Chief Risk Officer Survey

Industry perspective:
Industrial Manufacturing

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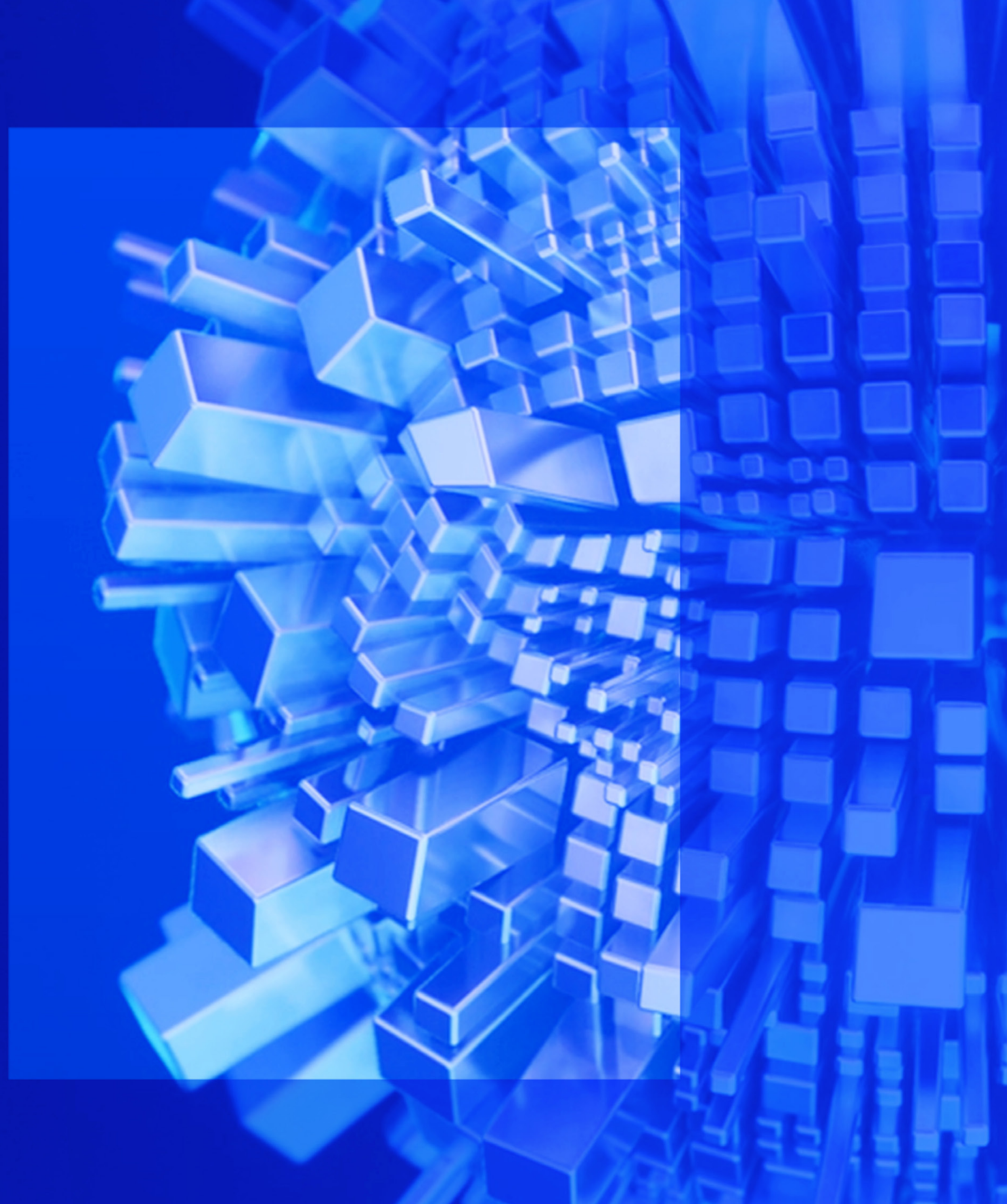

Introduction

Risk management has become a critical focus for Industrial Manufacturing (IM) companies as they navigate an increasingly complex and uncertain business landscape.

With challenges ranging from regulatory changes and supply chain disruptions to geopolitical risks and compliance pressures, IM companies are seeking strategies to enhance their risk management efforts and ensure the resilience of their organizations.

To gain better insights into the risk-management issues facing businesses today, KPMG conducted its 2023 Chief Risk Officer Survey. The survey results indicate how companies are addressing current and future risk challenges, opportunities, and priorities across five intersecting drivers of risk transformation: de-risking, growth or strategic change, compliance risk, effectiveness and efficiency, and cost takeout (Exhibit 1). This report digs deeper into our overall survey to identify the challenges specifically facing the IM sector, reflecting data from 41 U.S. IM risk executives who responded, combined with analysis and perspectives of KPMG Risk Advisory partners.

Our survey found that IM CROs are focusing on business resiliency, regulatory compliance, and supply chain disruptions as their chief risk-management issues. IM CROs indicated a moderate to high level of preparedness for risks related to environmental, social, and governance (ESG); regulatory changes; and business resiliency. However, they feel least prepared to manage supply chain disruptions or logistical issues.

