



November 17, 2020



Logistics

- Today's session will NOT be recorded. Please speak freely.
- We will be sharing the presentations following the event
- Please post questions during the session in the Chat (send to 'EVERYONE')
- Add your organization to your name – for example 'Daniel Waldron (CGAP)':
 - Click 'Participants',
 - Right click your name
 - Click 'Rename'



Agenda (all times GMT)

11:00	Introductions
11:15	Risk Management Framework
11:30	Risk Culture
12:00	Risk Appetite and Risk Tolerance
12:30	Break
12:45	Governance
13:30	Risk Management Methodology
13:40	Investing and Risk

Poll Question #1:

How excited are you to be discussing risk management today?

1. *Cautiously excited*
2. *Prudently excited*
3. *Excessively excited!*
4. *Dangerously excited!!*

Facilitator



Walter Tukahirwa, CFA

Risk Management
Specialist



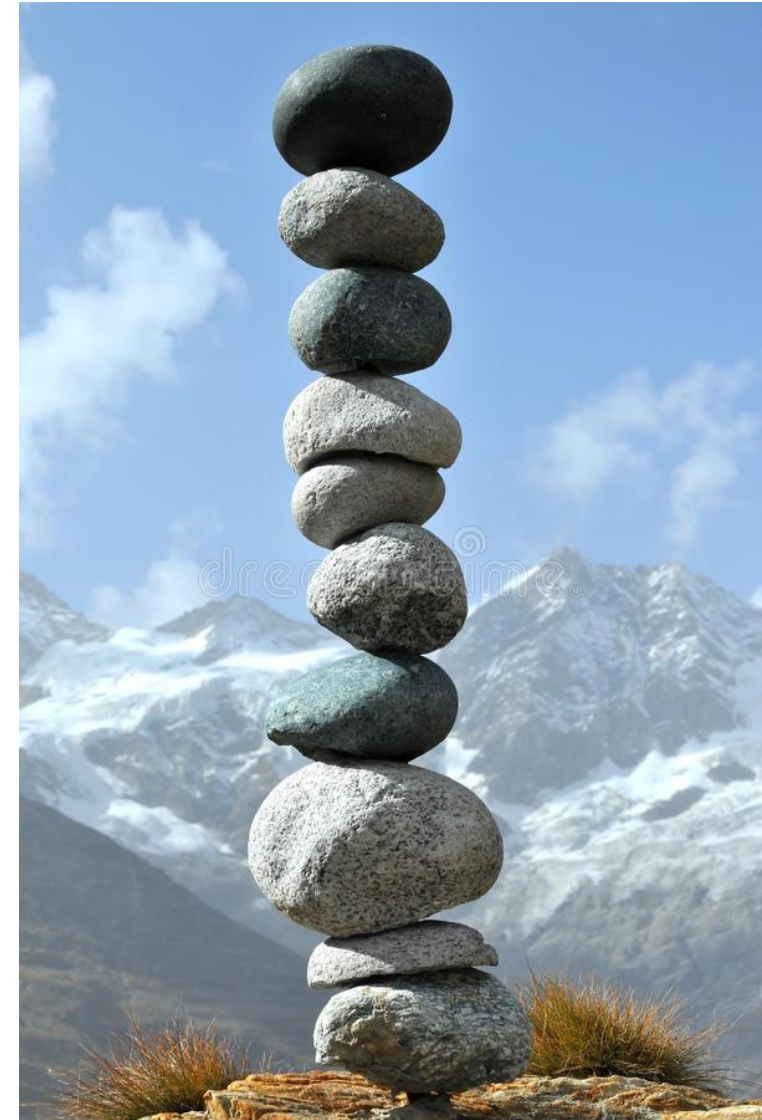
Drew Corbyn

Head of Performance &
Investment, G^OGLA



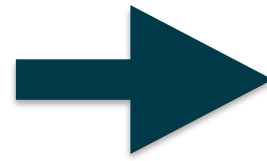
Why are we here?

- 1. Wanted to end energy poverty using distributed energy**
- 2. Distributed energy assets and appliances require consumer financing**
- 3. No one else was willing to finance assets for energy poor customers**



