Balanced Risk Management

A universal approach to identifying, evaluating and managing risk

An Organisation is Subject to Various Commercial "Risks" that Are Evident at Various Levels of the Business, from the Corporate or Strategic Level to the Operational and Business Activity Level.

- According to the International Organisation for Standardisation's publication ISO 31000:2009 and the Australia/New Zealand standard for risk management, AS/NZS 4360:2004, the term risk is defined as:

  "...the possibility of something happening that impacts on your objectives. It is the chance to either make a gain or a loss. It is measured in terms of likelihood and consequence."

- Chairmont summarises the definition of risk as "the likelihood of an event occurring and having an impact on an organisation's overall success". The types of "events" that may occur and have an impact on an organisation are numerous and varied, and they change as the business changes.

  The "impact" on an organisation of an event occurring may be of an economic, legal, reputational and/or other nature. Further, as indicated in the definition of risk above, the impact may provide a benefit to, or have an adverse effect on the organisation.

We Recommend that an Organisation Follows a "Balanced" Approach to Managing the Risks Associated with its Business.

- In this regard, we recommend that an organisation follows a sensible or moderate approach to risk management.
- We believe that it's inappropriate for an organisation to be too "risk prone" in managing its business, or overly commercial or entrepreneurial in its business practices, at the expense of having an appropriate risk management strategy or framework.
- We also believe that it's inappropriate for an organisation to be too "risk averse" or overly judicious in managing the risks associated with its business, at the expense of availing itself to the opportunities of creating a competitive advantage and increasing shareholder wealth.

In Today's Global Business and Economic Environment, Competition is Increasingly Fierce Adding to the Pressure on Businesses to Perform.

Diagram 1: The pressures today on business performance

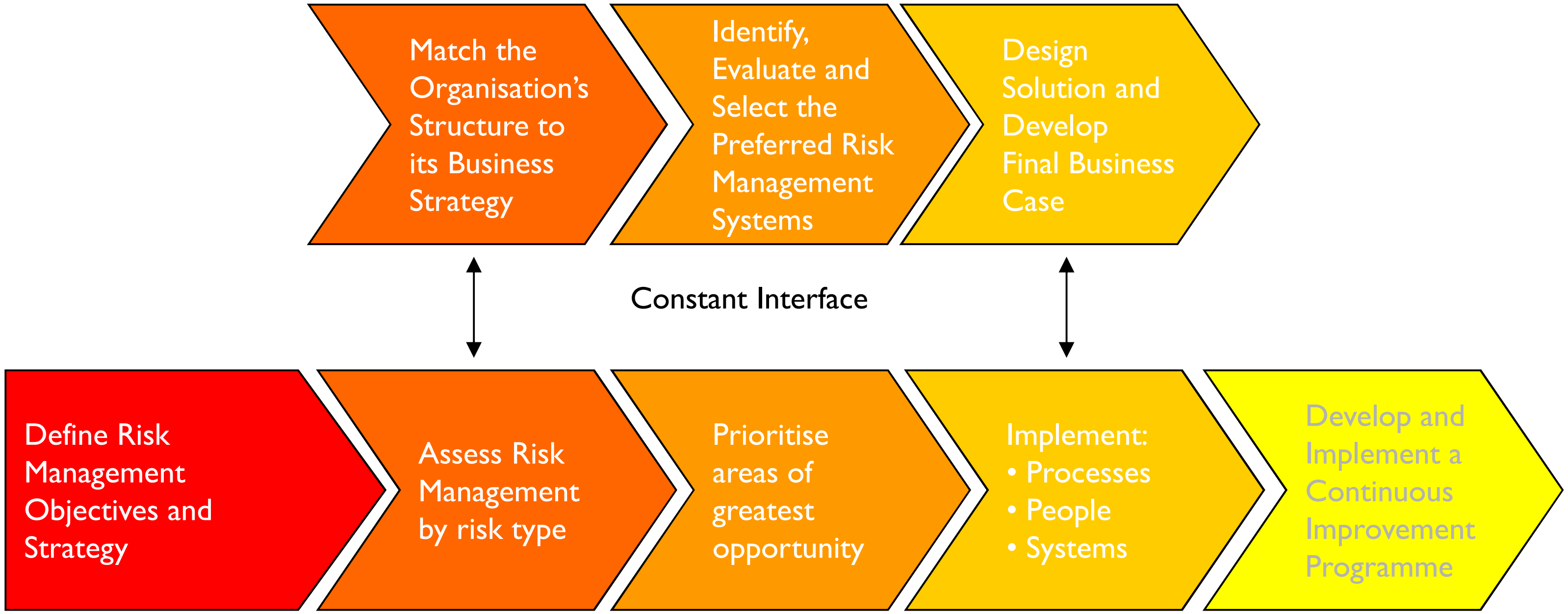
Generally, Organisations Manage the Risks Associated with their Businesses to Some Extent, or at One Level or Another.

