Risk Limited Corporation's

Top Ten Risk Management Tips©

10. Identify and assess risks

Risk is everywhere. Success in business often comes down to recognizing and managing possible risks associated with potential opportunities and returns. The types of risks faced in most businesses are quite varied and far ranging. Risks typically include both financial and physical categories. Types of risk include sometimes apparent hazards, such as safety and health risks associated with operations, as well as financial risks from exposures to market price volatility, counter party credit defaults, and legal liabilities. Some risks are intuitively obvious; unfortunately, many are not. Risk categories include: Market, Credit, Legal, Regulatory, Political, Operational, Reputational, Event, Country and Model Risks. So first identify possible risks throughout your business.

9. Know the numbers

Systematic processes such as a *RiskRegister®* to identify and rank risks by order of magnitude can be a key first step, but effective risk management strategies typically depend on quantification of risks, often through probabilistic modeling techniques. Said another way: one must 'measure it to manage it.' Measurement and valuation can be one of the most difficult efforts in risk management and finance, but these are crucial for cost effective risk management and informed decision-making. Spend the time and money to get the tools and expertise to best quantify the company's key risks. A close corollary is to know what is in any 'black-box' models used for valuation & reporting.

8. Risks are interrelated

Interactions and correlations of risks are a key element of which to be aware in identifying, quantifying and mitigating risks. For example, exposure to credit risks may also affect market price risks, whereas operational risks such as fraud may create legal and reputational risks. Recognition that risks interact between business activities is the one of the basis for the 'enterprise-wide risk management' approach now widely practiced by leading companies.

7. Continually reassess risks

Things change, and so do risks. Market conditions and volatility levels change, financial strength of counter parties change, physical environments change, geopolitical situations change, and on-and-on. And these changes can be rather sudden, or they can be creeping and hidden. Exposures to risks that result from business activities may also change. Effective risk management requires that one reevaluate risks on an ongoing basis, and processes such as a *RiskAudit®* should be built into the corporate risk management framework to assess both current and projected risk exposures. Forecasting future exposures is necessary since hedge decisions are based on projected risk levels.

6. Commit adequate resources

Effective risk management also requires considerable expertise and resources, from basic risk control, compliance and governance activities, through advanced quantitative risk analysis. The costs for these resources are usually not cheap, but as has been proven repeatedly by high-profile business failures, the cost of losses due to risk management weaknesses or lapses can be catastrophically high. Investment in risk management capabilities for most businesses has a high payoff. Due to the potentially extreme cost of mistakes, risk managers should be especially well trained.

5. Review the cost of risk mitigation

Transferring risks through hedge transactions or other activities is often an effective and advisable risk management technique, but risk mitigation strategy may largely depend on the hedge costs. Risk mitigation strategies also depend on the capacity of the firm to sustain risks and possible losses. Trading activities that are truly for hedging should not be avoided due to concern that trading could be misconstrued as 'speculative'; however, various hedge instruments may not have the same cost effectiveness or appropriateness for every company and environment.

4. Reduce exposure

Risks arise from exposure. A commonly accepted definition of risk is exposure to uncertainty (at least that uncertainty for which one is concerned about the outcome). Reduce the exposure and you likely reduce the risk. The selected approach and structure of business activities can have a significant effect on the exposure & risk levels generated. Commercial agreements and transaction structures may result in transference or acceptance of risks with a counter party. Risk awareness in business processes and commercial activities can lead to opportunities to reduce current and *future* exposures. Billing currency for international purchases is an example of exposure effect.

3. Assess the Risk/Return Ratio

Risk management does not equate to risk aversion; however, decisions driven by risk/reward assessments usually have a higher probability of successful outcomes. A consideration in such risk-based business decision-making should also be the capacity of the firm to sustain risks. As in the well developed finance field of portfolio theory (which in general terms focuses on how investors can best balance risks and rewards in constructing investment portfolios), business decisions based on risk/reward balance should optimize returns.

2. Monitor for quantum shifts in risk levels

A key value of quantitative risk measures is to highlight significant changes in risk levels. Although opinions may differ on the optimal methodology for some valuation metrics, significant changes or trends in risk metrics, such as Value-at-Risk measures, can provide a key signal to management. Best practices designs of management reporting 'dashboards' provide this risk monitoring capability, also showing segment reporting and consolidation to reflect correlations such as offsets in price risks between markets.

1. Create a risk aware culture

Educate the organization in practical aspects of risk management, and that especially includes the most senior business executives and the corporate board of directors. Risk management responsibilities should be clear. Whether it is intuitive actions based on experience and expertise in risk management or whether it is a result of institutionalized risk policies and procedures, effective risk management is typically a key factor in successful businesses. Training and building awareness can lead to a risk management culture that will drive business success.

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