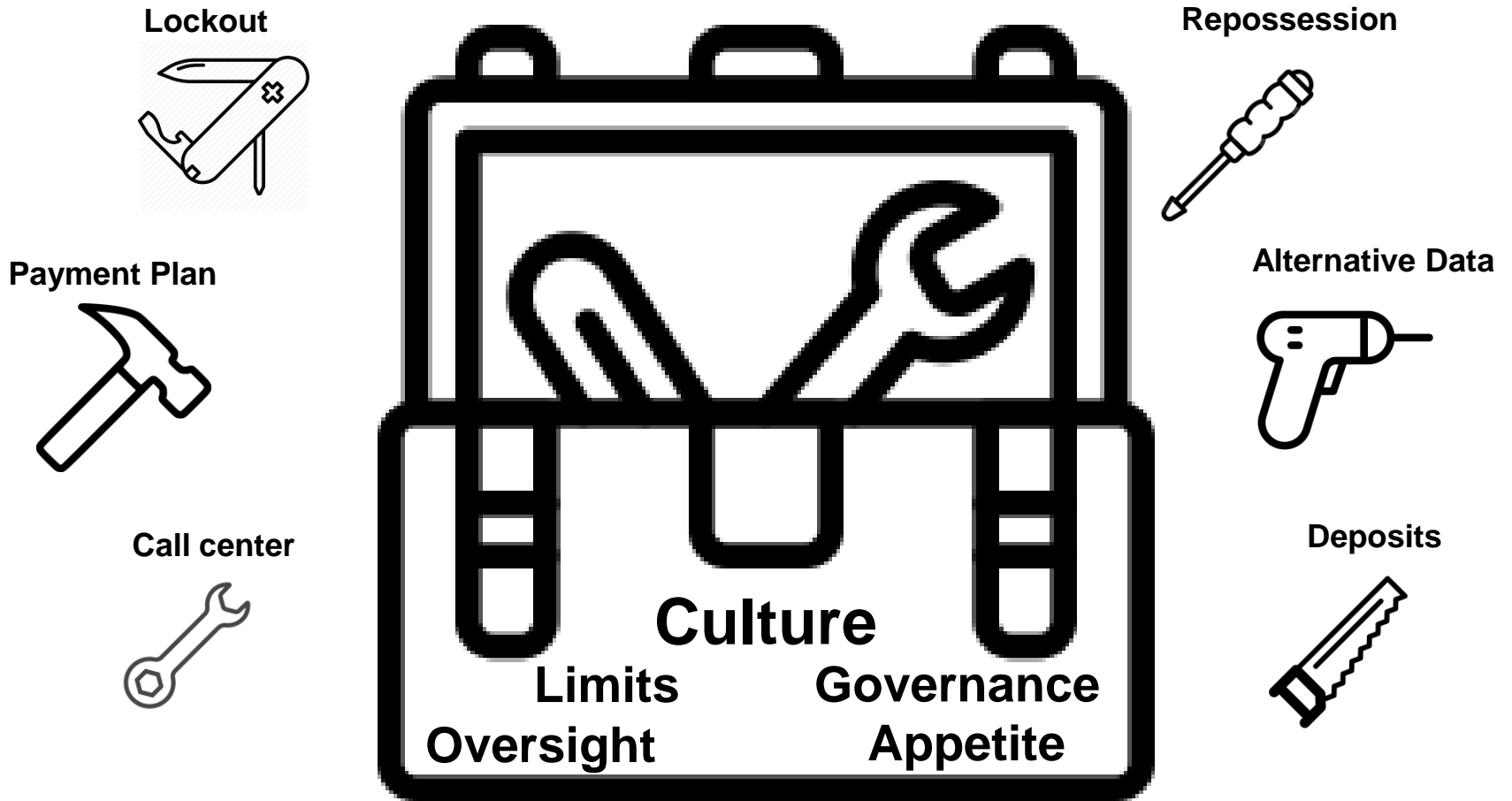
Let's get past semantics

Loan
Lease
Hire Purchase
Payment
Plan



RISK

PAYGo risk management: The tools and the toolbox



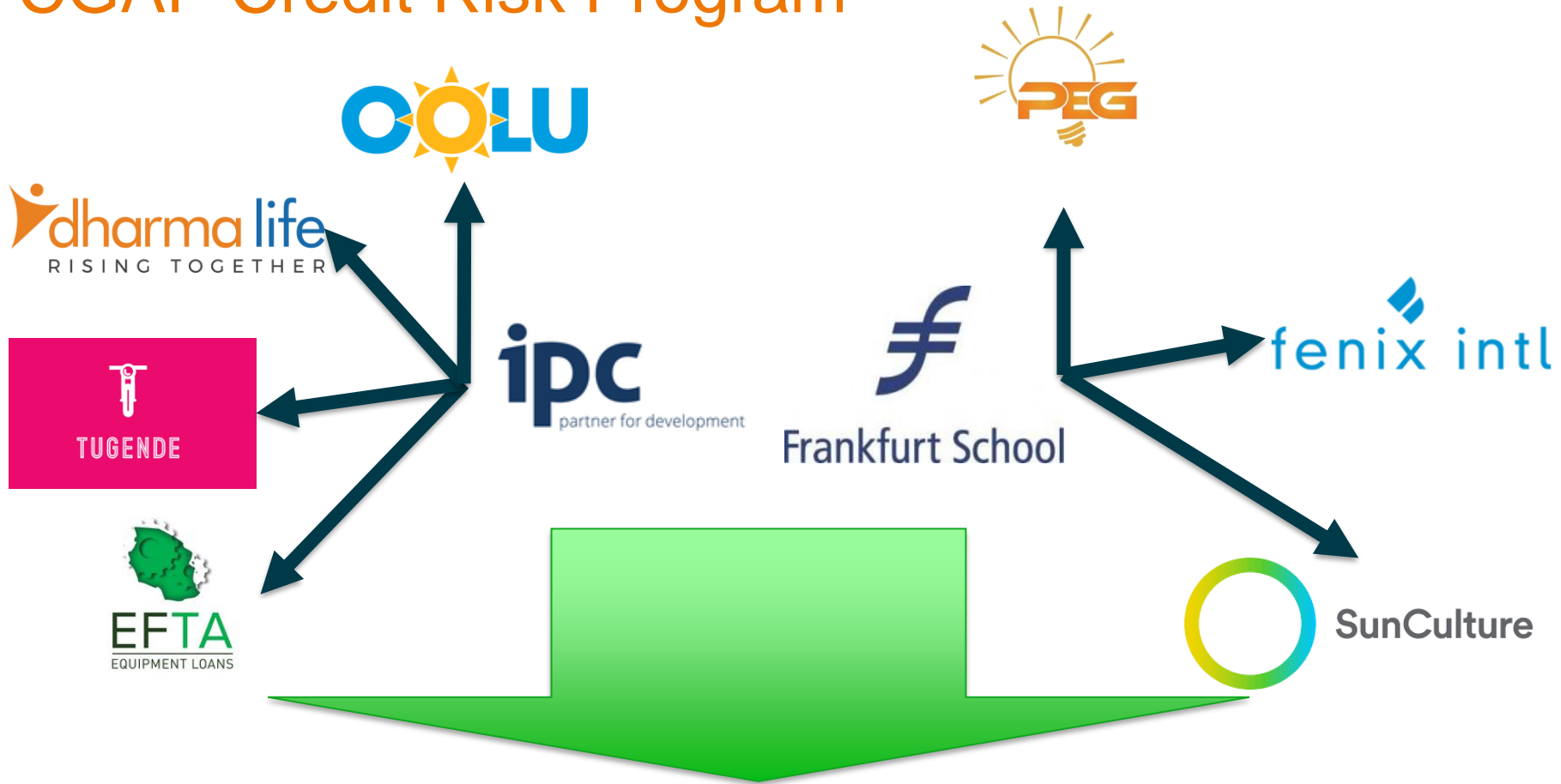
Why is credit risk management important?

Sustainability

Affordability

Development

CGAP Credit Risk Program



Objective of this webinar

- Understand the risk management framework
- Comprehend risks faced by asset finance companies
- Be able to describe the relationships between risks

Risk Management Framework

ERM - ENTERPRISE RISK MANAGEMENT FRAMEWORK

DIMENSIONS

LEVELS

1 Strategy



CORE ELEMENTS

- Objectives and philosophy
- **Appetite**, tolerance, limits

ERM - ENTERPRISE RISK MANAGEMENT FRAMEWORK

DIMENSIONS

LEVELS

2 Operating Model



CORE ELEMENTS

- Decision making
- **Authorities, responsibilities**, approvals
- Incentives, education, control
- Risk processes, control policies
- Risk manual and set-ups

ERM - ENTERPRISE RISK MANAGEMENT FRAMEWORK

DIMENSIONS

LEVELS

3 Methodology



CORE ELEMENTS

- Definition and **quantification**
- Scenario analysis and stress testing
- Mitigation strategies

ERM - ENTERPRISE RISK MANAGEMENT FRAMEWORK

DIMENSIONS

4 Communication

LEVELS

Information **Reporting**

CORE ELEMENTS

- Internal, external communication

DIMENSIONS

5 Infrastructure

LEVELS

Core Banking System, IT & Data

CORE ELEMENTS

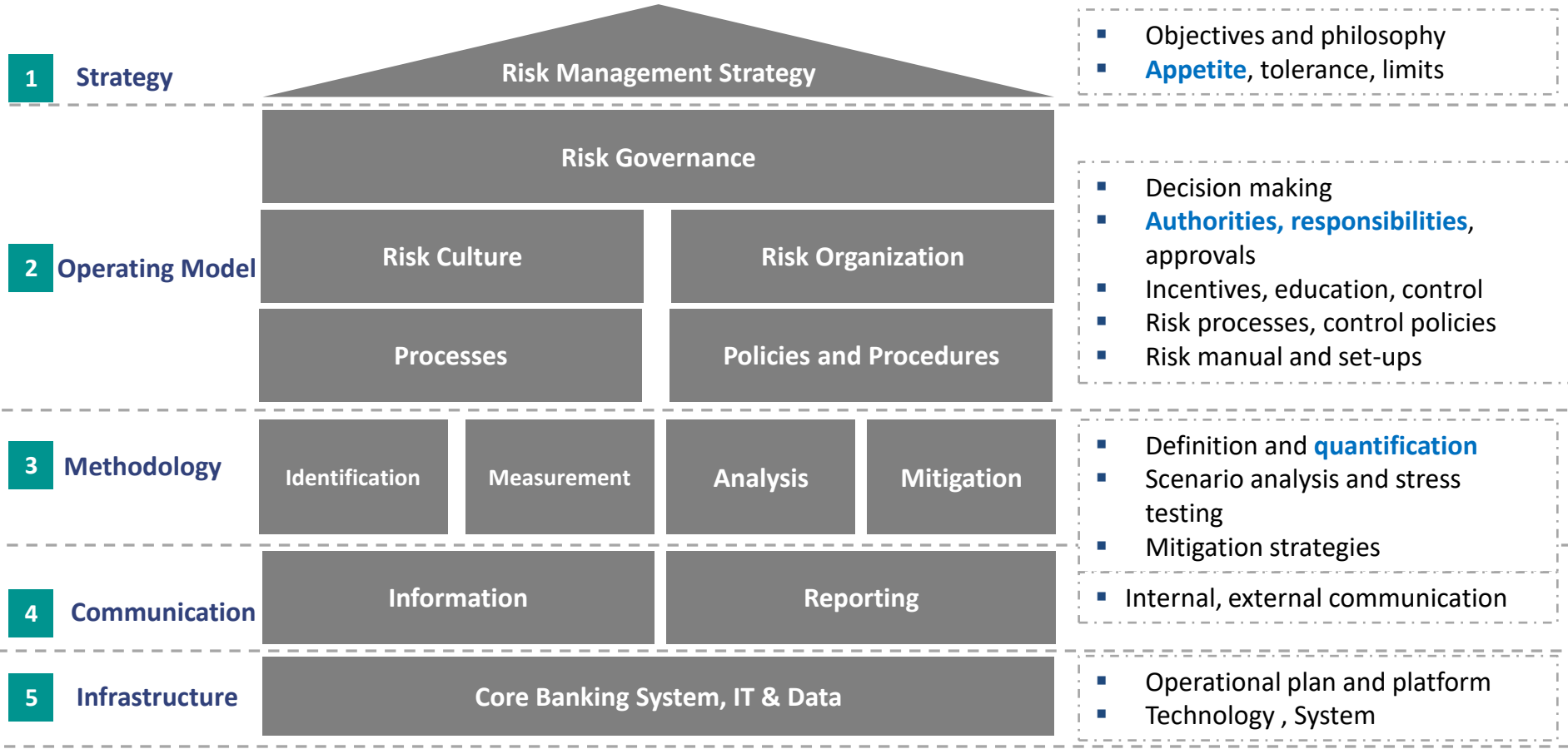
- Operational plan and platform
- Technology , System

