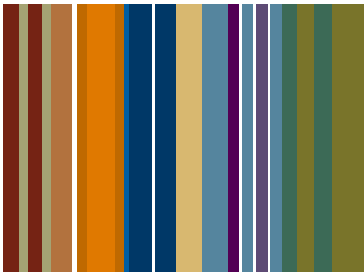
SUNGARD ADAPTIV



FIT FOR PURPOSE? REASSESSING THE ROLE OF RISK MANAGEMENT

Josie Palazzolo
product manager, Senior Vice President,
Adaptiv Product Management SunGard Adaptiv

As the industry reassesses the role of risk management, and keeps up with new regulatory demands, legacy systems are becoming a constraint to progress. Josie Palazzolo outlines what capabilities a modern-day risk application must possess and how advancements in technology can make these applications a reality.

It is the unfortunate lot of risk managers that when their stock is rising, the stock of their institutions is falling. And when the institution is enjoying a boom period, the risk manager is often the first to be ignored and the last to be awarded a budgetary boost.

Currently risk managers have never faced so many requirements – from investors demanding more transparency, from regulators and their new Accords, and from senior management seeking more regular updates. Their workload has never been larger yet the tools and budgets at their disposal have not kept pace.

Indeed many risk managers are finding they are being asked to do more with less. They are under pressure to reduce the cost of maintaining their current risk processes with reduced budgets in IT and with reduced staffing levels in the Risk Department. To compound the dilemma, many risk managers are saddled with legacy systems that cannot even meet their current requirements and are too inflexible to be adapted or improved to meet new regulation.

For risk managers this is a source of constant frustration. At a time when they are under the spotlight and presented with an opportunity to demonstrate both their individual worth and the value of their profession, they too often find themselves held back by the operational restrictions that result from sub-standard applications.

For example, a typical risk analyst at a small to mid-sized institution with a growing but modest derivatives portfolio will mostly be concerned with ensuring trading hedging strategies meet the risk appetite of the firm and that diversification effects across business lines are within policy. Even so they can soon find themselves managing as many as 50,000 open positions. Rather than analysing the risk data and adding strategic value to the institution, risk analysts are increasingly finding that the majority of their time is taken up with ensuring numerous calculations are running on time and that the risk data, sourced from multiple front office departments, is accurate and reliable. In a time of widespread automation, risk management is one of the

few roles that have become an increasingly manually-intensive and iterative process.

RE-EVALUATING RISK MANAGEMENT:

The financial crisis led to a re-evaluation of risk management and what constitutes best practice. From a regulatory perspective, the update of the Basel Accord demonstrates the kind of changes that risk managers must now deal with. In addition to a higher capital charge, there are also new risk measures being demanded by the regulators, such as incremental risk charges; credit valuation adjustments (CVAs); more regular and rigorous stress tests, Stress VaR and subjecting staple numerical measures such as Value at Risk (VaR) to a simulation-based environment.

The themes that underline these regulatory requirements are also evident in the demands of banks' senior management and end investors. They demand transparency and greater resilience, meaning that risk managers now have to produce more detailed reports that cover the entire enterprise, show independence from the front office, are calculated in a timely manner and are fully accurate.

Many of these new demands have merely confirmed what risk managers have been stressing for years – that risk calculation and aggregation of data must be conducted at an enterprise-wide level; that the data must be collected in a timely fashion; and that any calculations made must ultimately be expressed in a business context and not merely exist as an isolated series of numbers.

But while it is gratifying to have your viewpoint acknowledged, the satisfaction is tempered by the fact that risk managers are often ill-equipped to put these ideas into practice. Many are realising that their current legacy risk systems are unable to meet either the pace or the breadth of these changes. People are now seeking a risk application that provides the capabilities required in a manageable and affordable framework.

A FIT-FOR-PURPOSE RISK APPLICATION:

In order to be fit-for-purpose in today's environment, a risk application must be available as a centralised solution that is able to collect, collate and aggregate information from multiple systems within the bank. This makes it possible for risk managers to have an enterprise-wide view of their exposures and compile their own, independent, risk analysis rather than relying on results supplied by front-office staff at each different business line or department.

Risk managers must be able to drill down and get to the bottom of every risk number presented in a final report. Transparency is vital in this regard. Accuracy is obviously important as is the ability to make corrections easily and quickly without undue disruption. Regulators are taking far more interest in the timeliness of risk data – after all, there is little value in calculations that are based on data that is three days old because no-one acts on stale information.

Banks are realising that the calculations only form part of the risk management process. What is more important is a supporting infrastructure and application that can take these calculations and rapidly and accurately produce reports that can be understood by senior management for decision making, regulatory and audit obligations. Risk management today is about putting risk calculations into a proper and practical business environment.

This point is best illustrated by the changing attitude to the use of VaR. In previous years a VaR figure would be calculated by the risk department, often based on inconsistent and unreliable data supplied by front-office staff, and then distributed out to various departments. All too often this single VaR figure would have no business context, no attribution to sources of risk, and would be easily dismissed by departments as long as it was within the limit; adding to the general isolation of risk managers.

