



Put your house in order

For **Andrea Giubboni**, risk management starts at home, with good organisation and communication. Michael Jones went to meet household appliance manufacturer Indesit UK's new finance director as he gets his feet under the table.

Michael Jones: What are the major duties of CFOs in the current environment in forming a risk management strategy and how has this changed in the last six months?

Andrea Giubboni: The role of CFOs in forming a risk management strategy has changed over the past six months, however, this is part of an evolution that has taken place over several years. Back in the eighties, the CFO was a very important player but was obliged to deal mainly with financial issues and, in some cases, even to take risks in order to try and achieve further gains for the operating business.

Today, CFOs of complex organisations have to lead the process of developing a complete management strategy for all types of risk, whether financial, strategic, compliance-related or operational.

When a company is developing its risk management strategy, in my opinion only the CFO has the skills to put in place a proper risk management system. Many senior employees, managers or directors will have a clear understanding of the risks, but when the risks have to be assessed, prioritised and dealt with through a robust internal control system, only CFOs have

the appropriate insight and the wider perspective to achieve this.

Crises and globalisation in the recent past – from the big downturn in financial markets in 1987, followed by the recession of the late eighties, early nineties, through to the rouble default in Russia in 1998 with the effects felt around the world - has shown there is no 'comfort zone' for any entity. And now we have a recession which is likely to be the worse than any of these. Furthermore, the scandals in the last decade involving major companies, Enron in 2001 and Parmalat in 2003, brought about a

need for tighter governance and compliance rules. Risks of “black swans” in this new era have increased dramatically.

Why are strategic risks so different from operational risks and how do you prioritise the different elements – reputational risk, business continuity, fraud and corruption, for example?

There are many managers and consultants who have tried to classify and describe different types of risks. In practise, it is not an easy exercise. There are operational risks which, due to their nature, can result in a change in the approach to strategic risk, and there are strategic risks which can significantly influence operations. For instance, customer change is a major strategic risk, but it can involve operational risks in your supply chain as well as impacting on payment terms. It is a financial risk that can dramatically change your net working capital and, accordingly, your dependence on loans.

In my opinion it is not important to define the classification. More important is the prioritisation that is to be made, based on a risk assessment process. Many elements have to be taken into account as part of a comprehensive risk assessment, where the probability of events and their impact have to be evaluated. Referring back to the first question, this is where CFOs have led the way. You mention different elements when it comes to risks – reputation, fraud and corruption. These types of risks have played a major part in contributing to major crises in very large companies in recent years – crises which have highlighted the significance of these risks, and in many countries has resulted in new compliance and governance legislations.

What kind of grounding in the area of risk management has your experience as a consultant in corporate finance at KPMG and as an auditor given you?

I have to say both have been of paramount importance. The auditor approach is based on risk analysis and I had to consider what the major risks were for every company I audited, in order to address any concerns in the financial statement. I brought this approach with me when I joined Indesit as the head of internal audit.

As an associate consultant, I was able to use my knowledge and experience to better assess financial risks, which, of all risks, are

the most difficult to be technically evaluated. In the seven years I have been working with Indesit, I have had the opportunity to fulfil a variety of roles including head of internal audit and group accounting manager, both of which enhanced my knowledge in regard to compliance and governance rules. It is this background that has rounded my approach to risk and enhanced my ability to prioritise.

How is strategic risk handled at Indesit? What are the key risk areas for your company and how might these differ from other large corporates?

My role is within the UK subsidiary, but to respond to your question, I will need to widen the net and refer first to the group as a whole, and then the subsidiary.

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Strategic risk management is based on risk assessment, and is performed by several key players with a bottom-up approach. In the case of the subsidiary, the managing director involves senior management in the process of assessing risks and developing an appropriate strategy to monitor these risks, particularly regarding budgets and long term plans. At group level, it is the CEO and the group CFO who mainly perform the risk assessment and collate all relevant information from each of the subsidiaries.

Thanks to strong governance rules, which have been further enhanced in recent years, boards of directors (comprising of independent and non independent members) have been increasingly involved in this process. They operate through the audit committee – a separate board which operates within the company through an internal audit department. The audit committee bases its audit program on risk assessment and handles strategic risks on a day-by-day basis. A reporting system monitors these risks and feeds this through as supporting material for management decisions. Now, in the midst of a recession, it is more vital than ever to monitor all strategic risks, as a lack in monitoring could be disruptive.

Other major issues we monitor include competitors’ reactions to the crisis, customer changes as the crisis reshapes the market, and consumer demand, which can change significantly, particularly for durables. These are all risks that have to be monitored, in order to put in place a proper strategy in terms of market approach. Our commercial and marketing departments have a strong reporting system which is used to analyse a significant amount of information to consider those risks. The way risk is handled at Indesit Company is much in line with best practice for most large corporates.