ERM - ENTERPRISE RISK MANAGEMENT FRAMEWORK

DIMENSIONS

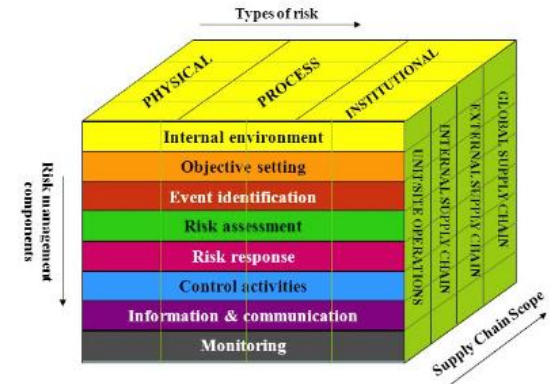
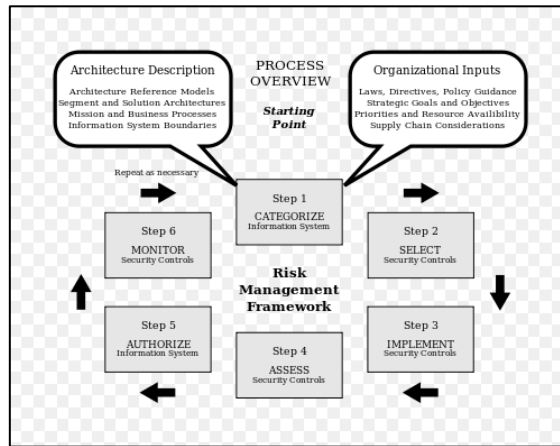
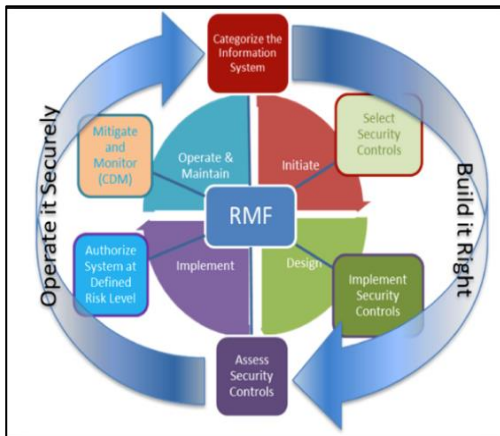
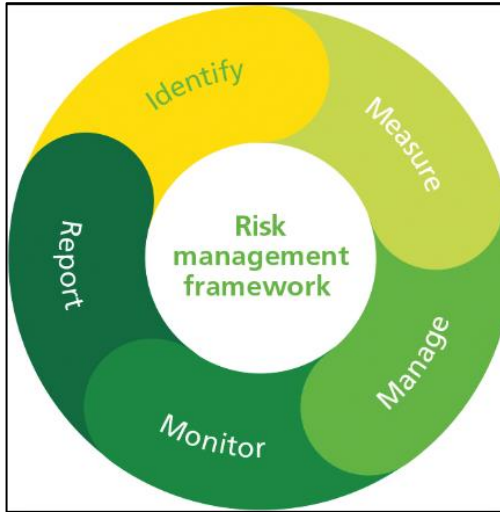
LEVELS

CORE ELEMENTS



Risk management framework

VARIOUS RISK MANAGEMENT FRAMEWORKS TO CHOOSE FROM...



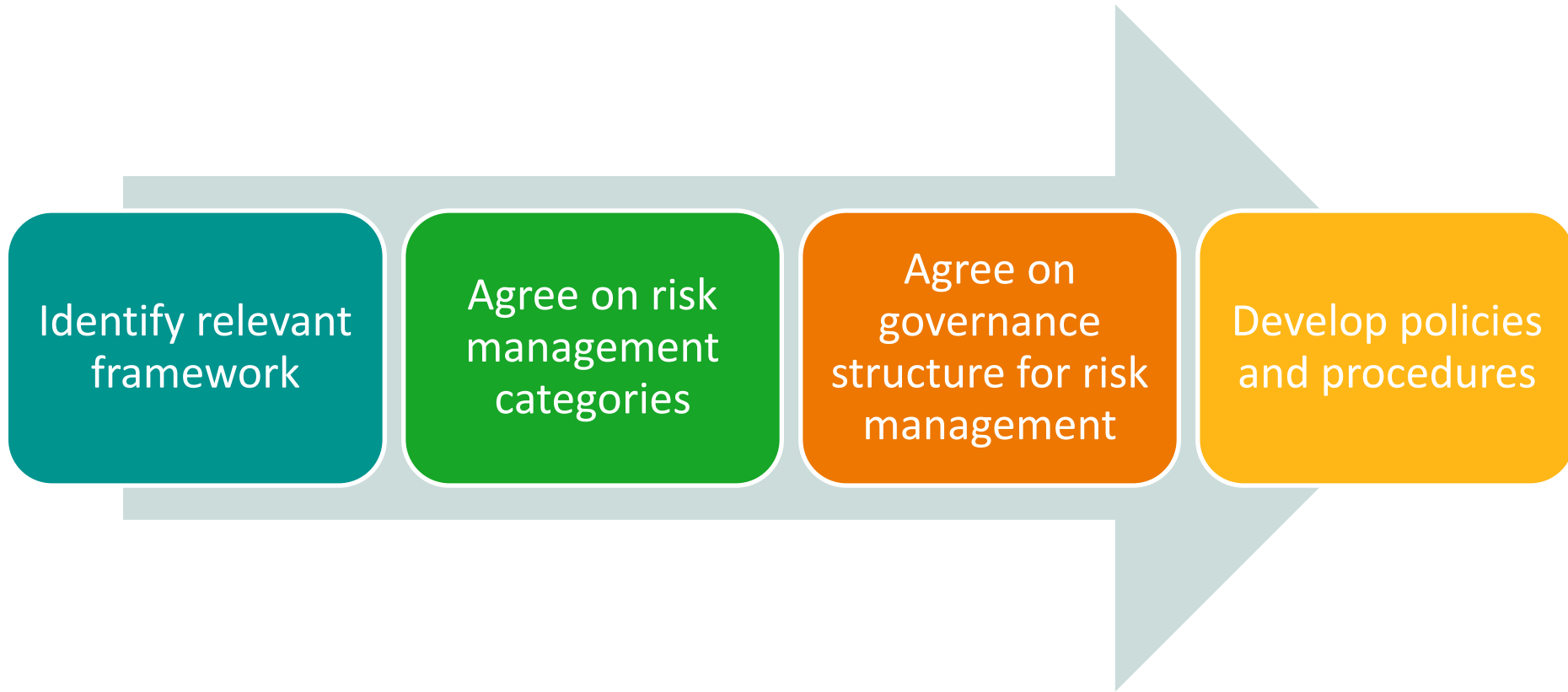
Risk management framework

SELECT APPROPRIATE RISK CATEGORIES



Risk management framework

THE KEY STEPS ARE....





Risk Culture

▶ Corporate Governance

- In its most generic form, corporate governance is defined as the system by which companies are directed and controlled.
- Corporate governance involves regulatory and market mechanisms, and the roles and relationships between a company's management, its board, its shareholders and other stakeholders, and the goals for which the corporation is governed.

Risk Culture

Risk Management starts at the Top

BCBS "Principles for Enhancing Corporate Governance". October 2010.

- Drawing on the lessons learned during the crisis, the **2010 Principles** set out best practices with a particular focus on:
 - 1) the role, qualifications and composition of the board;
 - 2) the importance of an independent risk management function, including a chief risk officer or equivalent;
 - 3) the importance of monitoring risks on an ongoing firm-wide and individual entity basis,
 - 4) the board's oversight of the compensation systems; and
 - 5) the board and senior management's understanding of the bank's operational structure and risks.