To enhance their risk-management strategies, IM CROs plan to align their risk strategy with business objectives and improve risk identification and assessment mechanisms. They also seek greater support from senior management in terms of overall alignment and budget allocation.

With respect to regulatory compliance activities, respondents said that IM companies face heightened expectations from such stakeholders as regulators, government agencies, and investors. To address this pressure, they plan to supplement their risk management teams and focus on employee training and leadership engagement.

IM CROs are focusing on technological-driven risk management, such as artificial intelligence (AI) and machine learning (ML), and see digital tools and solutions as critical to optimizing risk management capabilities. Meanwhile, to curb costs and increase efficiencies, IM CROs are considering outsourcing activities such as business continuity and disaster recovery planning, as well as compliance monitoring and regulatory reporting.

Overall, this report provides valuable insights into the risk management efforts within the IM sector, highlighting the challenges, strategies, and priorities for risk management in the coming years.

Exhibit 1. Five intersecting drivers

De-risking: Organizations' effort to reduce risk exposure and hedge against expected market conditions

Growth or strategic change: Organizations' organic or inorganic growth; change in products, services, delivery channels; and/or other large-scale strategic initiatives

Compliance risk: New or emerging regulatory requirements, non-compliances with existing requirements, or need to enhance the relationship with oversight authorities

Effectiveness and efficiency: Increase the quality, consistency, extensibility, and confidence in risk management requirements and outputs

Cost takeout: Reduce the overall costs associated with the governance, maintenance, oversight, and execution of risk requirements and practices

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De-risking

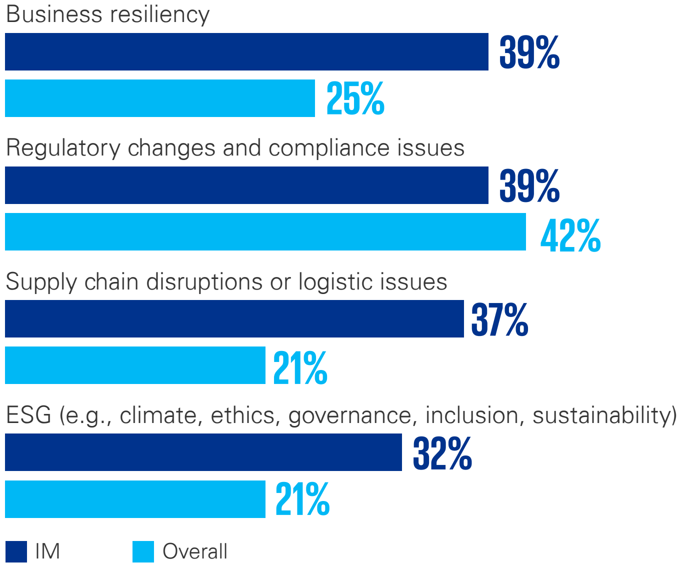
Organizations' effort to reduce risk exposure and hedge against expected market conditions

Key findings

- Looking at the chief risk challenges they expect to face over the next few years, IM companies are putting equal emphasis (39 percent of respondents) on business resiliency, and regulatory changes and compliance issues. Those areas were followed closely by supply chain disruptions or logistic issues (37 percent) (Exhibit 2).
- Since many IM companies have a global footprint, it follows that regulatory challenges are top of mind, particularly in Europe, where business regulations tend to be stronger. Similarly, IM companies have also had to address supply chain disruptions in the past several years, due to geopolitical unrest and the pandemic, and chief risk officers still see a need to prioritize business resiliency.
- Readiness to respond to risks is another key measure of the soundness of an organization's risk management strategies. Most IM respondents indicated being well to very well prepared to tackle top challenges related to ESG (85 percent), regulatory changes (75 percent), and business resiliency (69 percent), exhibiting resilience in navigating market fluctuations and compliance issues.
- In addition, all respondents said they were well or very well prepared for cyber threats (100 percent), litigation or legal disputes (100 percent), and export controls and sanctions (100 percent), representing organizations' strong investment in IT and legal protections.
- On the other hand, respondents said they were least prepared to manage geopolitical risks (25 percent), followed by third-party risks (20 percent), suggesting concerns about political instability abroad and uncertain economic conditions domestically.

Exhibit 2. Top challenges your organization will face within the next 2–5 years

Q. What do you think are the biggest challenges your organization will face within the next 2-5 years?



Recommendations

- Build resilience into the risk management framework that will help ensure that first line risk processes and controls stand firm in the event of disruption.
- To hedge against unusual risks, allocate more "time, talent, and treasure" to improving understanding of and planning for less likely, but high-impact risks.
- Because some risks simply cannot be well planned for, it is critical to look at business continuity and crisis planning and management through a new lens. Resilience plans must go beyond documenting how to get core platforms back up and running and incorporate robust processes to minimize disruption.
- While it might require significant changes to the risk function, do not shortcut potential issues with regulators or other stakeholders and be sure to appropriately assess potential risk impacts.

"Given the continual focus on cost management across industrial manufacturing, today's Risk leaders are challenged to take a broader and deeper view of potential risks, while keeping the cost of their function contained. These seemingly contradictory objectives can be best accomplished by thoughtfully leveraging digital tools and technologies, such as Generative AI, in the exploration and identification of risks, thus enabling their human capital to spend their valuable time on risk mitigation and containment."

