craig, 24 January 2014, *The Knowledge Effect*, Thomson Reuters <<http://blog.thomsonreuters.com/index.php/whats-next-disruptive-technology-innovation-financial-services-download-davos/>>

### Risk sensing—monitoring emerging risks

The entire world of digitization—of experiences, transactions, and currency—provides new drivers of value to businesses while presenting new risks. Both risk and value creation now often originate in cyberspace or quickly find their way there. Certain technologies, deployed to scan the Internet’s structured and unstructured data can sense nascent risk events, monitor changes, trends, and patterns, and distill them into actionable information.

These risk sensing capabilities can enable an institution to:

- Combine data mining, scanning, and analytical technologies with machine learning, modeling, and human judgment to develop insights on emerging strategic risks and their implications
- Scan cyberspace for factors considered critical to the success of a strategy (e.g., consumer spending, business investment, governmental fiscal or monetary policies) as well as for events that may affect value (e.g., regulatory actions, changes in credit quality, or interest rate movements)
- Define thresholds and indicators, and combine them with human judgment in iterative methodologies to deliver increasingly useful insights
- Establish a system that continually improves its ability to detect nascent reputational, technology, market, economic, and security risks
- Revisit organizational strategies and underlying assumptions to ensure alignment of strategies, assumptions, and thresholds, escalation procedures, and response plans

A formal, properly resourced approach to identifying emerging risks—and opportunities—will provide far better capabilities than periodic or part-time efforts. Data on risk is quite diffuse and people focus mainly on their operational responsibilities; therefore, a dedicated resource may well provide superior monitoring and analysis of emerging risks.

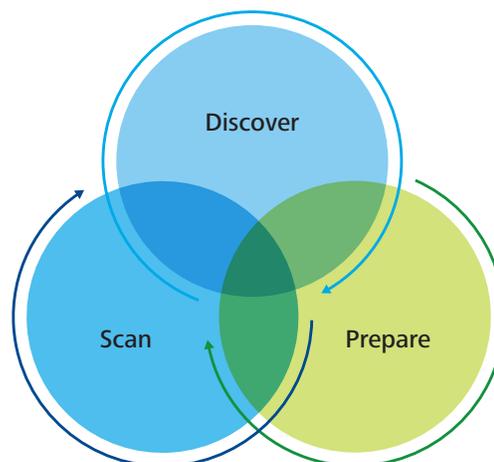
### Scan, discover, and prepare

Many organizations believe they are already managing strategic risks when they are not, particularly when it comes to emerging strategic risks—early-stage, off-the-radar developments that rapidly escalate or morph into value killer risks.

To address this, Deloitte has developed the following iterative, three-step approach to scanning, discovering, and preparing for strategic risks (see Figure 3):

- **Scan:** Monitor the environment and interpret the signals
  - Apply risk sensing technologies and tools to big data and media feeds
  - Analyze signals being tracked
  - Summarize results in dashboard or executive summary formats
  - Add insight through human analysis
- **Discover:** Employ analytics and human capabilities to gauge potential outcomes
  - Use scenario planning to identify potential risk events
  - Conduct simulations to gauge potential outcomes and impacts
- **Prepare:** Identify responses that will mitigate impacts
  - Reassess your assumptions and identify new strategic options
  - Develop contingency and recovery plans
  - Mitigate and manage risks (via insurance, hedging, diversification, exit, etc.)

Figure 3: An integrated, iterative approach to strategic risk



Deloitte has found this approach, described here at a high level, to be structured, practical, and relevant enough to be sustainable. It incorporates risk sensing at the scanning stage as well as human review, and continually uses the findings of the process to improve the process.

This is not to say that every strategic risk can be detected at embryonic stages. It is to say that large financial institutions should consider a repeatable, integrated approach to risk sensing to help prepare for major risk events as well as for subtle yet potentially profound changes that could undermine strategy or achievement of goals.