Risk Culture

- A Risk Culture Framework



Source: IFC 2015; Risk Culture, Risk Governance and Balanced incentives

Risk Culture: Recommended best practices

Recommended best practices in Risk Culture



- It is not the **Compliance Officer** who does the complying nor the **Risk Manager** who manages the risk!
- A proper Risk Culture means that everyone across the entire hierarchy understands that the “buck stops with him or her”.
- Everyone must identify and manage the risks under their control and diligently carry out the controls embedded in the business processes of the bank.
- Compliance and Risk are facilitators, methodology leaders on best practices in Risk Management. They cannot do it alone.

Participants: What does your organization (or your investees) do to create a culture of risk management?



Risk Appetite and Tolerance

Risk Appetite and Tolerance

Risk Appetite vs. Risk Tolerance



- **Risk appetite** is the amount and type of risk an organization is prepared to pursue or take, in order to attain the objectives of the organization and those of its shareholders and stakeholders. (ISO Guide 73).

"Risk tolerance" is generally used with a more specific meaning that is subordinate to risk appetite. It already begins to operationalize risk appetite by means of tolerance thresholds or limits:



- **Risk tolerance(s)** is/are quantified risk criteria or measures of risk exposure that serve to clarify and communicate risk appetite. Risk tolerances are used in risk evaluation in order to determine the treatment needed for acceptable risk.

Risk Appetite and Tolerance

Risk Appetite & Risk Tolerance



Risk Appetite Statement

- Written statement about types of risk that a financial institution is **willing to accept/avoid in order to achieve its objectives.**
- Should consider material risks and reputation vis-à-vis stakeholders and shall **align with the institution's strategy.**
- Qualitative statements and quantitative measures, relative to earnings, capital, risk measures, liquidity and other measures.
- Should also address more difficult to quantify risks: reputational risk, money laundering and unethical practices.

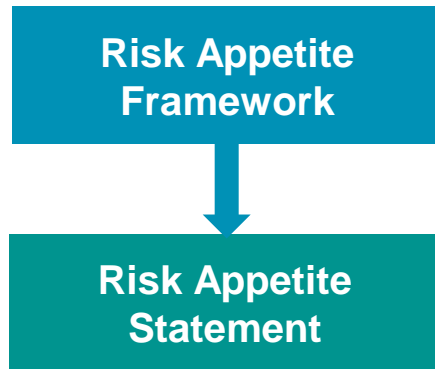
Risk Appetite and Tolerance

Sample Risk Appetite Statement

- The Risk Appetite Statement for Company X articulates the willingness and ability to take risk.
- The Risk Appetite Statement is aligned to Company X's vision and mission and defined for each of the risk categories below
 - Strategic risk
 - Credit risk
 - Operational risk
 - Technology risk

Risk Appetite and Tolerance

Risk Appetite & Risk Tolerance

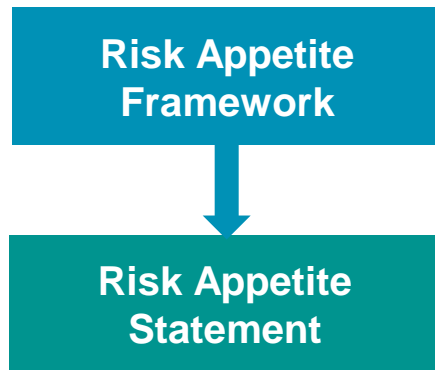


Risk Capacity

- Maximum level of risk given resources, before breaching constraints related to regulatory capital/ liquidity/ operational environment and obligations.

Risk Appetite and Tolerance

Risk Appetite & Risk Tolerance

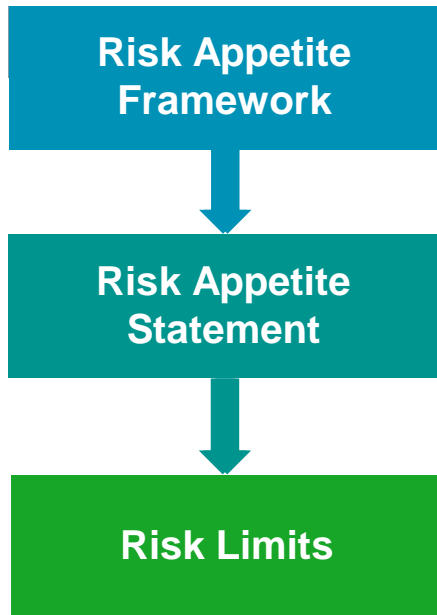


Risk Appetite

- Total amount of risk that an organization is prepared to accept, tolerate, or be exposed to at any point in time while pursuing its business model