- However, an organisation's risk management practices and procedures may not be developed and/or implemented fully, or to their optimum level.
- Efficient and effective, or "best practice" risk management provides an organisation with a significant opportunity to realise a number of major benefits including:
  - satisfying the organisation's critical business objectives and achieving a competitive advantage;
  - enhanced operational performance and productivity, and hence, profitability of the organisation;
  - identifying opportunities to reduce the expenditure of the organisation and improve the profitability of the business;
  - increasing the likelihood of identifying and being able to take advantage of new business opportunities;
  - increasing the likelihood of identifying new threats to the organisation and being able to manage the relevant threats to their timely resolution; and
  - helping to ensure the organisation's compliance with the requirements of the law and relevant regulatory authorities.

Our Balanced Risk Management Methodology May be Integrated into a Client's Overall Strategy and Planning, Governance and Business Culture.

Chairmont's comprehensive risk management approach may be applied to the whole of an organisaiton and its many business units or to specific business functions, business activities and corporate projects .

Diagram 2: Chairmont's approach to Balanced Risk Management



An organisation may follow Chairmont's Balanced Risk Management methodology in conducting a review of its current risk management practices and methods, and identify opportunities to develop and implement an enhanced risk management programme.

A Critical Stage of Work in Our Approach to Risk Management is the Implementation of a Continuous Improvement Programme.

