


Risk Management in the Financial
Services Sector Conference

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Carob Mill, Limassol

Risk Management Framework

A CEO perspective

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of Management & Finance


MAP S.Platis

Target Risk Framework

Effective risk management is part of a wider governance structure and covers several elements



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Target risk management framework

Strategy and policy deals with:

- Overall objectives, strategy and risk appetite.
 - High level description of approach and minimum standards for key risk processes.
 - Relationship with other related risk management and control policies and processes.
- **Organisation & governance structure** deals with:
- Senior management oversight.
 - Central risk function which provides independent risk measurement, monitoring and reporting to the Audit and Risk Committee and the Board.
 - Clearly documented risk accountabilities and responsibilities tied to job descriptions.

Risk processes deals with detailed standards and guidelines for:

- Risk and control assessment process, including limits.
- Risk monitoring / key risk indicators.
- Incident and loss tracking / reporting.
- Entity and consolidated risk reporting.

Risk infrastructure deals with:

- **Technology to support / enable risk data capture and reporting.**
- **Models to measure / quantify risk.**
- **Risk management dashboards / reports.**
- **Supporting methodologies and tools.**

Risk Framework

Risk Appetite - Business growth targets and risk appetite must be aligned

Regulatory & Economic Capital must relate

Available Capital / Own Funds

Crawl, Walk, Run & Fly

CRAWL WALK RUN FLY

Runaway Ends, No Return Point

The Must "Takeoff or Crash" Decision by Pilot

Enough Thrust

Company Goals

Confusion & Fear of Taking Other Bad Decisions

ALIGNED?

Something has to give!

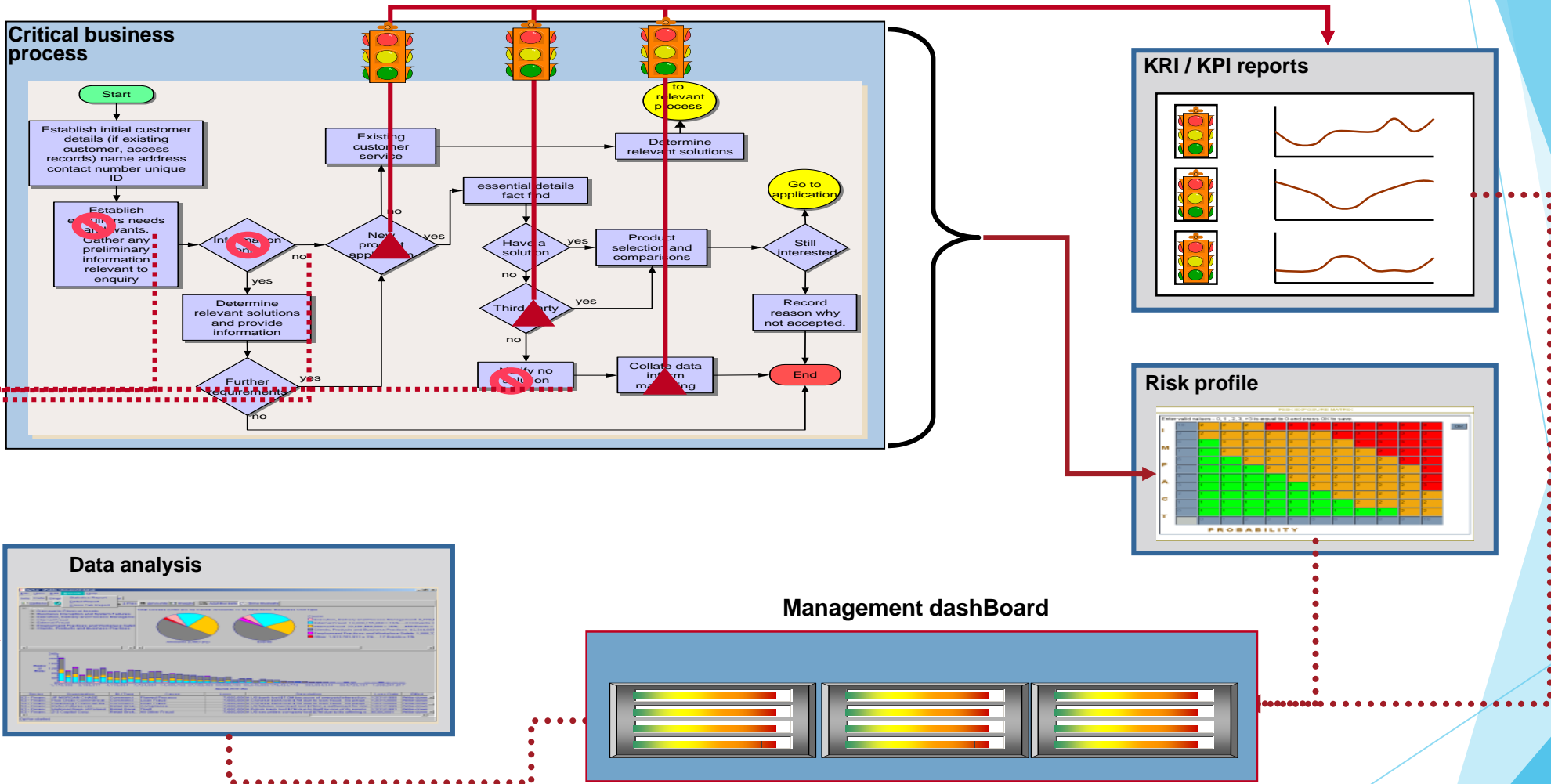
Think performance of Porsche 911 Turbo before and after "restricting" air allowed to pass in fuel burning process.