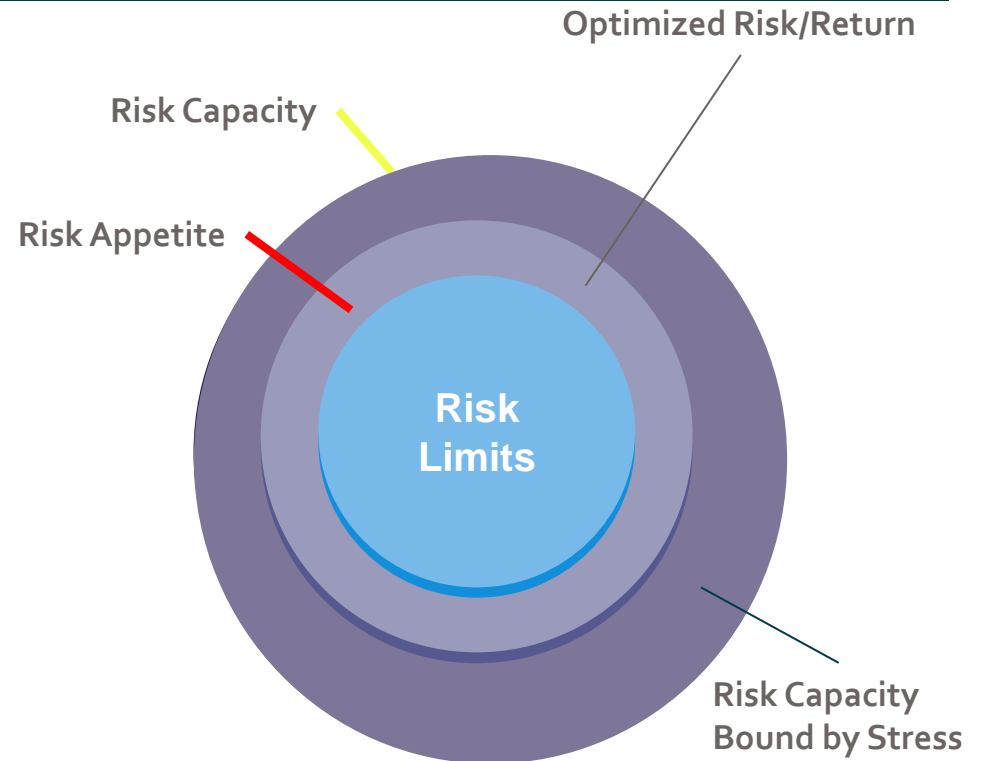
Risk Appetite and Tolerance

Risk Appetite & Risk Tolerance



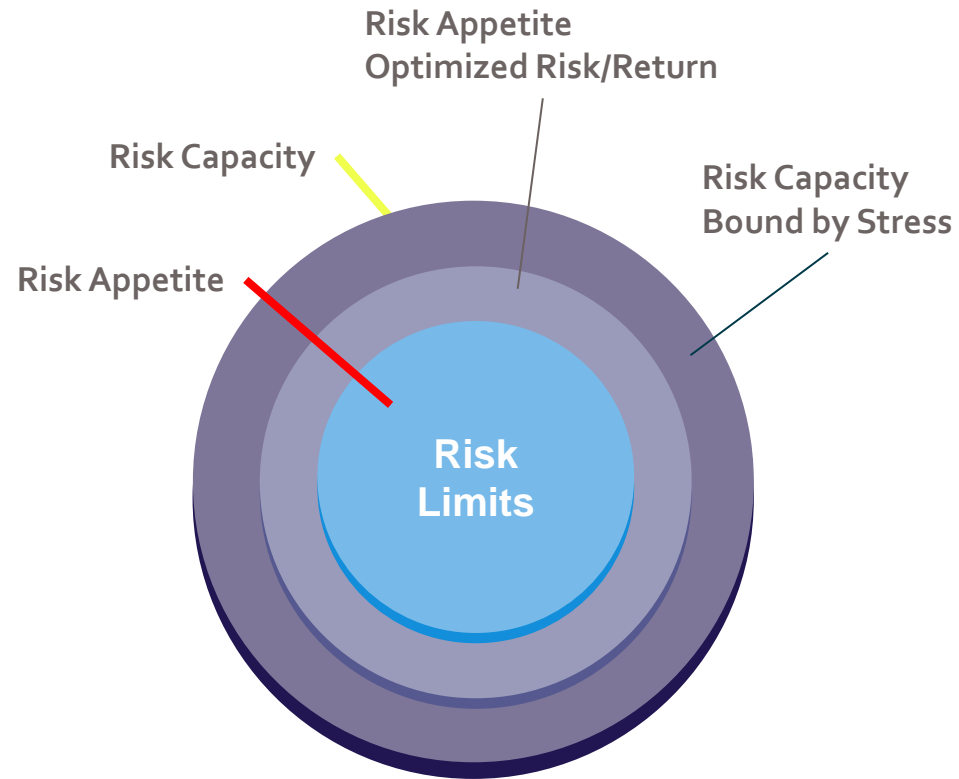
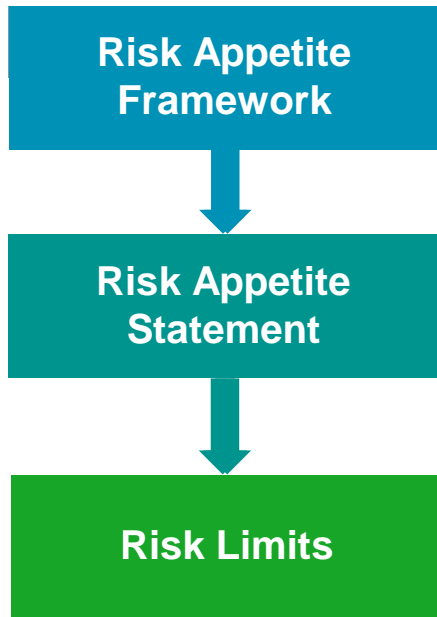
Risk Limits

- Quantitative measures based on forward looking assumptions that allocate the entity's aggregate risk appetite statement to business lines, legal entities, specific risk categories, concentrations, etc.



Risk Appetite and Tolerance

Risk Appetite & Risk Tolerance



Risk Profile

- Point-in-time assessment of the gross and net risk exposures (as appropriate, after taking into account mitigants). These measurements are aggregated within and across each relevant risk category and based on forward looking assumptions.

Poll Question #2:

Which elements of the risk management framework does your organization have in place? (Select all that apply)

1. *Risk Appetite*
2. *Formal Credit Policy*
3. *Established Portfolio Limits*
4. *Board-level Risk Management Committee*
5. *Credit Department*
6. *Independent Risk Management Unit*

Questions?

Time for a 15-minute Break

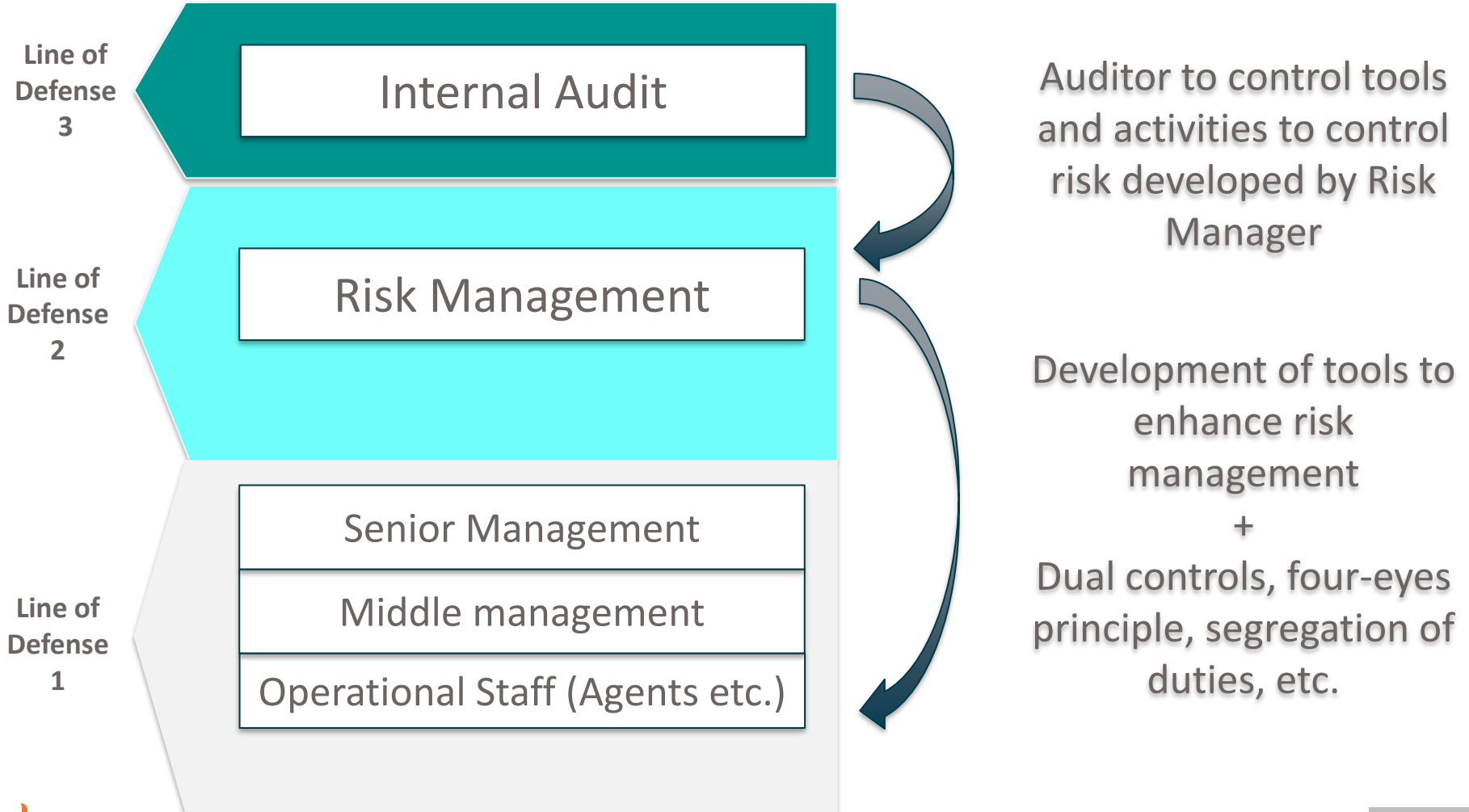




Governance arrangements

Governance and Organization of Risk

The Three Lines of Defense



Governance and Organization of Risk

Three Lines of Defense in Risk Management

1st Line “Asserts”

Business Line

Owns and Manages Risk

- Carefully assess risk: e.g. credit risk of a borrower before entering into a credit agreement
- Monitor the credit risk during the life of a transaction
- Portfolio optimization on the macro and micro level
- Promote a strong culture of adhering to limits and managing risk exposure

Governance and Organization of Risk

Three Lines of Defense in Risk Management

2nd Line “Reports”

Risk Management

Oversees the Risk

- Overarching “risk oversight unit” across all risk types, reporting
- Combination of watchdog and trusted advisor
- Enforce limits and actively challenge business
- Develop methodologies and tools to monitor risk
- Portfolio assessment, analytics, and training

Governance and Organization of Risk

Three Lines of Defense in Risk Management

3rd Line “Assures”