— Claudia Saran, Principal, U.S. Sector Leader, Industrial Manufacturing

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Growth and strategic change

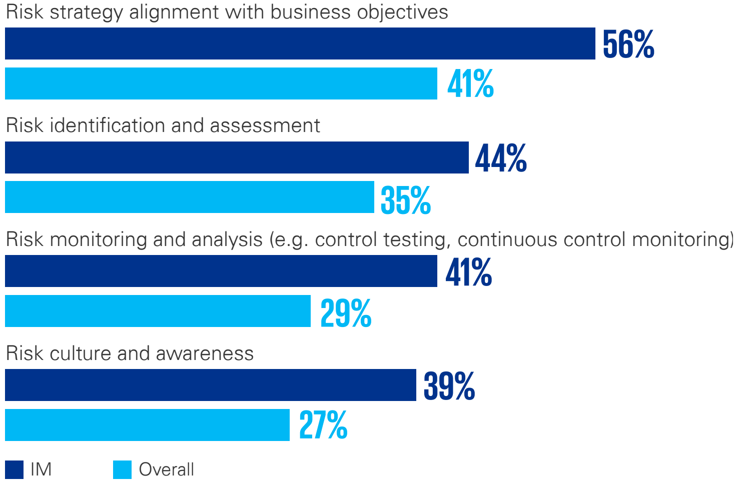
Organizations' organic or inorganic growth; change in products, services, delivery channels; and/or other large-scale strategic initiatives

Key findings

- As IM companies face a changing and uncertain risk landscape, over the next two years they will be looking to improve certain areas of their risk-management strategy. A majority of respondents (56 percent) said they are planning to prioritize enhancing risk strategy alignment with business objectives, demonstrating the growing emphasis on integrating risk management with organizational goals. For 44 percent of respondents, improving risk identification and assessment mechanisms is the top priority, indicating a growing recognition among businesses to accurately identify and assess potential threats (Exhibit 3).
- Successfully syncing risk management with business strategy requires C-suite buy-in. More than three-quarters affirmed they have a high level of support from their C-suite. And of the respondents who received a moderate level of support, more than 80 percent want greater support from senior management in terms of overall alignment of the risk management business strategy and sufficient budget.
- CROs are increasingly expected to align their top risk objectives with the organization's business goals. We asked respondents what their top strategies were to achieve that alignment. Fifty-six percent said providing training and resources for employees on risk management and corporate strategy alignment was an essential aspect of an enterprise-wide strategy to align their risk objectives with the strategic goals. The results suggest that IM CROs recognized that well-trained employees are better equipped to manage risks more effectively as well as being more effective in the role of the first line of defense in risk management.
- The other top strategy, cited by 54 percent of respondents, was analyzing risk mitigation successes and updating the corporate strategy accordingly. This indicates the need for continuous improvement and adaptability in response to evolving risk environments

Exhibit 3. Top risk management activities that will be enhanced in the next two years

Q. Which risk management framework components and activities within your risk organization will be enhanced/strengthened the most over the next two years?



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Recommendations

- To make progress on strategic enterprise risk management, incorporating shifting risks and strategic changes into the risk framework should be a key goal.
- Helping the organization make decisions and investments where there is greater certainty of upside and reduced severity of downside will enhance the risk function's value to the enterprise. As such, the risk framework should be designed to surface and disseminate information that business decision-makers should know but do not, provide informed perspectives on "what if" scenarios," and tap the brakes when appropriate.
- It is also important to know when to veer away from the playbook. Executing the risk framework blindly, without asking strategic, forward-looking questions can cause risk leaders to miss important opportunities. Prioritize compliance risks as integral with strategic business priorities and funding. Build compliance assessments and controls upfront and ongoing, as a core element to business strategy.

04

Compliance risk

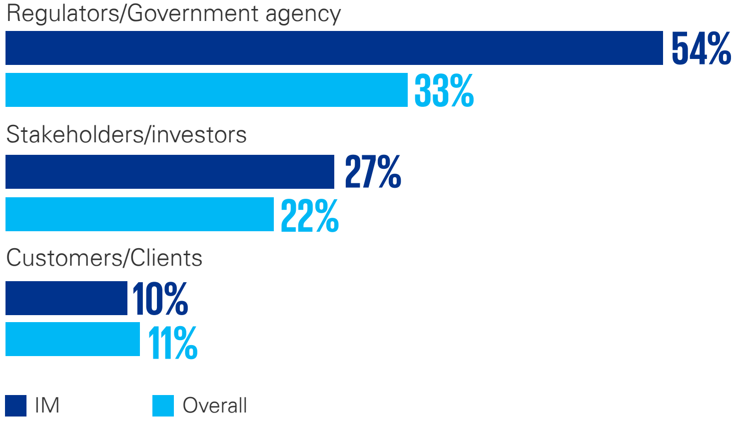
New or emerging regulatory requirements, non-compliance with existing requirements, or need to enhance the relationship with oversight authorities

Key findings

- IM companies are coming under increasing scrutiny from stakeholders about their overall regulatory compliance activities. Among respondents, 54 percent said that external entities, such as regulators and government agencies, followed by investors (27 percent) impose the highest pressure and have maximum expectations around their organization's regulatory risk compliance record (Exhibit 4).
- Moreover, 63 percent of the respondents are concerned or very concerned about compliance risks due to not implementing technologically supported compliance tools.
- Given this increasing scrutiny and heightened pressure, it follows that 61 percent of respondents said they plan to supplement their existing risk management teams in spearheading regulatory compliance and change management initiatives to minimize risks associated with non-compliance.