Why not buy a Golf 1.4L?

CONFLICT?

Risk Framework

Risk management: Measuring - Monitoring - Reporting



Risk Framework

Risk management: Measuring - Monitoring - Reporting

Measuring / Quantifying Risk	Description
Value-at-Risk (“VaR”)	Method: Historical Simulation, Variance/Covariance; Confidence level: 95%, 99% (assuming normal or t-distribution) Time: daily, weekly, monthly
Sensitivity Analysis	Parallel / non-parallel move, pip value, correlation etc
Scenario Analysis	On portfolio & risk factors & historical actual events
Stress Tests	Black swan events - extreme market movements
Measurable indicators	Intra-day vs non-intraday, frequency of trading, concentration, liquidity impact etc
Profit attribution	Mapping P/L to risk factors
Simulated P/L	Using different scenarios of volatility & correlation
The “Greeks”	Options portfolio: Delta, Gamma, Vega, Theta

One size does not fit all

Identify risk factors (that drive P&L)

Economic & Regulatory Capital

Available Capital

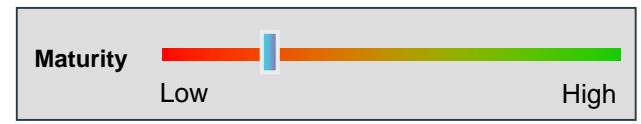
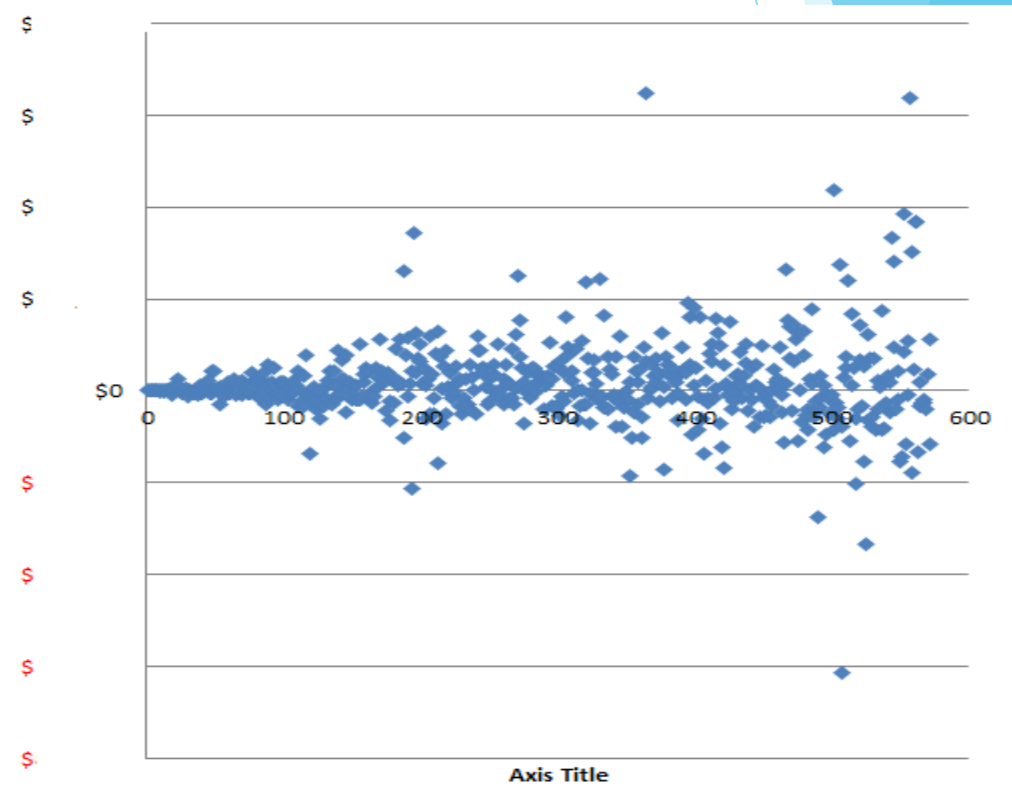
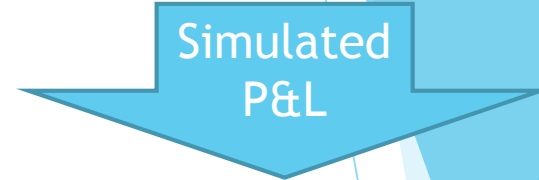
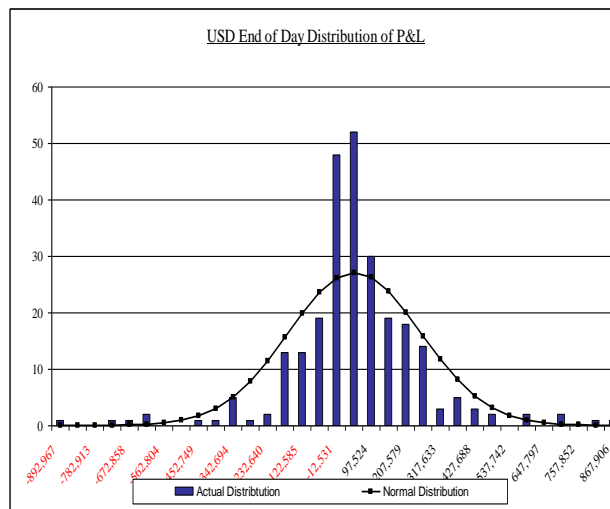
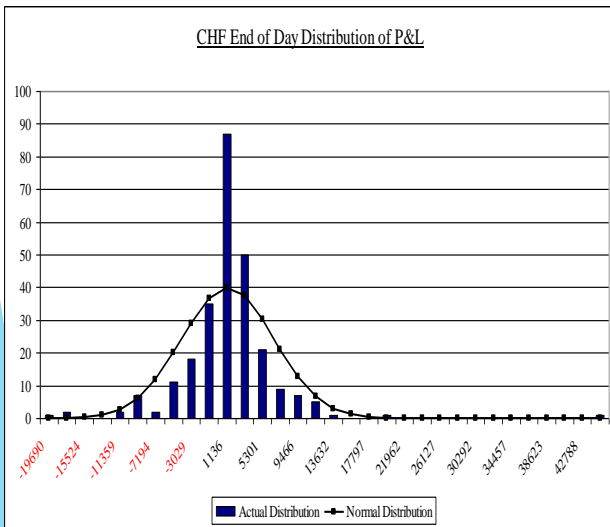
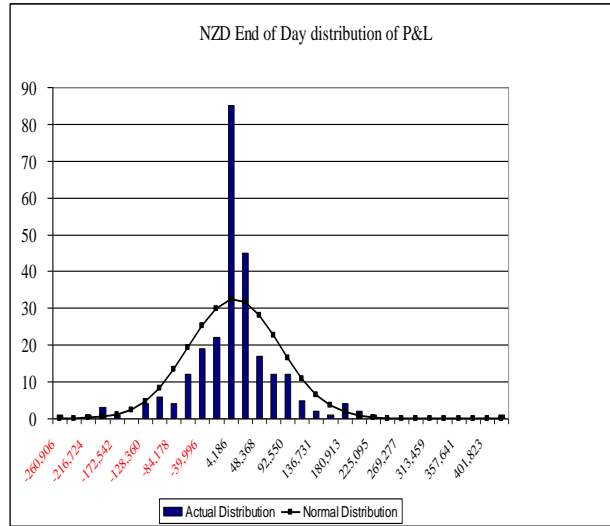
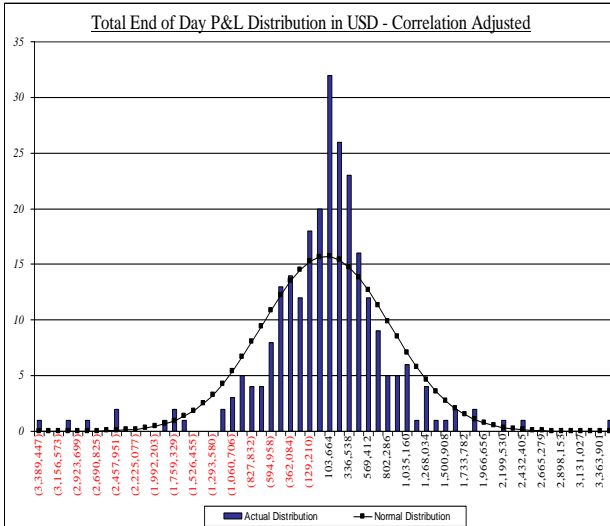
Higher risk → higher the return (?)

