A RISK CHECKLIST TO WEATHER DIFFICULT TIMES

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How are businesses working out the crisis and what are the best-practices in terms of confronting risks and seizing opportunities? Risk thinking used to be a back office type of thinking and risk reports used to put board members to sleep. Not anymore. As the confusion and the impact of risks have dramatically increased, suddenly those that have developed special skills, flexibility and acumen gather terrific advantages.

Best practices align physical, mental, strategic and governance checks. Any slippage may doom companies to failure or underperformance. Balancing these checks is a necessity for real success.

The Physical Health Check – Technical Risks

Every firm should now be cognizant of where it hurts. Ideally, it should also be aware of its major clients and suppliers' pains. Threats and opportunities come from many different sides. Suddenly, risks are converging and interconnecting, leading to greater complexity. Supply of capital, disruption of markets, and volatility of values address the credit side, the market side and the operations of banks all at the same time. This means companies have to go back to the drawing board to identify, assess, manage and structure risks.

Identifying risks requires a sharing of views at the top level of management fed by bottom-up type of reporting (with open lines of communication in the corporation).

Assessing risks is crucial to have a better understanding of them. Risks cannot be assessed well - otherwise, they would not be risks. The role of the assessment is to grow awareness. The best risks to manage are those that create more downside than upside. Finally, the structuring of risks consists of finding in the network of relationships of the business (investors, clients, suppliers, etc) the different risk exposures, and agreeing in risk sharing towards the least sensitive in order to create value for all.

The Mental Health Check: Behaviors

How is your attitude? Senior management should test itself on the following behavioural risks:

Herd behaviour: Are you following the herd? Many prefer to be wrong with the others than to be wrong alone, which has led us into today's mess.

Optimism: Are you better driver than average? Are you better manager than average? A reality check may be welcome.

Belief perseverance: Have you kept the same views steady for a long time, despite the large shifts in the world? If so, time for a reality check.

Hindsight bias: Are you one of those that tend to think: "I told you so. I knew it". If so, are you truly going back in time or are you second guessing how you would truly have reacted from today's situation, not from the past?

Anchoring: Are you holding on to your stocks because they used to be worth three times more and thus it would be a loss to sell them now? Is your view of your assets linked to what they were a few years ago?

Representativeness: Do you believe that markets will go back up because they always do? Some true changes happen in life and we have to accept the possibility of it.

All these behavioural patterns are liabilities to your awareness of risks. Checking will help you figure out the reality.

Strategic Risks

As major shifts happen, strategies need to be revisited. While strategic thinking is complex, and the building of strategies requires much work, there are ways to test the pertinence of overall strategic choices. Smart moves will lever the company's distinctiveness, objectives, values, culture, capabilities in terms of skills and resources and resources in terms of assets, clients, and partners; not fall into psychological traps related to over-confidence; and address significant market opportunities.

Once the strategy has been well assessed and the move is agreed upon, all change management techniques have to be involved. Quality leadership, aligning all towards the newly defined goal, will consistently drive towards success. But, of course, mistakes can also be made at leadership level, which leads us to governance risks.

Governance Risks

Leaders are human. While the selection process is high, good leaders in some circumstances may turn out to be ineffective. The problem comes when a failing leader lasts for too long. In order to control for that risk, governance rules need to apply, not to constrain but simply to make sure that if leadership failure occurs, it does not become too costly to the organization.

Governance can be self-checked in any organization. Classical factors are a domineering CEO, an inefficient board, conflicts of interest at board or senior management levels, compensation schemes that have strong side effects and a board not well-aligned to its mission (whether supervisory, strategic, connecting or hands-on). Once good governance is insured, the structures are in place for continued corporate awareness.

When companies have done their checks, the basis for success is there even in tough times.

Professor Didier Cossin is Professor of Banking and Finance at IMD. He teaches on the following IMD programs: Strategic Finance, High Performance Boards, Breakthrough Program for Senior Executives, Orchestrating Winning Performance and Leading the Global Enterprise.

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