### Goals of strategic risk transformation

In an institution that has transformed its approach to strategic risk, the following five conditions prevail:

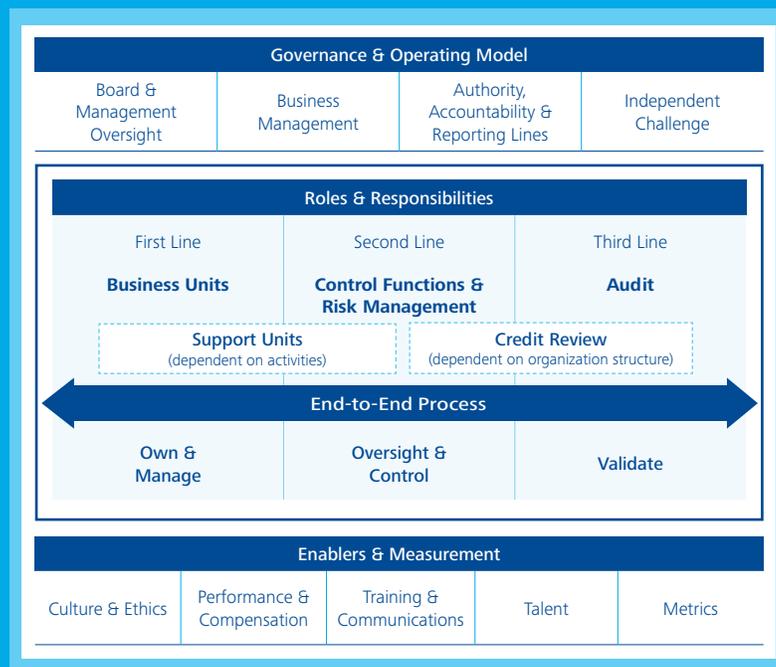
- Senior leaders manage strategic risks proactively:** Senior executives, in concert with the CRO and business-unit leaders, work proactively to identify, detect, monitor, and address strategic risks. Contingency and response plans are in place, with specifics such as backup sources of capital identified. Insurance, diversification, hedging, and other tools are used to mitigate strategic risks. The board and management appropriately disclose strategic risks and measures taken to address them.
- Transactional and portfolio risks are well understood:** Strategic decisions determine the kinds of transactions the organization will engage in and the portfolios it will construct. While institutions have tools for analyzing quantifiable risks in these areas, management realizes that less quantifiable risks are generally less well understood. Therefore, management looks beyond transactions and positions to assess all strategic risks.
- Risk infrastructure is aligned with business strategy:** The risk governance and management infrastructure is capable of recognizing and addressing strategic risks. This infrastructure includes the risk-related roles and responsibilities of individuals, as well as policies, procedures, and mechanisms for managing risk. As noted in the governance and culture paper in this series, the risk culture and business strategy must be aligned in order for a strategy to succeed. This alignment also enhances the three lines of defense of risk governance (see sidebar).
- Capital allocation is in line with risk appetite:** While moving to increase capital efficiency and meet regulatory expectations, management understands the risks of new business models and changes to the risk profile. They therefore adjust the risk appetite—or the strategy—to allocate capital to the most profitable uses.

- Regulatory environment is factored into strategy:** Regulatory issues are considered in the business strategy, as are issues of talent, organizational culture, and risk governance resources. In addition, strategic flexibility (discussed below) enables the organization to adapt its strategy as regulations evolve.

### Implications for the three lines of defense

Risk transformation strengthens the three lines of defense model—the business units, risk management function, and audit function—a generally accepted industry framework (see Figure 4). Transforming strategic risk strengthens the three lines of defense by linking the daily activities of each line to the risks that could undermine implementation of the strategy and achievement of strategic goals.

Figure 4: A depiction of the three lines of defense model of risk governance



Source: Deloitte United States point of view *What's next for Three Lines of Defense?*

A clearly understood strategy provides a strong sense of direction and common purpose for all three lines of defense. At the same time, each line plays a management-mandated role vis-à-vis the strategy. Those working in each line must understand and interpret that mandate and its implications for each line, and conduct themselves accordingly.

- Business units:** Due to their front-line positions, business units implement strategies. Thus an awareness of strategic risks—and underlying assumptions—helps them to understand the challenges they face and potential impacts of risk events. That awareness can enable them to view customer behavior, new technologies, and other developments through a strategic lens. While they should remain focused on their goals and on risks they can directly address, they should also recognize emerging

strategic risks and know when to communicate them to relevant parties.

