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My risk management blog is now up and running and I encourage everyone to log in to read my previous articles and to engage me and your peers on the topics I cover.

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Once you've signed on you can view previous thought leadership pieces, engage your peers, or ask me questions as it relates to the topics I have covered. As an added bonus you can also view my latest web cast on Stress Testing of Commercial Loan Portfolio's, so sign in today!

Good People Versus Good Risk Methodology

Recently, I attended the Global Association for Risk Professionals (GARP) conference in New York City. On the first day of the conference, Timothy Geitner, the U.S. Treasury Secretary, happened to be delivering his "bailout" speech to the public at 11 a.m., the same time Professor Robert Jarrow was delivering his presentation on economic bubbles. Half way through Professor Jarrow's presentation, the conference organizers decided to stop him, since the bailout speech had far more immediate pertinence. The organizers planned to use the hotel's Internet connection to show Geitner's speech, and had the CNN Web site up and ready to go.

I stepped out of the conference hall and planned to watch it on a smaller television in a common area. As I stood there, one of the GARP personnel said, "This isn't right. The speech is supposed to be on." He went to the laptop and tried to find it, to no avail. I recommended he try CNBC, because they were sure to broadcast the speech. He said, "Here, you do it" and so I did. I typed in "cnbc.com," found the live feed button and clicked on it. And voila, there was the speech.

Immediately, the conference organizer said to me, "Now go and do this for the main conference." So I dutifully entered the conference room and in front of approximately 600 risk experts, proceeded to escort Professor Jarrow off to the side in order to access his computer, type in "cnbc.com" and click on the live feed button. I then astutely used my computer skills to right click the mouse and expand the speech to fill the giant

screens in the hall.

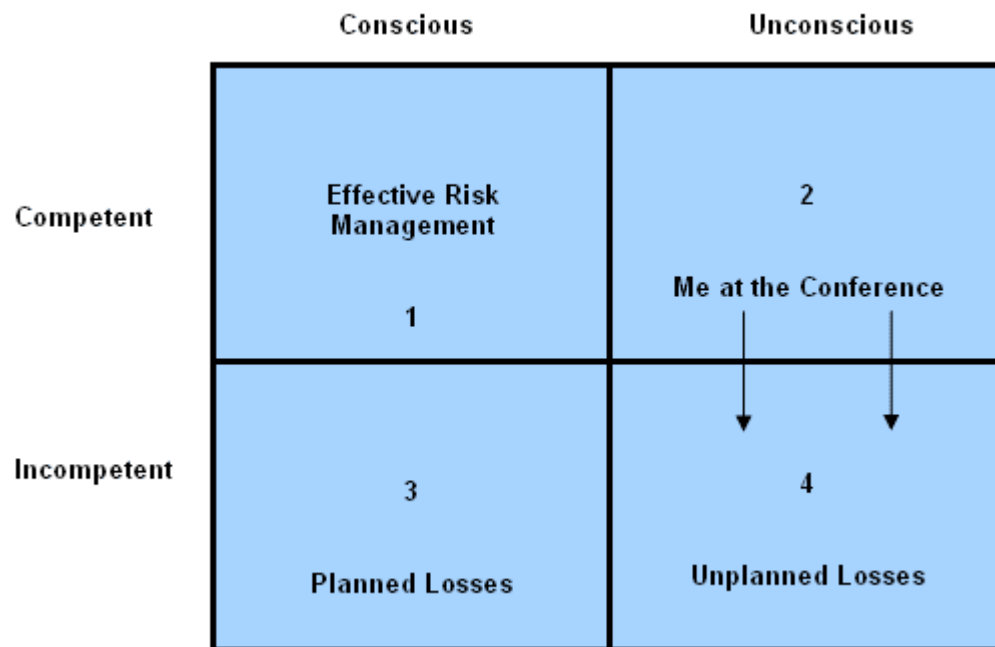
Certainly, not an average day at a conference.

I bring this up because quite often I find good and experienced bank employees who care about the bank and are very effective at dealing with risk. The problem is that solely relying on good people without a solid risk framework and identified (and documented) methodologies leaves the bank with a false sense of security (the opposite is just as true).

As an example, I was in a large financial institution earlier this year discussing its spike in Internet banking fraud. The bank's staff was concerned because the losses had climbed from practically nothing to what they deemed significant in a very short period of time (several months). As we discussed their challenge and how it was being addressed, it became apparent that they had very good and experienced people involved. The problem was that they had not taken the time to build a fraud methodology for Internet banking and were in a reactive mode, fixing issues as they arose. The fixes they were applying were aimed at specific areas, but there was not an understanding of how the fixes overlap or what they were missing. As we all know, a significant number of single applications can be purchased, especially in the area of fraud. But without a plan, we never know what a significant loss number is, and where you have significant exposure.

A Grid to Think About

One of my favorite decision grids appears below. I think this grid captures where we are in risk management and where we want to be. The four labels are Conscious, Unconscious, Competent and Incompetent. Our goal, I believe, is to be consciously competent (good people and good methodology). But we will accept being unconsciously competent (good people and weak or no methodology), because we know we can't plan for everything, and risk management is not the same as risk avoidance. The danger is there can be very little separation between quadrant 2 and quadrant 4.



Effective risk management requires understanding why something went wrong and why something went right. With this knowledge, and a goal of building a methodological approach to risk management, you will have helped your organization manage the risks so that everyone else can focus on the reward.

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