Exhibit 4. Sources of pressure and heightened expectations on risk functions

Q. As it relates to risk management, from which of the following stakeholders are you getting the most pressure, interest, and/or heightened expectations?



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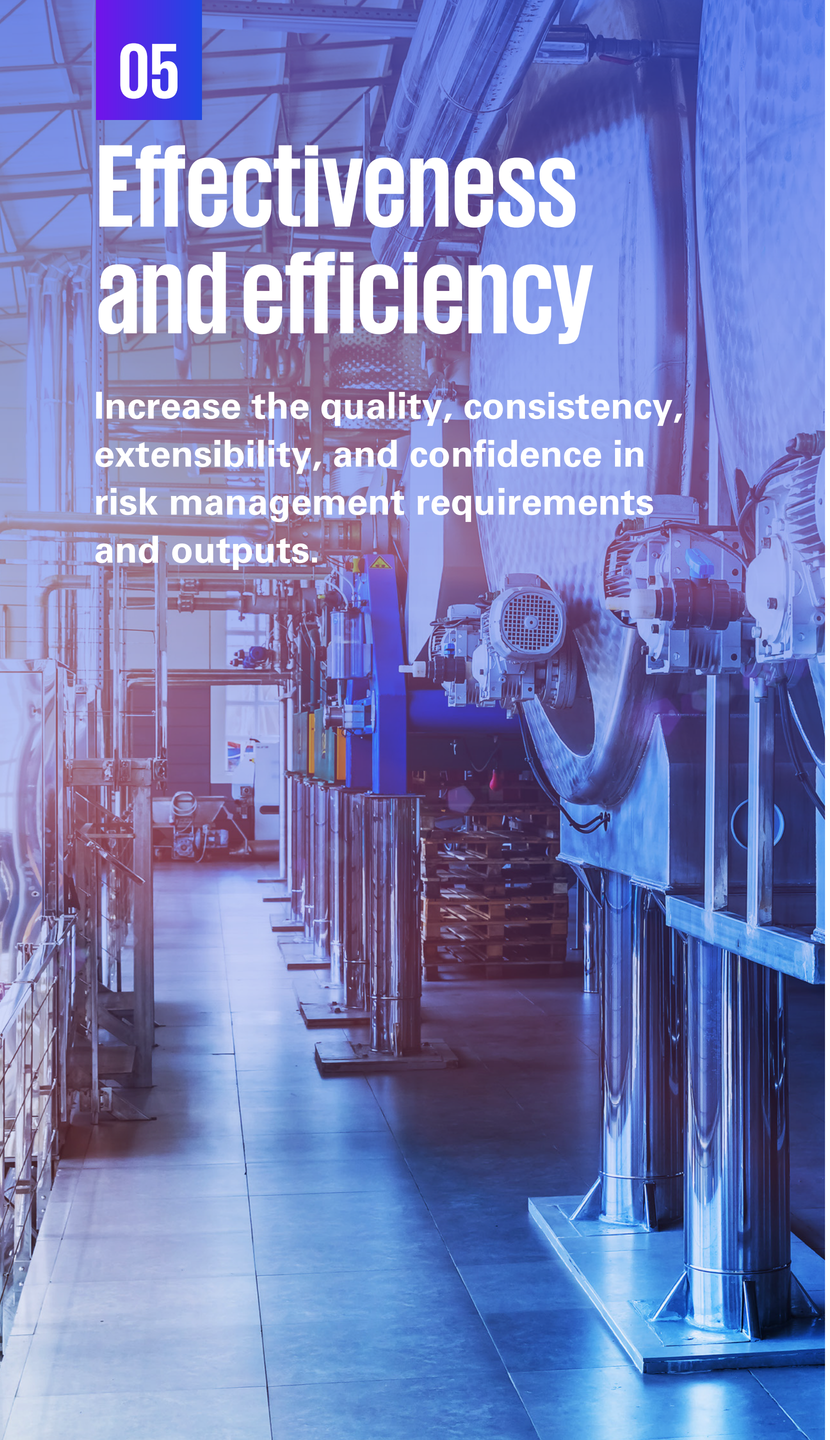
Recommendations

- While it might require significant changes to the risk function, do not shortcut potential issues with regulators or other stakeholders and be sure to appropriately assess potential risk impacts. Invest accordingly to help ensure small problems do not become big.
- Prioritize compliance risks as integral with strategic business priorities and funding. Build compliance assessments and controls up front and make them ongoing, as a core element to business strategy.
- Ensure you understand the principles that regulators are looking to see the organization embrace, in addition to the formal regulatory obligations, and align the risk strategy to meet those objectives.



