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THE FUTURE OF RISK MANAGEMENT

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When considering the future of risk management, taking stock of where we are now will allow us to identify what action we need to take. As Albert Einstein so clearly stated, "The world as we have created it is a process of our thinking. It cannot be changed without changing our thinking."

There are three key themes to consider when it comes to what the future of risk management looks like - risk data and information and how risk reporting can be elevated, how aligning risk with project methodology can be achieved and the capabilities of risk professionals required in the future.

While exploring the current environment for risk management, we can't avoid the fact that traditional practices are being eclipsed by change taking place in other key management functions. To remain relevant as risk professionals, we need to change our way of thinking and look internally at our own risks – or we may no longer enjoy our seat at the decision table.

1. Bringing value to decision making

The future for risk data and information is already here. Organisations are readily adjusting to an environment that is dynamic, integrated and unpredictable. The need for analysing, monitoring and reporting on risks needs to keep pace with this change to maintain a valuable contribution to decision making.

Risk reporting needs to be objective and presented in real-time, limiting the influences brought about with usual human biases and group think. It also needs to focus on the upside of risks as well as the downside in order to guide decision makers throughout an organisation.

Risk heatmaps

The traditional risk approach is a narrow two-dimensional view created by likelihood and consequence variables. This approach is commonly presented on a risk heatmap with risks represented in green, amber and red. However, there are many drawbacks to this visual representation that may not be considered by decision makers:

"Green" risks by virtue of their individual low rating for likelihood and consequence do not reveal any systemic significance. For example, green risks can trigger other risks, and therefore exceed its 'green' consequence rating. This amplification effect is often not portrayed in traditional risk methodologies.

Risk clusters or 'centres of gravity' contain a group of risks of varying and somewhat random heat colours. The interconnections between these individual risks could be numerous and stronger than any other group of risks on the heatmap. If these links are unable to be detected, risk owners will not be aware that they need to manage and monitor the risks together rather than as discrete items.

Similarly, risk clusters will have a compounded level of likelihood and consequence. These levels may even exceed the likelihood and consequence of the most significant and single "red" risk on the heatmap. This could result in risk clusters unknowingly falling outside of an organisation's risk appetite even though individual risk ratings comply.

Traditional risk management techniques of assessing and managing risks in isolation creates a perception that these risks also manifest in comparative isolation. This thinking may lead risk owners to underestimate the severity of potential contagion and the systemic importance of the risk.

Decision makers require risk insights and a view to the future. Simply regurgitating the same risk data and information that has sufficed in the past will not lead to optimal decision making, especially in today's environment where the stakes are even higher due to the fast pace of change. Risks need to be presented in a way that reflects how the risks interact in terms of network effects, with the expected contagion of consequences lit up across an organisation. Without understanding the systemic risk view the picture is incomplete and organisations will continue to be surprised by downside risk events.

Structural breaks and future modelling

To be of value to a decision maker, modern risk reporting needs to make allowances for the existence of structural breaks. These are events or occurrences whose future trends will not reflect those of the past. For example, Covid-19 has created a structural break in our environment by forcing new ways of working to limit physical contact. Current risks influenced by this event will not be reflected in any of the past risk data and information. There needs to be explicit allowances for the existence of these structural breaks within risk data rather than continuing the traditional approach of simply refreshing risks periodically.

Risk reporting also needs to overcome the issue of insufficient data being used to determine what the future outcomes may look like and understand that past risk data is a poor predictor of the future. Research shows that the trigger events for 17 of the most significant economic crises since 1971 have been macro socio-political and/or macro-economic events not observed before in history. Therefore, how do we account for structural breaks in the system and not rely on historical data for future risk modelling?

The answer lies in a fundamental change in the way we report. It is critical to visually illustrate risk connectivity, contagion and clusters to allow for optimal decision making. In order to achieve this, we can leverage techniques such as network theory and other sophisticated mathematics and analytics. Using these techniques is now accessible without the need for extensive academic training and study. Risk professionals do not necessarily need to understand how the risk data is analysed using these methods, but they will need to understand how to interpret the resultant outputs and speak with confidence to the relevant concepts.

We no longer have the luxury of time on our side. We need to objectively and visually illustrate risk connectivity, contagion and clusters to allow for optimal decision making, and allow decision makers to look beyond the data and focus on risk insights.

2. Aligning risk and project methodology

Organisations are absorbing change and transformation at a rapid pace. To remain relevant, organisations are adopting Agile project management in favour of the traditional 'waterfall' project model.