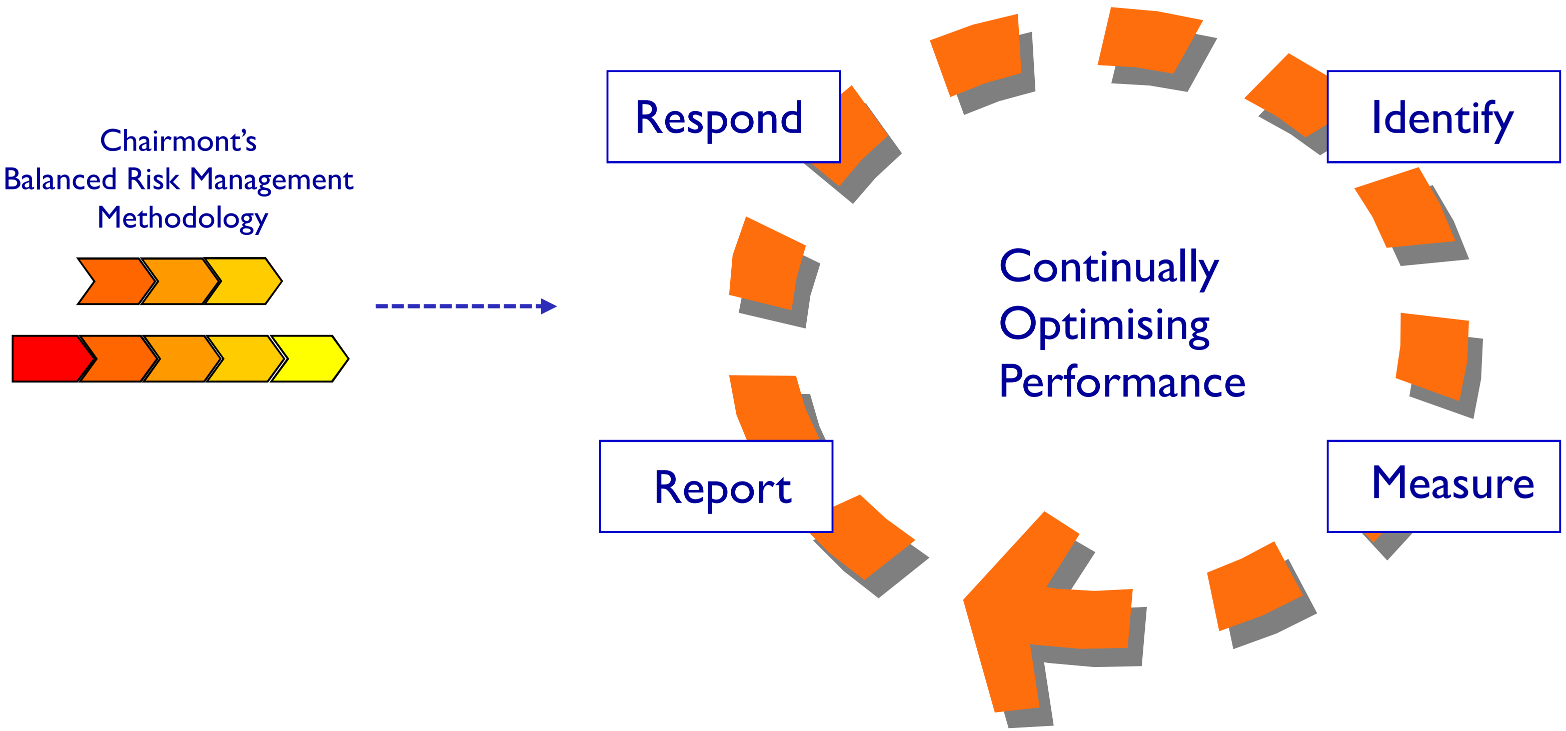


Diagram 3: The continuous improvement cycle in a Balanced Risk Management approach

Ensuring the continued relevance of an organisation's risk strategy in a changing world is of fundamental importance.

A Focus on Balanced Risk Management in the Banking and Finance Industry

Banks and Financial Institutions Are Required to Manage Different Types of Risks that Are Both Broad and Varied in their Nature.

These critical areas of risk may move together or independently of each other. Further, new types of business risk emerge as a bank changes the way it conducts its business. As an example, when a bank outsources its "back office" operations including its business systems to an outsourced provider, a number of risks occur that were not previously relevant to the bank.