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Effectiveness and efficiency

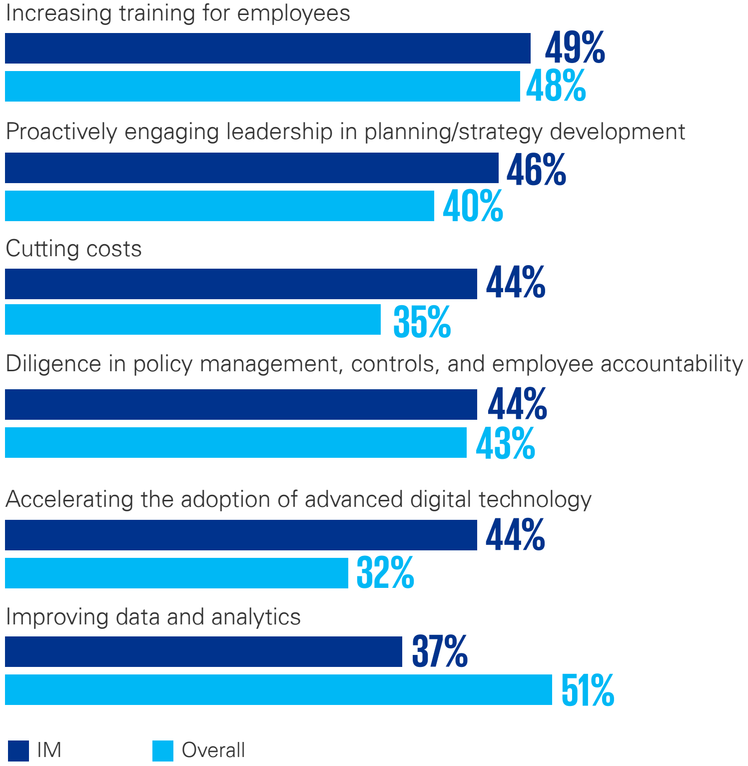
Increase the quality, consistency, extensibility, and confidence in risk management requirements and outputs.

Key findings

- IM CROs have a continual task to improve their organization's efficiency and effectiveness in their operations. Consistent with previous answers supporting employee skills development, 49 percent of respondents said that prioritizing training for employees in targeted and specialized areas was an effective strategy for strengthening teams in preparation for various challenges, highlighting the importance of continuous upskilling (Exhibit 5).
- Respondents reiterated the importance of leadership support to pursue effectiveness. They cited proactively engaging the C-suite and board in planning and strategy development as another focus area, with 46 percent highlighting the significance of integrating risk management with organizational objectives.
- After a period of relatively static spending plans, IM risk organizations are looking forward to increases in their budget allocations (90 percent), which can enhance efficiencies.
- IM CROs plan to allocate those additional dollars toward technological-driven efforts around risk management over the next 12 months. Specifically, technology-driven risk management, such as AI and ML implementation and oversight, was cited as a top priority.
- In our survey, 76 percent of respondents said they believe that AI and ML will play a critical role in accelerating risk management processes. Moreover, 90 percent believe their organizations are well or very well equipped in terms of utilizing tools and technologies to enhance their risk management capabilities.

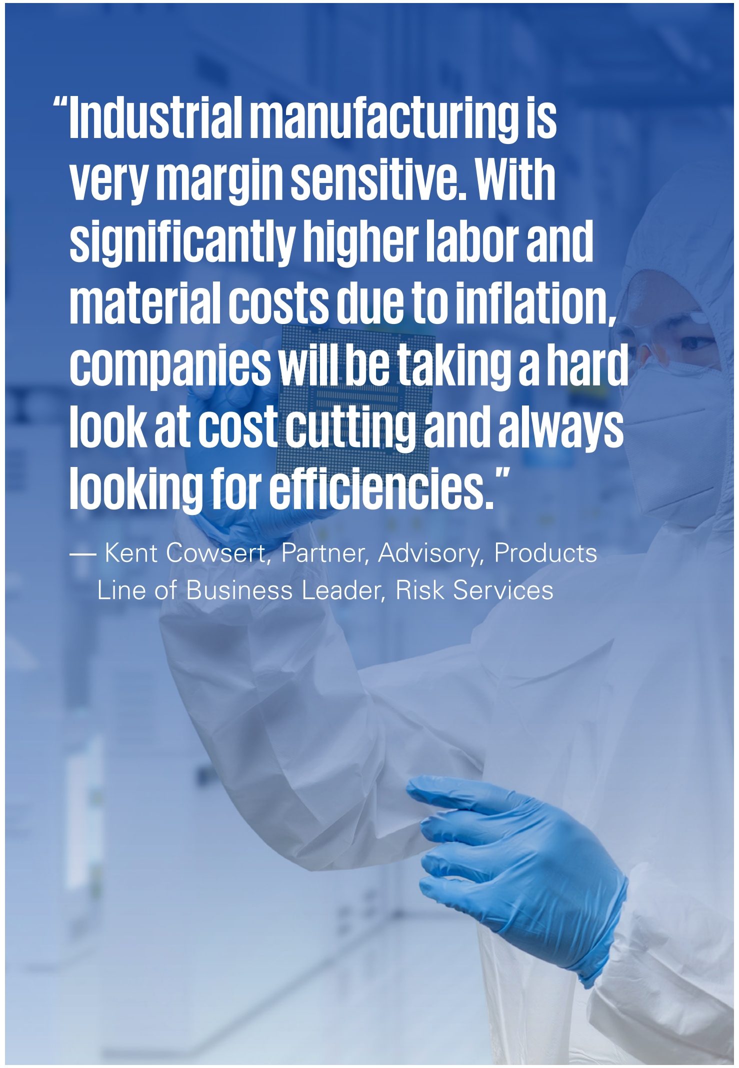
Exhibit 5. Focus areas for preparing to address risk challenges