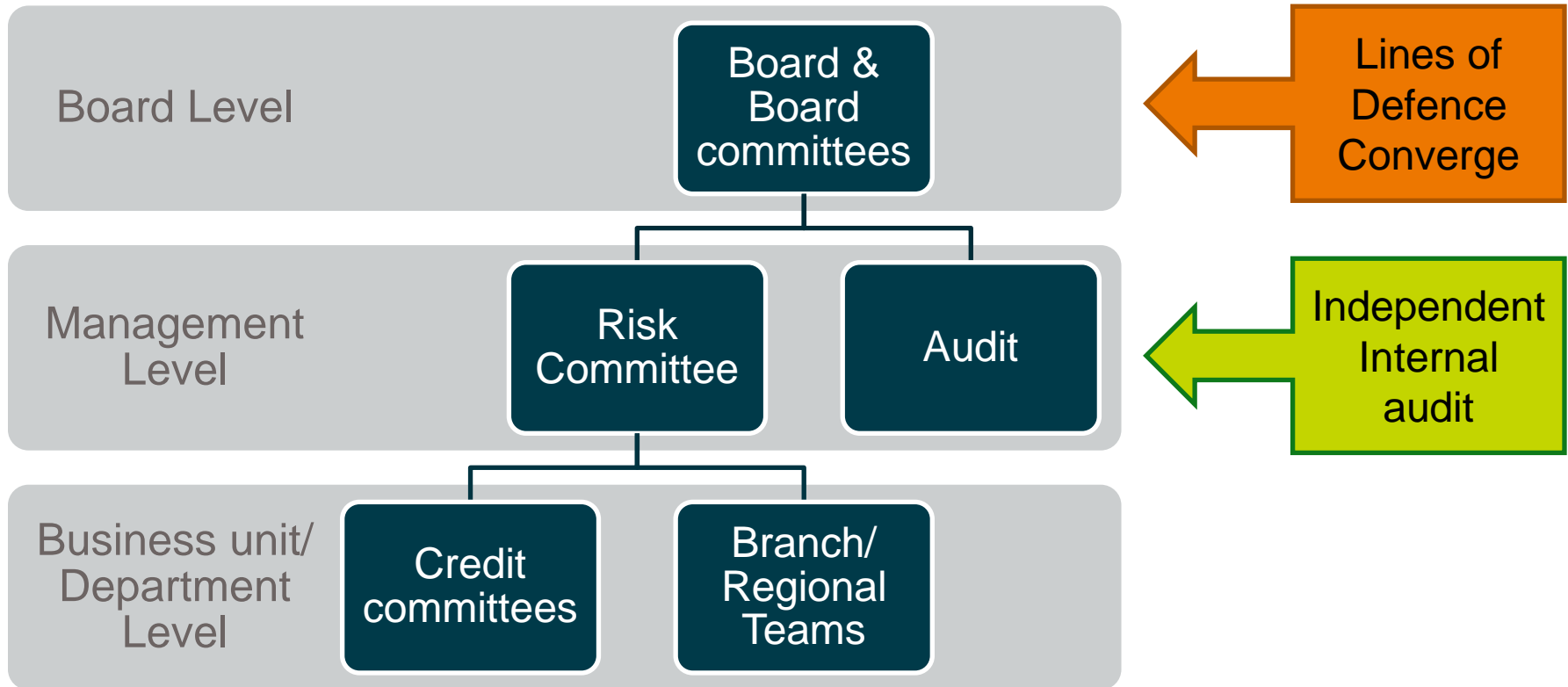
Internal Audit

Independent Assurance

- Independent oversight function with enforcement ability
- Provides assurance over 1st and 2nd lines of defence
- Monitor business activities and ensures compliance with policies
- Conducts special investigations on ad hoc basis

Governance and Organization of Risk

Sample structure for an Asset Finance Company



Governance and Organization of Risk

EVOLUTION OF RISK GOVERNANCE

Early Stage (Assets < \$10M)

- Vision and Mission
- Risk Appetite
- Board
- Management Information System (Loans & Accounting)
- SOPs/
Procedure manuals

Growth (\$10M - \$25M Assets)

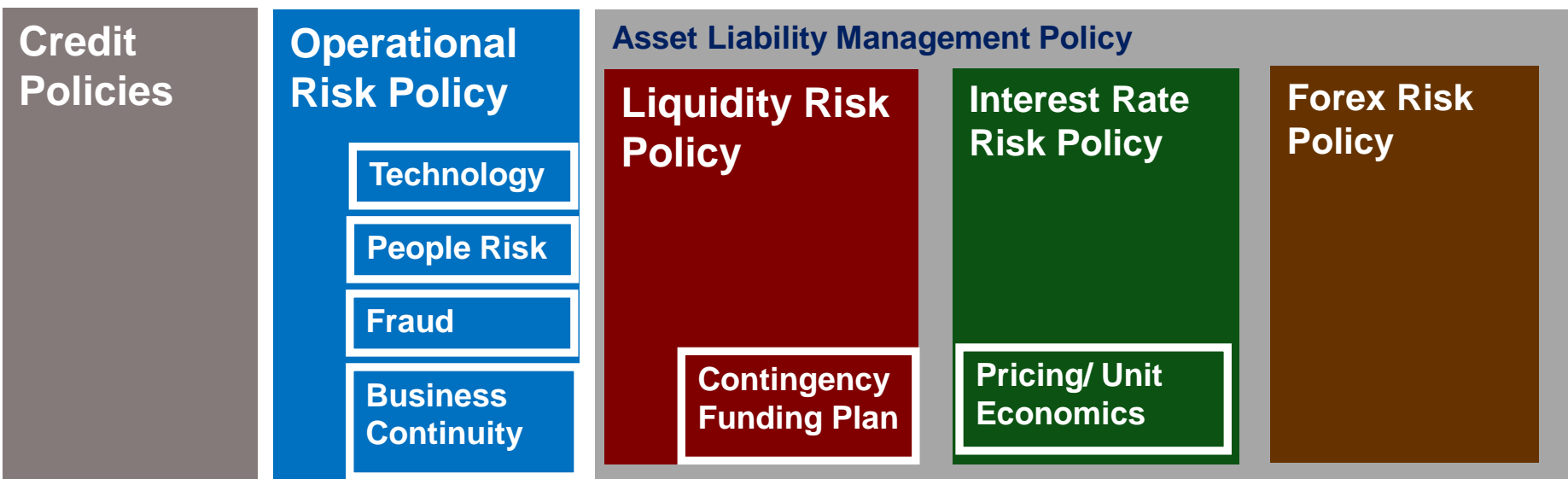
- + Chief Risk Officer
- + Risk Audit (Outsourced)
- + Basic Credit Policies

Mature (>\$25M Assets)

- + Board with sub-committees
- + ERP Software
- + Internal Risk Unit
- + Internal Audit
- + Risk Manuals

Risk Management Policies

Risk Management Framework Policy (Risk Organization & Governance, Risk Appetite)



Risk Management Policies

Detailed credit policy outline

Overview

- Policy scope and objectives
- Risk appetite
- Roles and responsibilities
- Products and markets