How closely do you work with your chief risk department at Indesit and where do the delineations of responsibility lie?

Indesit does not have a specific risk department as such. Risk assessment is a process that is handled at senior management level and then cascaded within the organisation to the relevant departments. In my opinion risk management is about organisation and sensitivity to risks and not focused on a single individual or department. For instance, in the case of financial risks, they are cascaded among the organisation into all the departments. Credit risk falls mainly under my responsibility as head of finance and administration of the UK subsidiary, as well as under the responsibility of the UK commercial director. Foreign currency risk is handled by the group treasurer.

Despite the different roles, credit and currency risks are handled jointly, with decisions being taken by myself, the managing director, the group treasurer and the commercial director, on how to deal with the risk; for example, the use of derivatives for currency risks, sale without recourse or insurance for credit risk. And the degree of confidence is not a result of another department providing us with guidelines, but more a result of good organisation and a high level of inter-departmental communication. It goes without saying that communication between departments is communication between people – the higher the level of confidence



between them, the higher the chance of managing risk successfully.

How much time should the CFO spend in their day setting the risk strategy and how can CFOs avoid over-managing risk?

Risk management is a matter of the quality of the risk assessment process and the level of organisation, rather than the amount of time spent on it. A good CFO could spend just 10% of his or her time and manage risk very effectively, but could just as easily spend 80% of time, with insufficient results. Regardless of how much time is spent, in the current market, this has to increase. I do not see any harm in over-managing risks at this particular moment in time. During a recession, the more time spent on risk management the better, and had more CFOs and CEOs done this in the past perhaps we would not have seen so many big companies going bust. To a certain extent, even though it is impossible to blame anyone for the recession, we can certainly say that understatement of risks – think sub-prime, housing markets, liquidity – has contributed to making the recession worse.

How can the CFO help to turn strategic risk into strategic advantage?

I can only repeat a leitmotif: good organisation. A CFO has to work to encourage cooperation between departments. This is not an academic answer – I cannot offer any mathematical model to turn risks into opportunities, but, in the real world this is the way to go. For example, as the credit crunch squeezes our customers, in my role presumably I should recommend that we immediately cut credit limits for our customers. But, I have to work with the

commercial director to understand if, in doing such a thing, I am actually increasing rather than decreasing the risk, as we could very well be accelerating our customers' own crises.

To understand how to put in place a strategy, I have to closely liaise with the commercial department and share any ideas and decisions with them. Relationships should be based on complete reliance and trustworthiness. Only in this way can we take the opportunity not only to reduce the risk, but also take advantage of a reshape in the market, where a customer could increase their market share as other players exit the market.

How can using a strategic scorecard as a tool help you to identify strategic risks?

Strategic scorecards can be very useful in providing step-by-step guidelines on how to align operational activities to strategic objectives. As a type of handbook, they can also help to better understand some risks. But a scorecard is a tool, not a magic wand. Again, people, the organisation, cooperation, the culture and sensitivity are what make a difference. A great strategic scorecard implemented in an environment where nobody cares about risks is utterly pointless. To build up a strategic scorecard is a matter of time and money and does not take long. To build up a culture of sensitivity to risk is a matter of people and takes a very long time.

The liquidity crisis has brought with it a call for tighter regulation and governance. Is business in danger of allowing compliance to take precedence over growth?

In short, no; compliance is the way to survive, not to curb growth. In recent

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years we saw a massive number of companies go bust due to a lack of focus on compliance. Indesit Company is listed, so compliance is a must and I have spent massive amounts of time in previous roles on it. Just a year ago I was responsible for implementing a control system to be compliant with new legislation in Italy which is the Italian version of Sarbanes-Oxley act in the US. But I believe strongly that it is not just a legal obligation but a matter of protecting the company, its stakeholders, ourselves, and acting according to shared rules that enable me to be proud to work in a company with a great reputation in the market.

How can the CFO work to re-shape the treasury functions in this environment? Is this a requirement for Indesit?

At this moment in time, treasury is probably the most critical area for a company. In our company it is a centralised department dealing with significant financial risks – interest rates, currency and liquidity. Because Indesit has multi-currency transactions, both external and within the company, it is of paramount importance to have a good understanding of this kind of risk. ■

Andrea Giubboni

Andrea Giubboni took on the role of finance director at Indesit Company UK in March 2008, in a move from his previous position as group accounting manager. Giubboni has been at Indesit for seven years, having previously held roles at KPMG as a consultant in corporate finance and as an auditor in the audit firm.

