Risk & Compliance

# CFO AND CRO FUNCTIONS TO CONVERGE AS MARKET VOLATILITY ENCREASES PRESSURE ON BANKS

A Central CFOs and CROs in the financial sector are facing a period of simultaneous and disruptive events consequent to the recent financial crisis. Markets and economic volatility together with regulatory and commercial pressures are producing a challenging environment never seen in the past.

Finance and risk functions within many financial firms have begun to build a closer partnership and a greater coordination, impelled by a combination of factors including cost and effectiveness pressures, regulatory demands, a desire to do more stress testing, reports on credit and market exposures with the goal to provide faster and more accurate figures to support the top management strategic and operational decision processes.

In this way finance and risk are different faces of the same coin and, though the two functions must remain separated, a closer collaboration is required to give different perspectives and vigorous debate to providing the CEO and Board with a balanced view.

Following areas should be the first testing ground to promote joint activities between finance and risk, while assuring their independence:

- **Data quality** - finance is, and should remain the ultimate custodian of data, however data quality should be a shared responsibility.

- **Joint development of risk and capital models** - risk models are developed by the risk function, but it must be done in close coordination with finance.

- **A greater use of risk analytics** - more and more organizations are using sophisticated risk analytics, not only to support credit and financial decision making, but to provide a stronger foundation for operational strategy. The risk function often provides analytics services to all functions, including finance, which can further foster integration (e.g.. stress testing).

- **Regulatory reporting** - new regulatory approaches now make compliance the common responsibility of the CFO and CRO (e.g.. Capital adequacy). Risk-adjusted capital models are at the heart of both the latest Basel regulatory initiatives in banking, and the latest Solvency initiatives in insurance. Implementing such models often involves extensive coordination by risk and finance on inputs, and possibly also on decision-making.

- **M&A** - it has been almost the sole domain of finance, but risk increasingly has a chair at the table, particularly during due diligence phases of an acquisition.

Some key issues should be addressed in order to reach an effective risk-finance collaboration:

- **Establish integrated and shared data sources** - solving data quality issues, including the development of shared data processes and systems, can be an effective way to reduce a common area of conflict and improve the risk-finance working relationship.

- **Jointly develop risk and capital models** - risk models development typically remains the responsibility of the risk function but data fed into models should come out of systems created by finance, and outputs from the models can in turn influence financial reporting (e.g. provisioning, ICAAP).

- **Strike the right balance to promote interdependence and cross-leverage risk management and finance** - independent CFO and CRO functions can actually provide a strong impetus for operational integration.

- **Give risk input into strategy** - even when working in close cooperation with other departments, allowing risk to retain its independent perspective can be essential.

- **Increase the value-added provided by the risk function** - risk should go beyond a compliance role to focus on adding value to the business.

- **Rotate personnel between risk and finance** - even if risk and finance personnel sometimes find themselves in opposition on an issue, speaking a common language and having common experiences can help enhance operational effectiveness.

Be has already started to support its Clients to be successful in this emerging trend. Quantitative skills in designing measures and reporting on the banking and trading book, culture in data quality and knowledge of processes developed in the CFO area and data governance projects can be easily extended with few risk management skills to support an effective CFO CRO Convergence.