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# Managing Macroeconomic Uncertainty in a Post-Recession World

## Executive Overview

Financial services leaders must manage the uncertainty of proposed governmental tax changes and financial regulations by introducing agility and strategic what-if scenarios to their project planning.

These uncertain macroeconomic factors require *agility* - the ability to pick good projects and execute them effectively and efficiently, as well as to develop methods for going beyond the reactionary and toward strategic decision-making.

## Introduction

The banking world has endured its share of challenges over the last few years. The aftermath of the financial crisis prompted the creation of one of the most comprehensive sets of new regulations in the last 70 years.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which passed on July 21, 2010, is unprecedented in both magnitude and the level of transparency that will be required. Its 2,300 pages contain at least 400 separate rulemakings and will impact every sector of the financial services industry<sup>1</sup>. Basel III, which requires banks to meet certain capital requirements and maintain proper leverage ratios, also threatens the financial industry landscape.

While these new rules may reduce systemic risks, they are also driving up the costs of financial institutions. New requirements for larger capital cushions could reduce banks' profitability by as much as one-third, according to one report by *The Economist*<sup>2</sup>, while pushing up borrowing costs for consumers and businesses. Financial organizations that can meet compliance requirements while simultaneously providing their customers with new innovative products and services will flourish in this environment.

In 2012, many institutions took a wait-and-see attitude about these regulations because the implementation procedures had not been ironed out. More than two-thirds (69 percent) of banking industry executives surveyed by KPMG LLC<sup>3</sup> in September 2012 viewed regulatory and legislative pressures as the greatest barrier to growth over the next year. Still, most respondents say they are generally optimistic about their bank's revenue and growth prospects.

But 2013 looks to be a year of regulation implementation - at least for U.S. banks, industry-watchers say, as much of the regulatory uncertainty has been resolved and industry leaders take a fresh look at their organizational structures and capabilities, according to Deloitte LLP<sup>4</sup>.

A healthy financial industry is critical to economic vibrancy, providing the essential credit, capital, and liquidity that supports growth and profit. The financial services industry stands at the crossroad of new regulations and competitive resurgence. Agility will be the key to success. Financial leaders must reach beyond the reactionary and toward strategic decision-making.

Deloitte points to several independent macroeconomic issues that senior-level financial services leaders must consider and act upon in 2013.

## 1. From Analysis to Action

What may be different for banks in the coming year is the movement from analysis to action. In the aftermath of the financial crisis, many U.S. bankers put a hold on making changes to organizational structure and operational processes. Most were waiting for the new regulations to crystallize to a point where they could more clearly understand the ramifications to their own business operations. In 2013, banks are likely to begin a fresh and long-term strategic plan. But Deloitte cautions that it's one thing to simply *say* that focus has returned. Without execution of these initiatives, these efforts may result in "nothing more than window-dressing."

## 2. Compliance Issues and Opportunities

As the implications of the Dodd-Frank Act and its focus on bank safety and soundness become more clear, financial institutions are expected to start making compliance as a "business as usual" activity, rather than a series of isolated regulatory responses. Compliance will become part of the everyday larger effort to improve business and operational performance -- initiatives that have been ongoing for decades. Transparency will also become a daily operational imperative.

The combination of enforcement actions coming from Dodd-Frank and the operationalizing of compliance should be viewed by banks as an opportunity to redesign processes and reduce the fire drill aspects of regulatory compliance, according to Deloitte.

## 3. Risk Management

Evolving regulation and changing marketplace dynamics have heightened the need for companies to implement a strong internal risk framework. When asked to identify any existing challenges preventing the adoption of a formal risk policy, 40 percent of KPMG survey respondents believe that process integration and operational efficiency pose significant obstacles.

Financial institutions must continue to address weaknesses in their risk management capabilities in light of regulations and market realities. This is being driven, according to Deloitte, by ongoing regulatory initiatives regarding stress testing and the development of recover and resolution plans, or "living wills."

Leaders must take the appropriate steps to embed and operationalize a more risk-intelligent culture throughout the organization, Deloitte says.

## 4. Mergers and Divestitures

The impact of regulation and resulting repositioning may drive a new wave of mergers and divestitures. Many financial institutions have acquired assets and even entire businesses over the last 10 years, and now those same purchasers are re-evaluating the current business value of those acquisitions. Those considered non-core will be cast off, which may reshape the competitive landscape.