- **Risk management:** Risk managers should provide the institution and its leaders with an awareness of strategic risks, and with the capabilities needed to identify, detect, track, and manage them. It is the CRO's role to point out the risks to (and of) a strategy, challenge assumptions, and point out unacknowledged assumptions. The CRO should also oversee efforts of the business units and management to detect and monitor strategic risk.
- **Internal audit:** The internal audit function should be aware of strategic risks and periodically assess the adequacy of risk management, control, and compliance systems in light of value killer risks. Internal audit should not act as a management quality assurance or quality control function or "police" the other two lines of defense; but should serve as periodic overseer, advisor, and backstop in the context of providing assurance.

Proper attention to the other three cornerstones is critical to aligning the lines of defense. Strong governance and culture enable the business units and risk management to balance risks taken in creating value against anticipated rewards. Practical, integrated business and operating models define the role of each line in implementing the strategy. High quality data, analytics, and technology provide much of the risk-related information each line needs to do its job.

### A practical, transformative approach

An organization needs a transformative approach to address strategic risks in the manner discussed up to this point. Risk transformation represents an integrated, sustainable, strategic response—rather than a piecemeal, ad hoc, tactical response—to evolution in the regulatory and competitive landscape. This goes beyond identifying "black swans," employing risk sensing capabilities, and improving risk escalation procedures, although those are important.

Risk transformation focuses on all the practicalities that senior executives and board members must attend to in order to identify and address strategic risks. This begins with leaders recognizing that strategic risks may differ, in kind as well as in degree, from other risks. Leaders must acknowledge that every strategy is predicated upon certain assumptions and poses certain risks, and then analyze those assumptions and risks. Moreover, that analysis should be integrated into the strategic planning process.

These actions position management to reconcile and integrate strategies across the various lines of business and into risk management and governance activities.

In addition, management should:

- **Monitor strategic risks at all levels:** Risk sensing capabilities are needed on the front lines of most business units and functions. These capabilities—enabled by technology such as real-time risk monitoring via dashboards, and human analysis—make risks more visible and manageable. While real-time monitoring of strategic risks is now practical, their potential impact must be gauged and responses calibrated such that management neither ignores important risks nor overreacts to unimportant ones.
- **Protect drivers of value:** Given that strategic risks can undermine drivers of value, management should use specific methods appropriate for their organization to identify threats to those drivers. These methods can include obtaining an outside-in view, and practices such as red-team/blue-team exercises and the champion-challenger approach. In the latter, a new or proposed policy or procedure related to lending, investment, or other activities (the "challenger") is evaluated against an existing one to project the new one's

### Case study #1: Reviewing a commercial bank's credit risk architecture

During a period of significant integration, a commercial bank needed to design integration and risk transformation activities for credit risk. Objectives included supporting Basel II program leadership, and providing program management, as well as design support and work-stream management.

Assisting in this initiative entailed:

- Analyzing the proposed risk architecture and identifying key challenges
- Defining the initial business case to support the overall program, as well as subsequent project business cases
- Developing a program roadmap to support risk integration and transformation activities
- Providing subject matter knowledge to support the client's model interpretation, regulation, and risk architecture

Key results of this effort included:

- Development and implementation of internal ratings-based (IRB) models
- Implementation of amendments to the IRB calculation framework, resulting in a significant reduction in the Pillar I capital requirement
- Delivery of a program roadmap to support risk integration and transformation activities across various strategic risk work streams

impact. In general, key drivers of value must not only be recognized, but understood, periodically evaluated, protected, and, when necessary, modified or even abandoned.

- **Develop strategic flexibility:** In a rapidly changing environment, the ability to modify a strategy or adopt an alternative one when needed can earn high rewards. Yet this can rarely be done on the fly. Strategic flexibility<sup>8</sup> depends upon senior management building future scenarios, creating optimal strategies for each of those possible futures, determining which strategies are required, and then managing the portfolio of options. This calls for senior leaders to focus on the intermediate-to long-term future, rather than only on daily operations and near-term issues.
- **Extend risk management:** Risk transformation extends risk management down to the levels where risk can be identified, tracked, and managed in the businesses and functions. This does away with the notion that risk management is the responsibility of the function with that name. It makes risk management the responsibility of everyone, as appropriate to their positions. That is the goal of risk transformation, and it is easy to overlook its importance where strategic risks are concerned, because they can be perceived only as leaders' bailiwick.
- **Go beyond covering regulatory bases:** Regulators are driving much of the rationale for change. This can prompt leaders to see regulatory compliance and the need to meet capital, stress-testing, and data-related requirements as the chief priority. Risk transformation takes the pervasive nature of these requirements as a rationale for substantive, organization-wide change because ad hoc, piecemeal, tactical responses have proven inadequate and wasteful. Again, this calls for a change in mindset for most executives and directors.

