Dynamic Risk Management: What Is It and How Can Banks Use It?

How often does your organization think about risk? Chances are it's top of mind for your leadership team, employees, and customers. But do you use dynamic risk management? That's a question more banks should ask.

After all, the days of one-time or annual risk assessments are mostly over. Compliance guidelines and regulations are evolving to meet the needs of existing and emerging risks. For example, cybersecurity threats aren't new, but bad actors' tactics are getting more robust and technologically advanced with the rise of ransomware and artificial intelligence-enabled phishing attacks.

So, how can banks create a more proactive and flexible risk framework? What opportunities and obstacles may they face as they implement dynamic risk management? Let's dive into that and more.

Understanding Dynamic Risk Management
Dynamic risk management, or DRM, is a risk approach where banks actively identify, assess, and mitigate risks in real time. While risk assessments are used in DRM, they are not merely formalities put in place to appease auditors. They are updated as risk conditions, both internal and external, change. For example, a DRM approach would consider the impact of staffing changes or a natural disaster on an institution's operational risk, and updates would be made accordingly.

Key Differences Between Traditional and Dynamic Risk Management
Traditional risk management, or static risk management, relies on an existing framework and scheduled periodic assessments. For example, a bank schedules its fraud risk assessment for one month, but the Office of the Comptroller of the Currency (OCC) issues new fraud risk management guidance for all OCC-supervised banks the following month. If the bank uses a traditional approach to manage fraud risk, it will wait until the next risk assessment to make updates.

Unlike traditional risk management, DRM considers the evolving nature of risks. If traditional risk management is a stagnant body of water, DRM is like a river, constantly flowing and adapting to changes in the landscape. Using the previous example, a dynamic risk-focused bank would promptly adapt to meet the guidelines.

Exploring the Benefits of Dynamic Risk Management

DRM offers financial institutions a plethora of benefits, including:

- **Proactive risk mitigation.** Rather than rely on past risk assessments and timelines, all departments are encouraged to continually monitor updates specific to their area, uncover new risks, and share their findings with other teams, improving the overall operational risk management of the organization and reducing the chance of regulatory penalties, among other benefits.
- **Regulatory compliance.** Banks can maintain compliance and avoid falling behind industry standards by adapting their assessments and strategies based on current or upcoming regulations.
- **Improved Operational Resilience.** Operational risk is a significant concern among banks as it touches nearly every department and outside relationships with vendors and partners. Organizations can adjust their controls and processes with DRM to adapt and thrive in fast-moving environments.
- **Enhanced Risk Culture.** DRM is contagious within an organization. If one department actively pursues other teams for updates and change, the entire culture must level up and adjust its strategies accordingly.

How to Implement DRM at Your Financial Institution

While DRM's benefits are worth the effort, there are some steps every organization should take to maximize their efforts:

1. **Assess your current framework.** Review your current risk management strategy to identify what's working and the gaps and areas where a DRM approach is a high priority.
2. **Engage stakeholders.** Involve multiple parties and departments, including IT, marketing, and operations, to discuss potential risks and ensure a comprehensive understanding of your institution's operations.
3. **Establish a continuous monitoring system.** Develop a system to track key risk indicators (KRIs), which identify and predict potential risks, and key performance indicators (KPIs), which measure your organization's success based on your identified goals and objectives.
4. **Prioritize risk assessment updates**. Dynamic risk assessments should be updated as needed based on changes in regulations, products, processes, and organizational risk tolerance.
5. **Enhance your internal controls.** Control self-assessments, audits, and testing offer a wealth of insights. Use them to create new internal controls or improve existing ones.
6. **Evaluate—and reevaluate—your approach.** You can't set and forget a DRM strategy. Modify your approach based on learnings, regulatory updates, and new insights.

How to Build a DRM Culture

Making the most of a DRM strategy is more than completing a set of steps—it's about improving your organization's risk management culture.

To do that, you need everyone, including your team members, to be educated and actively embrace this new perspective. Provide training on new or existing technology and systems. Encourage employees to communicate their concerns and any signs of risks. Remember, a commitment to clear and open communication starts from the top down.

It's also important to note that while DRM is arguably more suited for the evolving nature of risks, there are times when a traditional risk management approach may be necessary. Suppose your bank has limited resources, systems, and human capital to manage an area actively, or perhaps the area is low-risk. In those cases, traditional risk management might work. Communicate this information to your teams so everyone is on the same page.

As you revisit your organization's risk management approach, consider which areas would benefit from DRM implementation and the time and resources it will take to implement this approach successfully. You may find that some systems are working, but others need to be addressed now or soon. Regardless of the type of risk you're anticipating or actively mitigating, having a strong dynamic risk management approach will enable you to tackle the challenges and see the opportunities risk presents better.