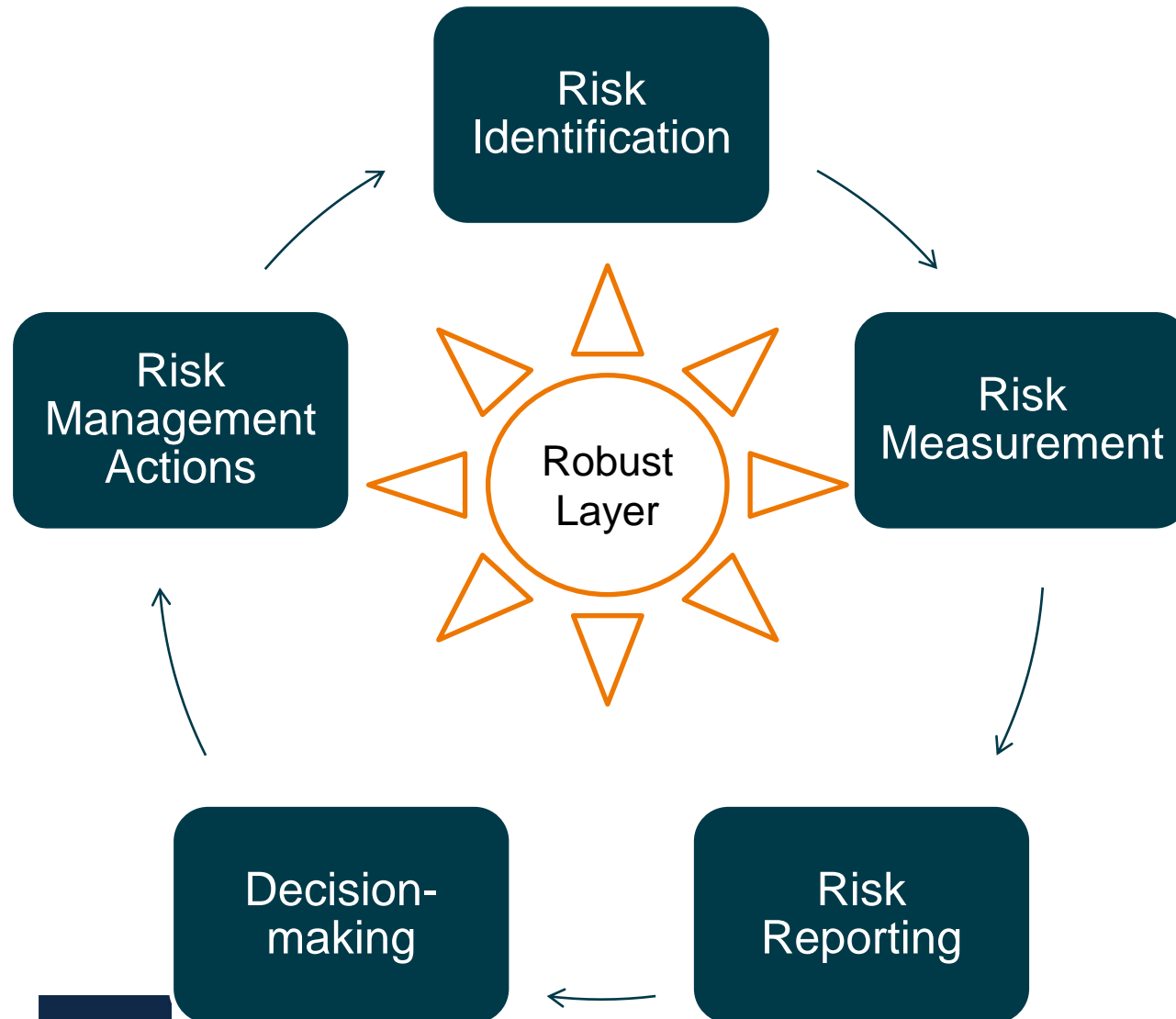
Transaction risk

- Assessment and approval
- Documentation
- Disbursement

Portfolio risk

- Credit Monitoring
- Portfolio Management
- Past Due Obligations

The Risk Management Process



Questions?