The ultimate goal for any risk manager is to become a true partner of the business. Fortunately the risk department is now being asked to work in closer partnership with each department and help them to find ways to reduce their VaR or else find a more appropriate method to measure and manage that risk. 'What-if' analysis is a vital component in this process because it gives the business lines an opportunity to see the impact of any changes in VaR calculations and to make business decisions as a consequence. For example, greater use of 'what-if' scenario analysis may determine the choice of counterparty selected by a front-office trader or determine how much of an overlay hedging strategy to deploy to get to the right level of risk. It is about ensuring that the business lines utilise the risk metrics in their everyday decision making process. This is where new applications need to be.

NEW TECHNOLOGY:

Flash analysis - New web technology and advanced business intelligence tools have made this aspiration a more distinct possibility. For example, a risk application can now enable flash analyses where real-time trade data incrementally overlays the previous day's risk results. This enables traders to analyse risk in real-time and gives risk analysts a good indication of the total risk across all businesses as trading is happening, reacting to up-to-date information.

Incremental Corrections - Today's technology enables incremental corrections to be made on many risk calculations rather than running the whole process again whenever an error is found. The more data that is used, the more room for error exists; this can be incorrect trade feeds, or market data errors. If the calculation results are saved at trade level rather than on an aggregated basis, then a partial re-run can fix what is wrong. Consequently, recalculations that previously took hours now take minutes.

Dynamic navigation - In a risk application where no data is thrown away, users are able to filter and navigate in a truly dynamic way. For example, a risk analyst can isolate and view only USD swap trades with Canadian counterparties.

No new report needs to be created because the all data required is available at trade level and risk results are dynamically calculated according to a user's request.

As-of date aspect - All data is time-stamped so every result that you report on can be reproduced out of the box for audit purposes – the trade, the market data, and the static data required to produce those results. This is important because most legacy systems have to create dedicated databases for specific dates, meaning that retrieving the data needed for end-of-month financial statements became a painstaking and time-consuming task.

The importance of these time-saving advancements cannot be underestimated. A modern risk system frees the risk analyst from the daily production process, instead giving them time to understand and manage their institution's risk profile.

MAKING THIS TECHNOLOGY ACCESSIBLE:

Advances in processor technology mean that high-performance analytics are available to all institutions, not just the preserve of tier one banks. New database technologies allow detailed results to be stored and quickly queried to provide real-time answers to ad-hoc queries. Web technologies allow easy distribution of risk results around the firm. Whilst these individual advances are important in their own right, their combination with business knowledge and systems expertise adds true value to organisations today.

At a time when banks are looking to reduce their total cost of ownership and be certain that any new risk application can be implemented on time and on budget, the fact that a risk application can be largely pre-packaged and pre-configured according to best market practice markedly reduces the cost of customisation and the time of implementation. The cost of ownership can be lowered even more through deployment options such as ASP that enable a solution provider to run and maintain the system on the client's behalf.

At SunGard our new applications have been built using the experience of professionals who understand the genuine pains of risk managers. Technology is the enabler that allows systems to perform faster, to be more transparent and to calculate and distribute results faster and wider. But technology alone is not the solution, just as an isolated VaR number devoid of any business context can serve little purpose. Today's risk applications must be developed within the specific context of the challenges facing risk managers and provide all the tools and workflows to meet both regulatory obligations and internal demands, thereby making risk managers true partners of the business.

To find out more and to see Adaptiv in action call +44 (0)208 081 2779 or visit: www.sungard.com/enterpriserisk

ABOUT SUNGARD'S ADAPTIV

SunGard's Adaptiv provides enterprise-wide credit and market risk management and operations solutions for financial services institutions. Adaptiv assists institutions of varying size and complexity to deploy technology to meet both internal and regulatory requirements for risk management and operational control. Adaptiv helps financial services institutions from the banking, hedge fund, asset management, insurance and corporate sectors with our deep understanding of risk management and operational processes.

For more information, please visit www.sungard.com/enterpriserisk

ABOUT SUNGARD

SunGard is one of the world's leading software and technology services companies. SunGard has more than 20,000 employees and serves 25,000 customers in 70 countries. SunGard provides software and processing solutions for financial services, higher education and the public sector. SunGard also provides disaster recovery services, managed IT services, information availability consulting services and business continuity management software. With annual revenue exceeding $5 billion, SunGard is ranked 435 on the Fortune 500 and is the largest privately held business software and IT services company.

For more information, please visit SunGard at www.sungard.com

www.sungard.com/enterpriserisk

Contact Adaptiv specialists located in:

Americas
Los Angeles +1 818 223 2264
Miami +1 305 395 4724
New York +1 646 445 1180
Toronto +1 416 646 5932

Asia
Beijing + 86 10 8802 0688 (3556)
Hong Kong +852 2913 9532
Seoul +82 2 6000 7080
Shanghai +86 21 3895 4588 (5927)
Singapore +65 65176 152
Sydney +61 2 8224 0000
Taipei +886 919 748 788
Tokyo +813 3237 1583

Europe, Middle East and Africa
Copenhagen +45 33 93 9090
Frankfurt +49 69 707680
London +44 208 081 2779
Paris + 33 1 4471 86 51
Milan +39 02 4544 2001
Stockholm +46 8 454 0000
Zurich +41 44 560 8400
Dubai +971 4 391 1180
Johannesburg +27 11 430 7600