# Dynamic Risk Assessment (DRA)

**Private Equity**

2018

kpmg.com

# Private equity

The global private equity sector is constantly facing new demands and evolving challenges. The fundraising environment is proving especially tough, as some investors adopt a more cautious approach to the asset class as a result of decreased returns during the global financial crisis. Investors are now seeking improved returns for lower fees, and greater transparency.

Although the postcrisis economic recovery has been slow in most developed markets, the private equity sector appears in a state of cautious optimism as banking markets continue to recover. However, high prices for quality assets and a likely low-growth economic environment in the medium term in most developed markets will require general partners to work harder and smarter to add value to their portfolios. This will require better operational understanding of targets preacquisition and likely more value-enhancing intervention during ownership.

As firms look for ways to address the uncertainties of these changing markets, they are under pressure to be more agile and efficient, which introduces more risk.

Leadership needs to understand and better predict trends; the correct portfolio of products, services, and markets will need to be identified; and—based on this information—investments will need to be concentrated on the opportunities and threats that best align with the growth and portfolio ambitions of the organization.

Risk Management 1.0—the traditional approach—does a good job of generating defensive responses to risks or threats and developing governance disciplines to safeguard stakeholders' interests. But typically, it doesn't do a great job of identifying opportunities or "mega trends" and formulating responses to them. Responsibilities are stuck in the defensive mind-set. The risk organization is seen as responsible for covering the downside of risk. Auditors, legal counsel, and risk committees are set up as the "no" guys. But who is responsible for the upside of risk?

That's why KPMG developed a new approach designed to help organizations transform risk into value. Dynamic Risk Assessment (DRA) is designed to focus on both upside and downside of risk. We focus in on both sides of the coin, helping clients analyze observable "mega trends" to find the opportunities in risk that allow them to gain a competitive edge.

# What makes DRA unique

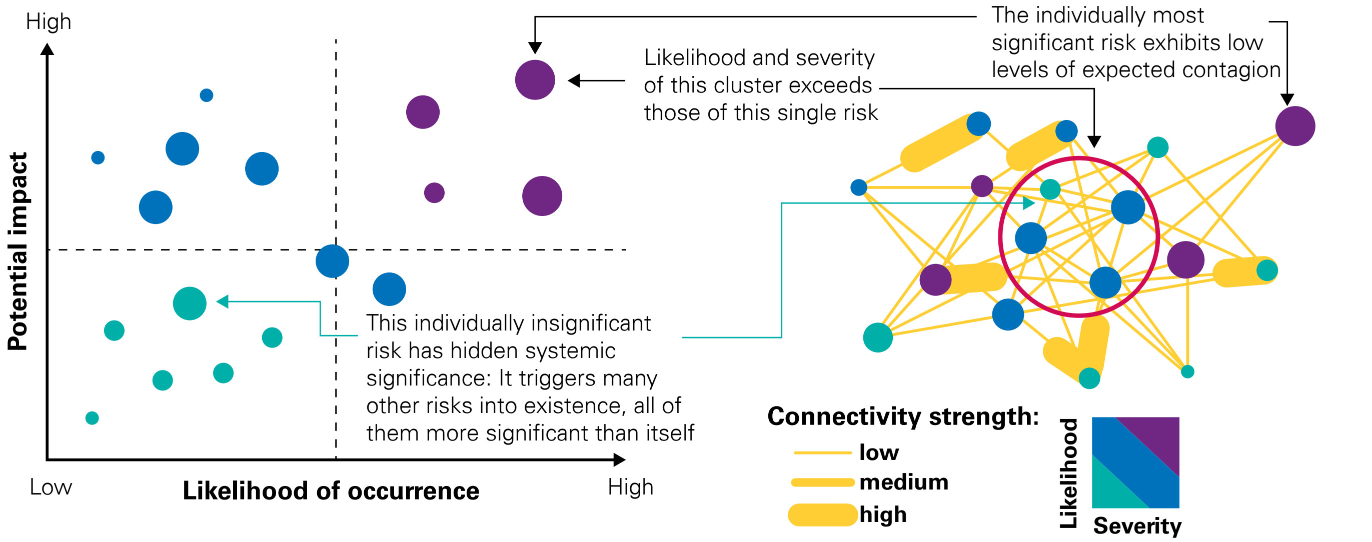
**DRA is a proprietary methodology developed by KPMG to help bring a better understanding of the risks organizations face in today's complex world. DRA takes an unprecedented approach to gaining insights into clients' risk environments by pinpointing central risks and shedding new light on the risk mitigation strategies.**