In the past, there was a reasonably predictable relationship between waterfall project methodology and risk. Waterfall followed a traditional approach of planning and designing followed by a large release on users. This command-and-control-driven work environment meant potential for risk was relatively minor in the early stages of the project lifecycle, so risk was not generally engaged. It wasn't until the project was nearing a major

release that an anticipated spike in risk and consequences identification would be addressed, as the project needed to move through specific approval gates. This late identification of risks could result in large overruns and remediation pressures, which in turn could influence the level of robustness in risk identification in order to keep to delivery targets.

Where risk and Agile working collide

To explore where risk and Agile collide, we need to understand the perceived gaps in their objectives. Agile focuses on bringing speed, momentum and action to a project, and does not follow a linear mindset. Traditional risk management focuses on working deliberately through a defined process and implementing controls in order to achieve the desired and known outcome. Here lies the perception that managing risk will immediately put the brakes on Agile methodology and dilute any advantages of adopting Agile principles. There is no slowing the Agile wave, therefore we need to find a balance where risk shifts its mindset and transforms in order to remain relevant.

There is a significant difference in the risk profile through Agile compared to waterfall project delivery. In Agile, the potential for risk impact is greater at the beginning of the project – not all at once at the end as in the waterfall approach. As an Agile project develops over time, the potential for risk impact becomes minimised as risks are continually identified and mitigated. Risk management is more informed, systematic and reliable due to early and continuous engagement.

In order to find the right balance between robust risk management and preserving the value of Agile methodology, it's important to define the risk operating model at the outset. This model needs to be co-developed so that it supports the principles of Agile and fits in with an organisation's overall risk strategy and appetite. To achieve this, attention needs to be focused on two key areas:

Governance and interaction: When will risk management be involved in order to maintain efficiency while addressing risk? What meetings to attend and what not to attend? When to be involved and when not? Risk professionals need to be engaged from the very beginning of the project and continuously be integrated throughout – not peering in periodically from afar.

Authorising environment: What decision rights will be allocated to which project participants? What is the structure and powers of project governance? How will the correct level of challenge be presented and addressed? Who is responsible for the aggregated view and acceptance of risk? Friction may appear if an organisation is seeking to impose the traditional hierarchical reporting lines of such models as the Three Lines of Defence.

Whatever form of risk model is agreed, this needs to be integrated iteratively and not just at check-in points. On the same account, project managers should expect risk professionals to have a reasonable level of knowledge of Agile methodology and principles in order to remain effective.

3. Developing future risk capability

The above themes all lead to the risk professional of the future having evolved their own personal development, capabilities and skill sets. No longer is a sound understanding of best practice standards, experience implementing traditional risk frameworks and administering risk registers enough for a risk professional to add value to an organisation. The same is true for the key decision makers who sit among the executive and at the board table. In order to drive optimal decision making, these leaders need to challenge the status quo and seek better risk insights and reporting in order to drive a more informed discussion. Without knowing and experiencing what is possible – both parties may not realise a change is required.

Stagnation and a reluctance to move away from 'what we know' can be seen in the current job descriptions posted for risk professionals. Experience in implementing standards such as ISO 31000, using standard risk assessment matrices, completing quarterly risk reporting for senior leadership teams, enabling line 2 activities across an organisation and facilitating risk workshops for front-line people are all commonly sought attributes.

Those recruiting and creating job descriptions for risk roles are guided by the perceived needs of executives and members of governance groups such as the Risk and Audit Committee. Those putting their names forward for the roles emphasise how they fit the job description in order to be a successful candidate. It seems a chicken and egg scenario with neither party seeing a need to change.

To move to a modern view of risk management, risk professionals need to turn up with more. We need to bring experience in risk reporting that goes further than traditional risk heat maps and linear risk registers. We need to upskill and cross-skill with knowledge of project methodologies like Agile, change management driving principles and transformation journeys. We need to illustrate to executive leaders and the board what risk insights look like, and experiment with new ways to visualise risk networks and analyse risk data points.

Finally, for those seeking to employ risk advisors, we also need to cast our net wider when we are recruiting and seek non-traditional skills such as systems thinking, data visualisation, strategy development, learning and development and business development skills.

Risk management as a profession is standing on the edge of an abyss. We need to look internally and manage our own risks. We need to address our own change management factors such as culture, roles and responsibilities, and capability and break out of the traditional risk management mould. If we don't understand the need to change and identify the right people to go on this transformation journey with us, theame thinking that got us into this place will most certainly not move us forward.

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Rachael has developed and implemented risk management frameworks that embed the organisations values and successfully deliver their strategic objectives, developed practical risk models that support organisations on their transformation journey, and assisted executive teams and Boards to understand their own personal accountabilities and deliberately influence risk culture.

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