GUEST SPEAKER



Sarah Mijabi
VP of Risk
Greenlight Planet

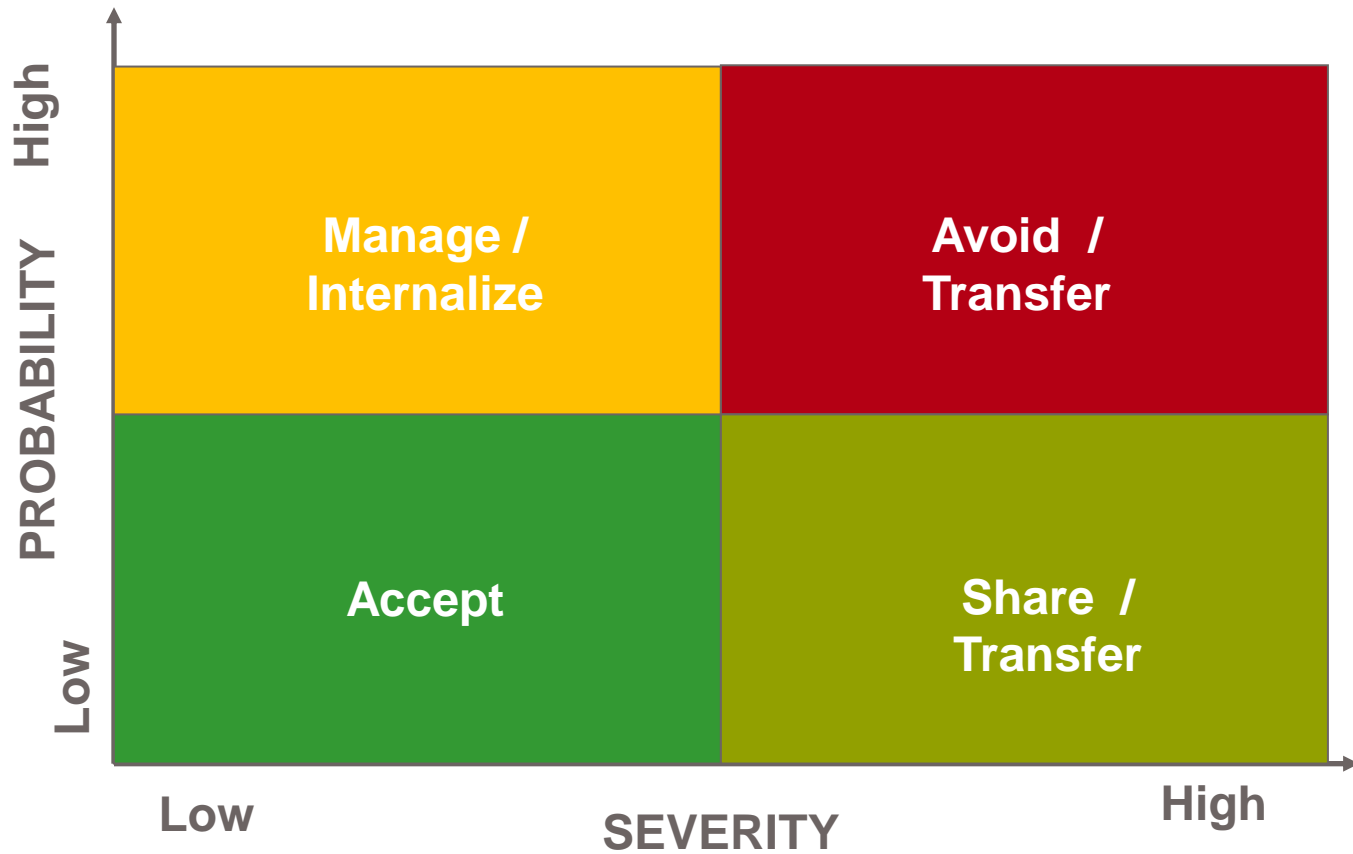


Risk Management Methodology

Potential Risk Management Actions

Risk Severity / Probability Matrix

Macro Risk Map and Risk Management Actions



Potential Risk Management Actions

Risk Severity / Probability Matrix





Investing and Risk

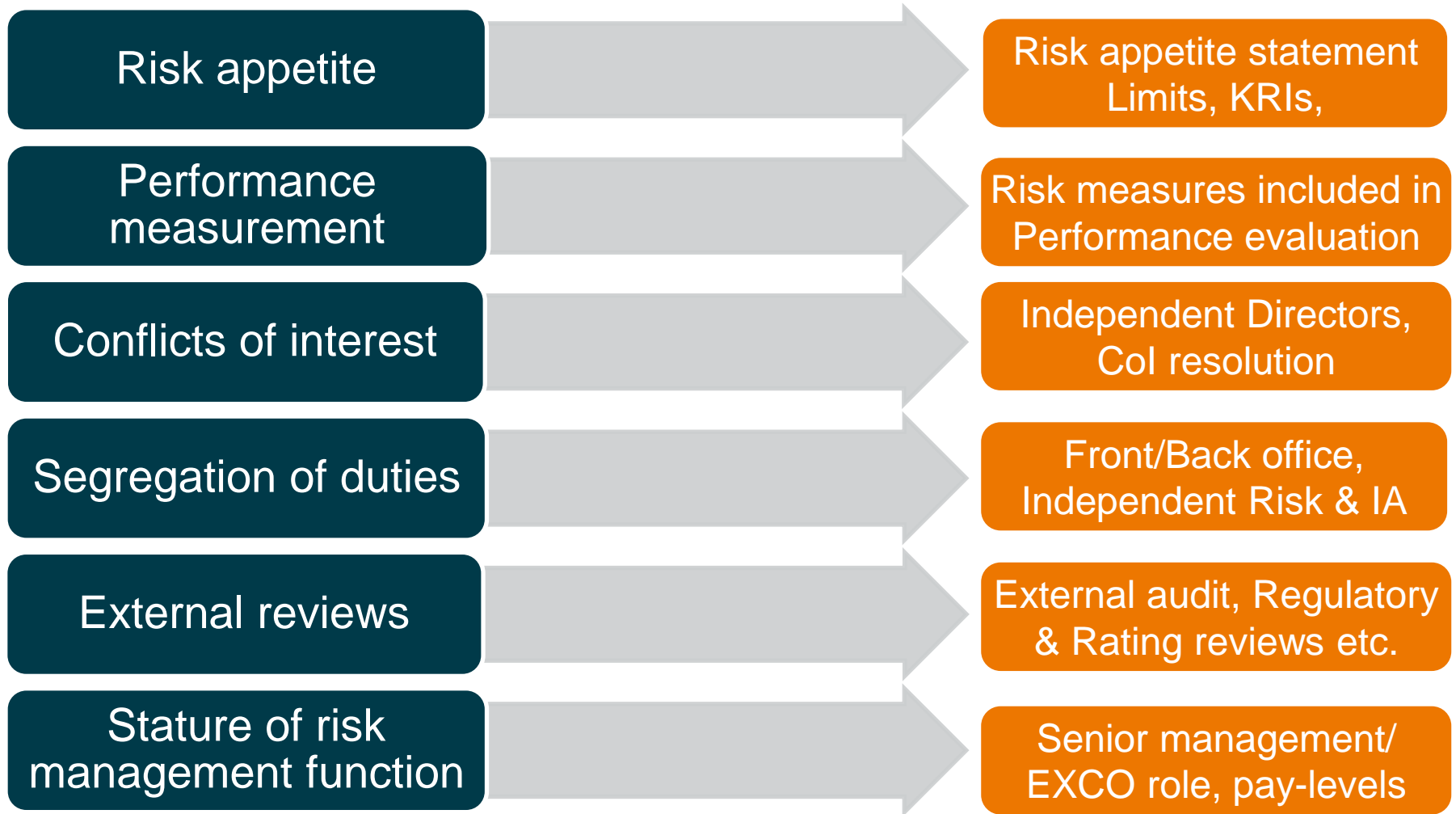
Poll Question #3 (for INVESTORS only): Which of the following best captures your approach to assessing risk management in potential investees?

1. *We only invest in or lend to companies with robust risk management frameworks who can also demonstrate compliance with their own policies*
2. *We need to see that risk management structures are in place, and then we work with companies to improve their implementation*
3. *We are sometimes forced to invest in companies with sub-optimal risk management, but then work to help improve it*
4. *Risk management is not a decisive criterion in our due diligence or investment decision-making*

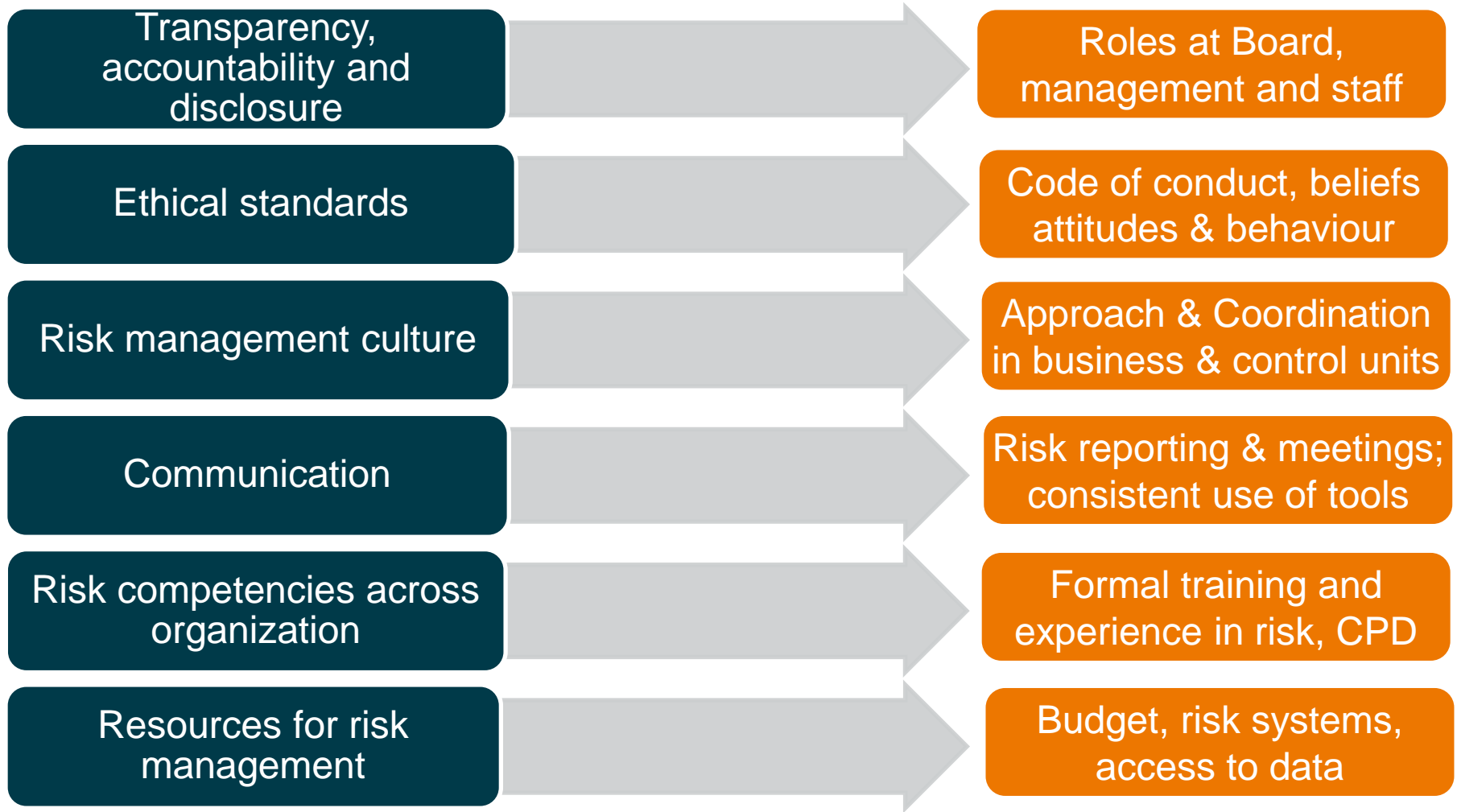
A risk management perspective



Key Risk Governance Principles



Key Risk Governance Principles, cont.

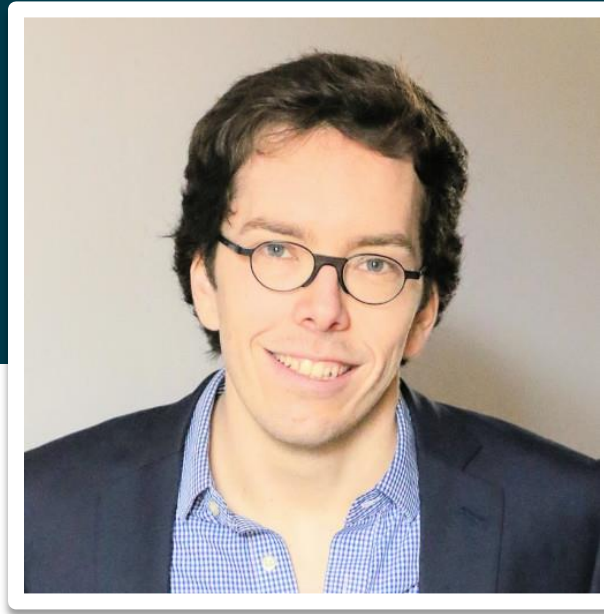


Investing and Risk: Credit assessment

A detailed assessment of the credit including:

- Risk management strategy and appetite*
- Review of credit policies and procedures*
- Organization of credit*
- Assessment of portfolio monitoring and control*
- Review of MIS and reporting*
- Evaluation of agency arrangements*

GUEST SPEAKER



Isaac Williams

Director
IPC GmbH

Questions?

Thank you

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