Q. How are you empowering your team to prepare for and address these challenges?



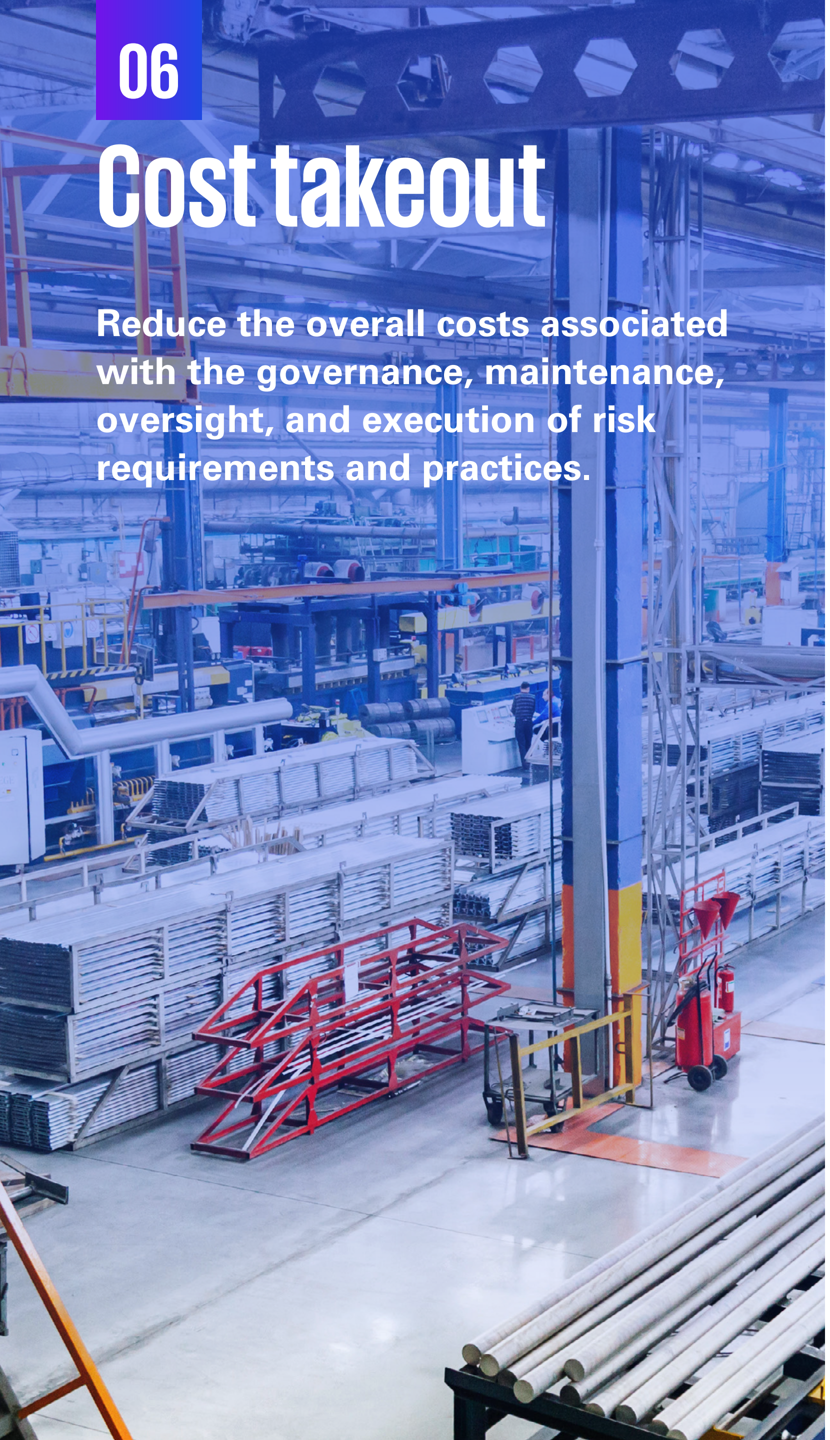
Recommendations

- Ensure digital acceleration of the risk function is in sync with the organization's transformation goals. Integrating strategically selected digital tools and techniques into risk processes in a way that is aligned to where the organization is headed can meaningfully propel its transformation.
- The skill sets for delivering risk services are changing. To manage these challenges, risk functions will need to acquire or upskill talent, especially in technical areas. Supplementing risk professionals with technical resources, including big data skills and the ability to build and use emerging technologies, will be important to future readiness.
- The most successful risk functions leverage the power of technology convergence. Take a broad view of technologies, knitting them together to empower one another to support larger enterprise goals.



"Industrial manufacturing is very margin sensitive. With significantly higher labor and material costs due to inflation, companies will be taking a hard look at cost cutting and always looking for efficiencies."