Institutions that have a clear strategy and a strong balance sheet in the midst of these acquisitions and divestitures, will gain a competitive advantage.

## A Powerful Partner

Amid all of the uncertainties is the growing realization that what's worked in the past may not work in the future, leading many executives to closely examine how their business is organized, how it creates products and services, how it manages projects and measures success, and how it grows its top line and builds revenue. Financial institutions must develop methods for going beyond the reactionary and toward strategic decision-making.

At the business level, achieving those objectives will require enterprise agility, team productivity, portfolio predictability and overall project management efficiency. Financial institutions must introduce strategic what-if scenarios into their project planning, pick good projects and execute them effectively and efficiently. A Project Portfolio Management system (PPM) for globally prioritizing, planning, managing, and executing projects, programs and portfolios is one powerful tool that can provide institutions with vital information that drives the perfect alignment of project strategy, execution and results.

## Providing Transparency

A Project Portfolio Management system connects all the different people and processes in a way that delivers value, the organization gains business transparency, profitability and project success. The financial institution that successfully implements PPM will be aligned around corporate strategic objectives, and will effectively cascade communication to its people, whether the communication is about shifts in strategy, project performance or resource capacity. Staff will work in a proactive mode, managing everything that directly impacts the performance and probability of success of the projects under way.

## Aligning Business Strategy

A Project Portfolio Management system allows financial institutions to clearly identify its strategic objectives and evaluate how well each investment supports those objectives. The system must support the comparison of multiple portfolio scenarios, and have the ability to identify the “waterline,” based on metrics such as funding limits or headcount available, and evaluate the many alternate scenarios against the waterline. The right PPM system can also analyze all the institution's constraints and key performance indicators (KPI) to propose multiple viable scenarios for consideration. The system should also provide a metric and KPI-driven means of comparing, contrasting and deciding which projects to approve, which ones to postpone, and which ones to drop.

## Monitoring Execution and Regulatory Compliance

Financial organizations that can meet compliance requirements while simultaneously providing their customers with new innovative products and services will flourish in an uncertain economic environment.<sup>5</sup> Unfortunately, few institutions in this industry currently have the project management maturity to meet project goals with any level of consistency.

A Project Portfolio Management system allows financial institutions to monitor projects' status and progress, as well as ensure governance. Based on the business systems that are integrated to share information, the PPM system ensures processes are followed as designed.

Failure to deal with troubled projects early has the biggest impact on implementing regulatory initiatives, which are of central importance for financial services executives. Missing these targets can cause a bank to lose its license and permanently damage its reputation among investors.

Consequently, when these projects flounder, organizations have no choice but to funnel resources away from other projects to bring them back in line—even if it means pulling people from more successful endeavors that offer better returns. This is where organizations with mature project portfolio management capabilities have a competitive advantage. These high-performing organizations can more confidently deliver projects on time and on budget, so they are less burdened by regulatory demands.

### Balancing Risk & Opportunities

A Project Portfolio Management system allows the organization to clearly document their projects' risks and anticipated rewards. Risks and rewards provide the basis for calculating many of the KPIs that institutions depend on to make the right decisions. The basis of estimates must also be captured so that project execution teams can later make use of this information to create mitigation plans and create more accurate estimates in cases where the risk events are triggered.

Using Project Portfolio Management technology can also identify opportunities for turning portfolios into strategic assets that produce measurable benefits. The portfolio can then be viewed as an investment that can be advanced in different directions as the fundamentals behind a strategy change.

### Conclusion

Banking executives maintain a cautious optimism for the near-term business outlook, expecting modest improvements in revenue, the economy, and hiring in 2013 but remain guarded longer term, not seeing a complete economic recovery until 2014. As a result, many banking executives are focusing their efforts on strategies to increase operational efficiencies and reduce costs. What's more is that an economic uncertainty due to new regulations requires financial institutions to become more agile and to move beyond reactionary and towards strategic decision-making.

A Project Portfolio Management solution can help financial institutions become more agile and to execute on strategy, which will drive down costs, minimize risk and deliver results to key stakeholders.

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