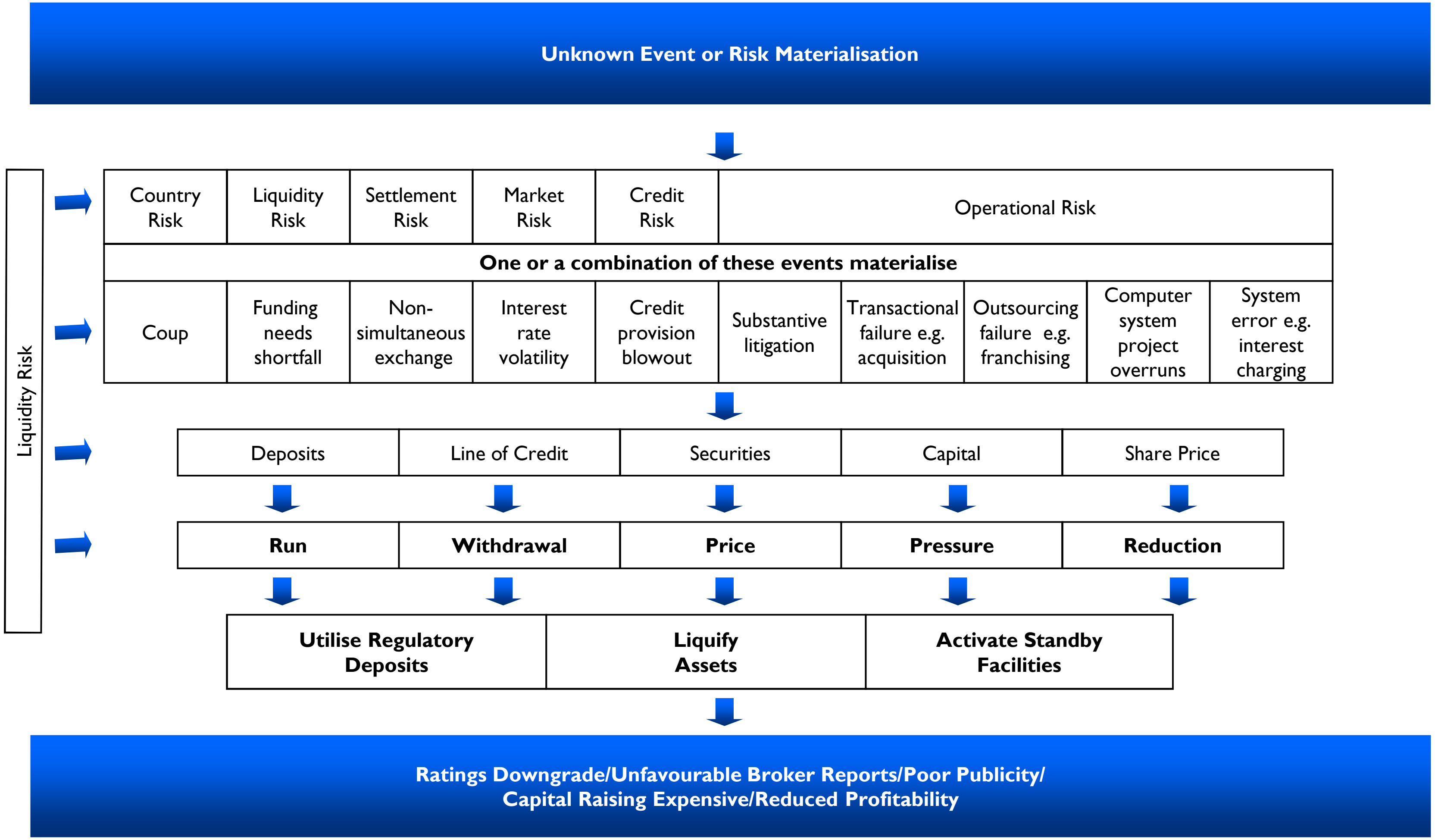
Diagram 4: Key areas of risk associated with a bank or financial institution

Country Risk	Settlement Risk	Credit Risk
Liquidity Risk	Market Risk	Operational Risk

At Chairmont, we recommend a "top-down" approach to risk management to ensure that not only the broad areas of risk are identified and addressed, but also the detailed and specific types of risk are identified and managed to the benefit of the organisation.

Banks and Financial Institutions Are Required to Manage Different Types of Risks that Are Both Broad and Varied in their Nature (continued).

Diagram 5: The impact on a bank or financial institution of various key risks and events occurring



Banks and Financial Institutions Have a Need to Address the Strict Requirements of the Australian Prudential Regulation Authority (APRA) and the Bank for International Settlements (BIS).

- In developing a suitable risk management strategy, banks and a wide range of other financial institutions including credit unions, building societies, general insurance and reinsurance companies, life insurance and most members of the superannuation industry are required to address various Policy Statements issued by APRA regarding a number of key areas of risk associated with financial services organisations.

- Relevant organisations are also required to implement the frameworks of Basel I, II and III as developed by the Basel Committee on Banking Supervision (BCBS). BCBS is a 17 member secretariat provided by BIS, an intergovernmental organisation of central banks that "…serves central banks in their pursuit of monetary and financial stability, to foster international cooperation in those areas and to act as a bank for central banks." (source: "About BIS", web page of BIS, 14 June 2012).

- The Basel Accords are global regulatory standards on bank capital adequacy, stress testing and market liquidity risk. Further, the Basel Accords have been developed as "…a comprehensive set of reform measures to strengthen the regulation, supervision and risk management of the banking sector." (source: "Monetary & Financial Stability", web page of BIS, 14 June 2012).

Chairmont is highly experienced in addressing the requirements of APRA, Basel I, II and III and other legal compliance and regulatory requirements having conducted a number of engagements involving prudential authority reviews , enforceable undertakings and other relevant engagements.

Chairmont's Approach to Risk Management Provides the Finance Industry with Significant Opportunities to Realise a Number of Major Benefits.