— Kent Cowsert, Partner, Advisory, Products Line of Business Leader, Risk Services



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Cost takeout

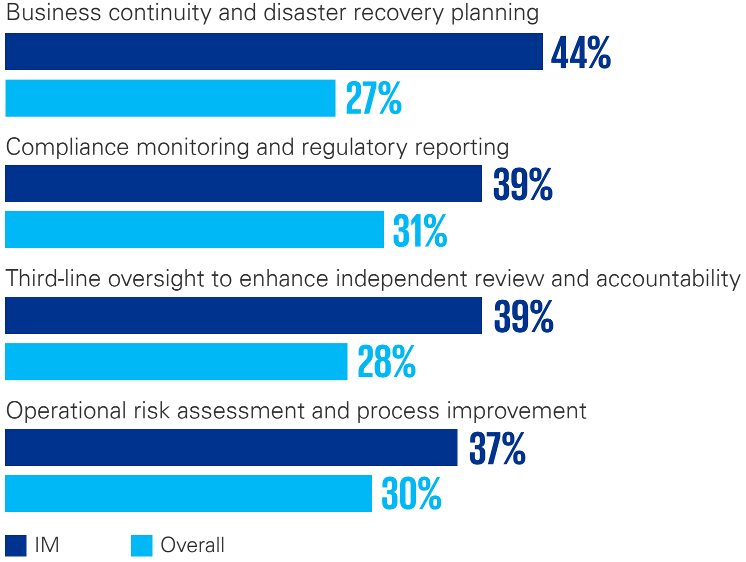
Reduce the overall costs associated with the governance, maintenance, oversight, and execution of risk requirements and practices.

Key findings

- IM CROs wanting to curb costs and increase efficiencies are looking at outsourcing certain activities. In our survey, 44 percent of respondents are considering outsourcing business continuity and disaster recovery planning, highlighting that increasing complexities of business operations and an ever-evolving landscape of threats have increased the need for specialized expertise in these disciplines.
- Another area in consideration to outsource is compliance monitoring and regulatory reporting (cited by 39 percent of respondents), which reflects the growing importance of outside expertise, as external partners can provide valuable, unbiased assessments and support in addressing the ever-growing complexities of regulatory requirements. The same percentage of respondents said they would consider outsourcing third-line oversight to enhance independent review and accountability, while 37 percent of respondents said operational risk assessments and process improvements would also be a potential area for outsourcing (Exhibit 6).

Exhibit 6. Areas considered for outsourcing to enhance risk mitigation strategies

Q. Which areas of risk management within your organization would you consider outsourcing or co-sourcing to external partners in order to enhance the efficiency and effectiveness of risk mitigation strategies?



Recommendations

- A modern risk management operating model makes the best use of technology, location strategy, and talent pools to lower costs while maintaining or improving risk posture. Start by understanding what is driving incremental spending in risk management before launching cost-cutting efforts. Consider direct spend categories but also cost avoidance categories, which are often unintended outcomes of an ineffective risk infrastructure.
- Weigh outsourcing and co-sourcing decisions against the process changes and additional resources required to maintain the required level of risk control and governance. Remember that core elements of risk management should never be outsourced as the risk is too great, and risk leaders must find a boundary where the organization can maintain quality without inadvertently creating new third-party risk.
- Consider the wide range of strategic cost takeout efforts available. Cost-reduction levers and cost-saving opportunities will vary by organization based on their objectives and current models but may include entity rationalization; product and channel simplification; global sourcing; operating model centralization and consolidation; and risk process automation and streamlining.

“Modern managed services are very different from traditional outsourcing models based on labor arbitrage for transactional work. Today’s leading providers are strategic collaborators. They combine advanced tech, data management, and sector expertise to deliver critical risk processes, such as cybersecurity and regulatory compliance, with outcomes like stakeholder trust, customer retention, and resilience. They can also reduce total cost of operations by as much as 15 to 45 percent, without prohibitive upfront capital investments.”

— David Brown, Principal, Advisory,
Global Head, Managed Services

How KPMG can help

KPMG Risk Services brings the strategic vision and technical edge to help you earn the trust of your stakeholders. Our deep IM industry skills concentrated in risk, regulation, cyber, and ESG, and our time-tested change experience, combine to create one powerful capability.

KPMG teams can help you anticipate and balance risk to generate value and a competitive advantage across your enterprise. By incorporating a detailed approach to risk, compliance, cyber, and ESG, we can help you identify new opportunities.

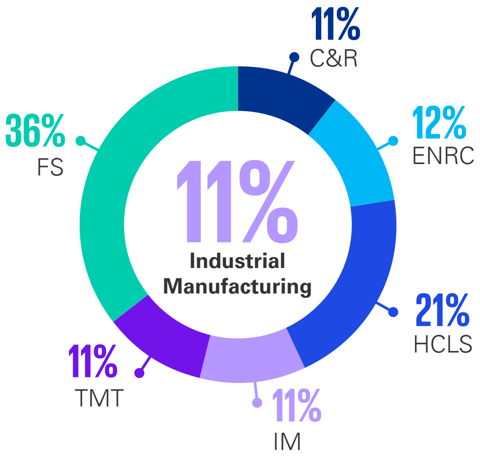
We are obsessively focused on the delivery of your strategy, your priorities, and your agenda. Using tools and solutions that accelerate your modernization journey and balance risk, we then apply deep domain knowledge across the spectrum of risk and regulatory issues, along with our skills in risk, technology, and consulting, to help drive borderless collaboration to convert the opportunities of risk into a sustainable competitive advantage for your organization.