Fortunately, when you prepare to address certain strategic risks, whether they affect liquidity, capital, talent, market access, or reputation, you actually prepare for a range of risk events. Similarly, once an institution establishes plans to address disruptions in communication, technology, cybersecurity, and funding, those plans can be applied in a range of circumstances.

#### **Case study #2: Assessing a bank's loan portfolio and pricing strategies**

The bank wanted a strategic assessment of pricing across its businesses to achieve adherence with leading practices in pricing capabilities and execution.

This involved:

- Conducting a series of interviews to identify the different views of specific business stakeholders and executives
- Documenting pricing practices across all relevant stages of the credit lifecycle
- Deploying a pricing assessment framework to assess existing policies, practices, and procedures in light of global leading practices in pricing
- Identifying significant pain points in pricing analytics, governance, strategy, and execution
- Prioritizing gaps between current and desired practices

Key results included:

- Definition of an end-to-end pricing strategy that served as a platform for subsequent pricing enhancement initiatives
- Identification of sector issues and their impacts while distinguishing between strategic and tactical responses required to sustain long-term growth
- Development of a means of comparing profitability and return benchmarks for other portfolios

<sup>8</sup> For more on strategic flexibility see *The Strategy Paradox* by Michael E. Raynor, 2007, Crown Business, NY

### The business case

Making the business case for transforming the strategy cornerstone means distinguishing strategic risks from other risks. This can be challenging. Also, many management teams assume the institution “has these covered” or is “already monitoring them” when that’s not the case.

To be sure, senior executives realize that strategic risks can originate with regulators, competitors, clients, investors, cybercriminals, the media, or other areas, such as technologies or social trends seemingly unconnected to the industry. However, leaders may fail to appreciate that these risks differ from “normal” risks. Also, in contrast to the business case for transforming the other cornerstones, the case for transforming strategy must often be made on more qualitative information.

The characteristics of strategic risks create this situation. Still, management can gauge the potential financial impacts of possible events, understand when assumptions could be invalidated, and prepare responses. Indeed, these are responsibilities of the board and management with regard to strategic risks.

In sum, transforming the strategy cornerstone enables leaders to better understand risks, build strategic flexibility, allocate capital more efficiently, and adjust strategies in response to changing conditions.

### Conclusion

Strategic risks often pose greater threats than those posed by other types of risks. Yet financial institutions and CROs remain focused primarily on financial and operating risks and on regulatory compliance risks—for understandable reasons. Managing those risks is their business and regulatory demands have reached new heights.

However, strategic risk can destroy huge amounts of value, very quickly. They can jeopardize lines of business or the entire institution. Therefore, strategic risks demand attention and resources and a transformative approach.

Transforming strategic risks enables executives and boards to understand and address a broad range of risks and interactions among risks. It enhances business and operating models, as well as risk governance and risk culture. This transformation encourages management to adjust strategies or their implementation in response to changing conditions, while prompting the board and the CRO to challenge the assumptions underlying strategic decisions.

Finally, only senior management and the board can lead the transformation of the institution’s approach to them. Given the current regulatory and competitive environment, now is the time to begin this transformation.

## Key contacts

### Scott Baret

Partner  
Deloitte United States  
Deloitte & Touche LLP  
+1 212 436 5456  
sbaret@deloitte.com

### Bruce Laing

Partner  
Deloitte United Kingdom  
+44 (0)207 007 8150  
blaing@deloitte.co.uk

### Paul Skippen

Partner  
Deloitte Canada  
+1 416 874 4411  
pskippen@deloitte.ca

### Andrew Blau

Partner  
Deloitte United States  
Deloitte & Touche LLP  
+1 415 932 5416  
ablau@deloitte.com

### Peter Matruglio

Partner  
Deloitte Australia  
+61 2 9322 5756  
pmatruglio@deloitte.com.au

### Michael Kearney

Partner  
Deloitte United States  
Deloitte & Touche LLP  
+1 415 783 4461  
mkearney@deloitte.com

### Henry Ristuccia

Partner  
Deloitte United States  
Deloitte & Touche LLP  
+1 212 436 4244  
hristuccia@deloitte.com

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