- In addition to the general business benefits of a implementing a balanced risk management strategy referred to earlier, banks and financial institutions may also benefit from our approach to risk management by:
  - being able to make optimal use of their available funds and capital;
  - being able to favourably influence share analysts' reports about the organisation;
  - being able to favourably influence credit ratings issued for the organisation by the relevant credit rating agencies;
  - allowing the organisation to negotiate the raising of additional capital at the most cost effective rates available in the market place; and
  - enhancing the reputation of the business amongst its customers, business partners and the public, overall.

- An underdeveloped risk management strategy, or a risk management strategy that is not fully implemented and regularly reviewed and improved, may lead to a difference in a bank's ability to raise additional funds, the cost to the bank of raising additional funds and the bank's credit rating.

Other Chairmont Tools and Techniques Relevant to Achieving Balanced Risk Management

Chairmont Uses a Number of Other Methodologies, and Diagnostic Tools and Techniques that Are Associated with our Balanced Risk Management Methodology.

Planning Diagnostic

- We have identified that an organisation's financial planning and reporting framework can become suboptimal and ineffective as certain risks undermine the planning process leading to incorrect risk/return scenarios being considered. This can result in poorly informed decision making that produce value reducing outcomes and place future shareholder value at risk.

  Our in-house developed budgeting, planning and reporting ("Planning") diagnostic provides an organisation with a focused "health check" on the performance of their existing planning and reporting framework.

  Our Planning diagnostic addresses the effectiveness of three key planning drivers, namely governance, people and culture, and process and structure. The "state of health" of an organisation's budget and planning framework is determined against these three drivers by testing it for 16 distinct and separate risk types. Rectification is enabled through a detailed scope and implementation plan that returns an organisation's planning framework to its appropriate health, or optimal effectiveness level commensurate with its stakeholder/shareholder value objectives.

We have Developed a Number of Other Methodologies, and Diagnostic Tools and Techniques that Are Associated with our Balanced Risk Management Methodology (continued).

Transtheoretical Modeling

- The Transtheoretical Model ("TTM") of behavioural change suggests that a person's 'readiness to change' can explain when and why people change. Behavioural frameworks provide a way of understanding why people might engage in behaviour A rather than behaviour B, and enable psychologists to predict how people will behave under different conditions in different environments.

  Chairmont applied a TTM approach during an engagement with a financial services client that required a better understanding of the "drivers" of its customers' behaviours regarding a particular savings product .

  To ensure the success of the product, our client sought to manage the risks associated with future enhancements to the design, development, distribution and marketing of the product.

Structural Path Equation Modeling ("SPEM")

- The widely used applications of structural equation modeling analysis typically focus on observing the simple one-to-one relationships between "independent" and "dependent" variables in order to understand cause and effect transmission dynamics.

We have Developed a Number of Other Methodologies, and Diagnostic Tools and Techniques that Are Associated with our Balanced Risk Management Methodology (continued).

Chairmont's SPEM diagnostic is based on an enhanced modeling approach which introduces a third variable type referred to as "mediating", which provides an association between dependent and independent variables.

Chairmont's use of its SPEM diagnostic overcomes the rudimentary weaknesses of traditional methods of risk management.

SPEM may be applied to the finance industry in conducing an analysis of the relationship between interest rate increases and home loan arrears.

At Chairmont, We Offer a Wealth of Experience in Providing Focused Risk Management Advice and Assistance.

- Our consultants offer both academic as well as practical knowledge and experience in conducting risk management advisory engagements.

- In developing our proprietary Balanced Risk Management methodology and associated tools and techniques, we referred to our knowledge of a wide range of risk management strategies and "best practice" methodologies. We also referred to our knowledge of the market for risk management software.

- Chairmont, however, is not contracted to, or associated with providers of risk management software and therefore offers strictly independent advice and assistance to its clients.

- Our methodology includes a series of focused questionnaires developed to address key areas of business risk.

- In addition to our comprehensive approach to balanced risk management , we also provide expertise in project management and implementing our advice.

Our risk management methodology provides an emphasis on accurate risk measurement, and is innovative and based on a world class approach to managing risk including risks arising from a new and constantly changing economy.