Learn more: visit.kpmg.us/RiskServices

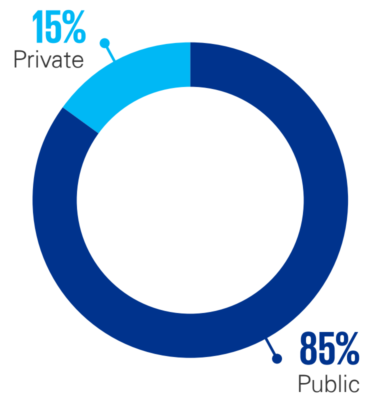
Research methodology

From July to September 2023, KPMG conducted an online survey of 390 enterprise risk officers representing U.S. organizations across six industry sectors with at least $4 billion in annual sales or $25 billion in assets under management (AUM). Forty-one respondents participated from the IM sector. Our research is designed to track trends in enterprise risk management and provide an outlook on the future of the enterprise risk function. Survey questions explore risk officer views on current and expected trends in the following areas: Risks and readiness, activities and investments, roles and approaches, and maturity and modernization.

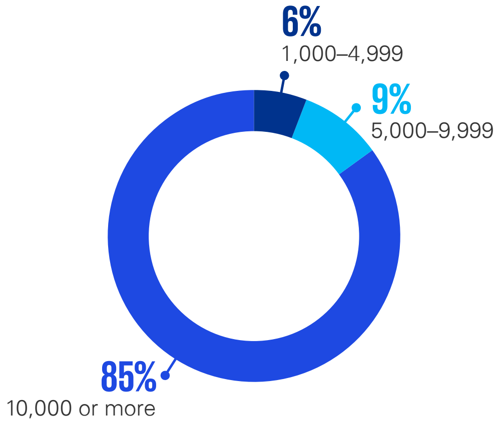
Organizational sector



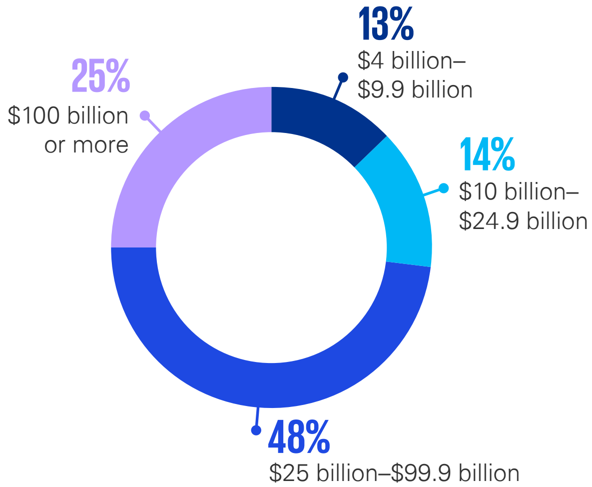
Organization type



Full-time employees in the company (Globally)



Company's annual revenue



Of the 390 enterprise risk officers responding to the survey, 41 respondents (11%) participated from the IM sectors.

Notes: N=390; Single select; Percentages may not total 100 due to rounding.

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KPMG is recognized as a leader in risk consulting

Financial risk

Third party assurance

Client advocacy in risk*

KPMG ranked No. 1 across multiple risk categories in Source's report, *Perceptions of Risk Firms in 2023*.

The Source study, *Perceptions of Risk Firms 2023*, is based on a U.S. client and prospect perception survey about risk consulting firms, led by Source. It reveals what 300 senior users in the U.S. think about the 16 leading risk advisory firms and examines how clients see firms differently as they move from awareness, to shortlisting a firm, to becoming a direct client. The report is intended to help in understanding each firm's positioning in the market and the overall competitive landscape in which they operate. For more information please visit: https://www.sourceglobalresearch.com/

*Advocacy score is based on the percentage of KPMG client respondents that say they would use the firm again and would put their personal reputation on the line for the firm.

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2023 Chief Risk Officer Survey

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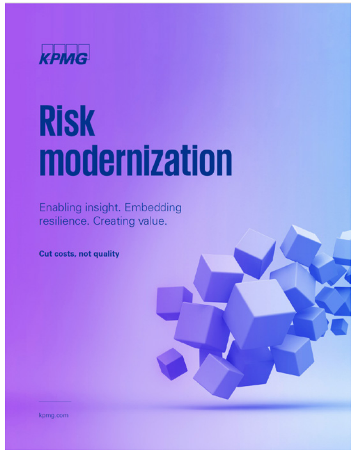
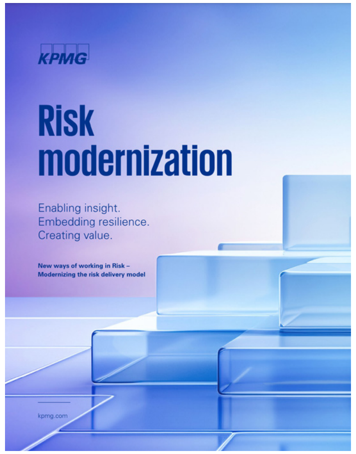


Cut costs, not quality

Unlocking the potential of digital acceleration in risk management

Implementing a modern technology architecture to accelerate risk transformation



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