Portfolio, asset class, concentration etc - hard and/or soft limits

Risk & Return

LIMITS (portfolio, asset class, concentration etc)

Risk Framework



Risk Framework

No risk management

- ▶ Operate without risk framework
- ▶ Rely on individuals' experience
- ▶ Take decisions on ad-hoc basis
- ▶ No mechanism to analyze/review risk management results
- ▶ Rely on luck not to face unusual market conditions
- ▶ Replicate same operations without considering different type of clients
- ▶ Absence of risk framework could lead to huge losses
- ▶ As soon as facing unusual market conditions, it might be too late to do risk management

Target Risk Environment

- ▶ Work using a dynamic risk framework
- ▶ Focus on protecting company's fund and managing it's exposure
- ▶ The company makes money from its business model not from its risk management
- ▶ Losing money on hedging is not a lost opportunity to make money
- ▶ Follow risk limits and use a risk group for unusual conditions
- ▶ Risk Management mitigates risks but does not eliminate it
- ▶ The Inherent risk in our business model that could lead to potential losses should be contained by the risk management framework

Risk Framework

- ▶ Can all risk be mitigated?

Recent CHF experience - doable but you had to price yourself out of the market.

Agency vs market maker business model.

- ▶ What should a realistic risk framework in our industry target to achieve?

The same as any other trading business and/or investment banking business.

Investment banking natural hedging across different business → P/L

Could be that more risk higher return but: Black Swan Event


- ▶ Risk management - ending point

Is it a shield or a sword ?



Thank you

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