In today's highly interconnected and volatile world, dominated by new technology and emerging business models, the past is no longer a reliable guide to the future. Past data is a poor fit for the future as the forces and trends that shape our future have increasingly not manifested themselves before. Moreover, risks combine. They spill over into each other—they don't manifest neatly in isolation—and we no longer have the luxury of dealing with risks discretely.

There is a need to advance beyond historical risk analyses comprising two-dimensional depictions of expected probability and severity, and consider a third, and indeed a fourth dimension: velocity and contagion. This, together with the consideration of global trends that are shaping our world, is what DRA encompasses.

# DRA vs. Traditional Risk Assessment

**Traditional, two dimensional risk map** | **Inter-connected view**

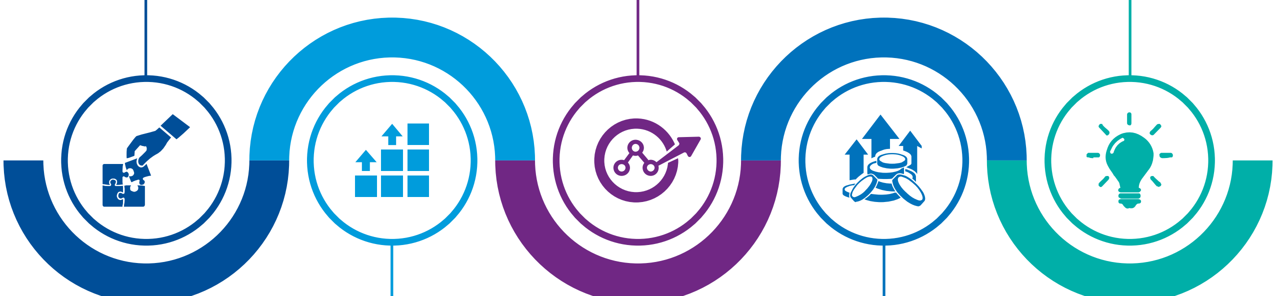



Certain risks connect more to each other than all other risks in the network, forming clusters.

DRA applies graph theory, the science of expert elicitation, actuarial modeling, sophisticated mathematics and financial mathematical algorithms, advanced data & analytics (D&A) and accounting science to assessments from experienced risk and non-risk frontline and back-office individuals within the business. This is done in a KPMG proprietary (and patent pending) methodology to identify, connect and visualize risk in four dimensions.

**The DRA methodology combines qualitative and quantitative data to help identify:**

- Your greatest systemic risk exposures, combinations and risk clusters to inform a risk mitigation plan
- How risks will impact each other in the network and how they behave in a dynamic manner over time
- A framework to revisit your risk tolerance and overall risk management strategy



- The impact of "mega trends" and their effects on your business
- Insights that may help you improve mitigation of systemically critical risks, to aid you in developing an investment strategy to counter those weaknesses

# The DRA process

Typically, the end-to-end DRA process takes six to eight weeks, with the key steps outlined below:

**1. Landscape articulation**

KPMG works with key stakeholders to identify the key risks facing the organization.

**2. DRA Survey**

Key stakeholders complete an online survey, for the collection of data on the characteristics of the risks facing the organization.

The survey requires approx. 45 min to complete.

**3. KPMG Analysis**

KPMG applies advanced network theory to the survey responses to identify the organization's interconnected risks and opportunity network, and it's dynamics.

**4. Follow Up Workshop**

KPMG discuss the findings with the key stakeholders.

**5. KPMG Deliver Dynamic Risk Assessment Report**

The DRA report is discussed with the client to form part of strategic planning and ongoing monitoring.

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