The current demand and supply fundamentals of the UK housing market are in significant disequilibrium, with a housing shortage that has been estimated to equate to between 7 and 10 years of supply (Source: Joseph Rowntree Foundation, Barker Report, NHBC). Projections of the number of households for England & Wales, and London and the South East in particular, indicate that demand for all types of residential property is expected to increase rapidly over the next 20 years. There is no sign that the house building industry will be able to keep pace with these expectations even with the Government’s proposed house-building programme in the South East.

With a high single figure net yield, investors can afford to be patient in awaiting future capital appreciation.

Certain commentators expect that the fall in UK house prices will emulate, or even surpass, the decline in US house prices. However, the characteristics of both the demand and supply profiles for the two markets are very different. Various studies have calculated that the price elasticity of supply for the US market is high (above 1) and is generally between 2 and 4 (meaning that a 10% rise in house prices will lead to between a 20% and 40% increase in the supply of houses) and could be as high as 20. In contrast, Kate Barker in her Interim Review, stated that the UK housing market has “a low elasticity of supply in response to price changes” (i.e. a 10% increase in house prices will lead to less than a 10% increase in the supply of houses). Further her report stated that not only do “UK households have a high income elasticity of housing demand, but a low price elasticity of demand”. This means (i) that as household income rises, the demand for housing rises faster; and (ii) that as house prices rise, demand for housing will not decline in proportion, but much more slowly.

Currently, it is possible to acquire portfolios that yield up to 10% on cost located in and around London that address the market segments with the greatest projected excess of demand over supply. Investing in straightforward physical bricks and mortar provides its own comfort and risk mitigation as compared to derivative and leveraged investment products. With a high single figure net yield, investors can afford to be patient in awaiting future capital appreciation.

In conclusion, the recent market turmoil will, if nothing else, force investors to examine more closely the methods and rationale behind their selection of investment assets and /or investment managers. History indicates that if an improvement is sought, then one’s methods and constraints should change – or at least be examined afresh. It would be contrary to reason to expect things to change whilst doing nothing differently.

Co-Sourcing or the New Way to Ensure Audit Excellence

There is no question that a risk management revolution has indeed happened and life in a bank, as we know it will never be the same again.

Well, they’re not our words. In fact they come from the South African Reserve Bank’s guidance on the Internal Capital Adequacy Assessment Process (ICAAP) which was a key document in a consulting assignment we recently completed for a South African client. So we thought it would be helpful if we spent some time pondering on this so-called revolution. Has one really taken place and, if it has, what are the implications for internal auditors?

There is no question that a risk management revolution has indeed happened and in a bank, as we knew it, will never be the same again. The events that led up to the revolution are spread over more than a decade and are well documented. They include the deregulation and globalisation of financial markets, business consolidations through mergers and acquisitions and greater concentrations of processing power in fewer locations enabled by the rapid pace of technological innovation. Most important, perhaps, is the emergence of risk intermediation and the proliferation of securitisations and derivative transactions and an ever increasing complexity of deal structures.

The truth is that this advancing sophistication of financial products and the markets where they are traded have combined with technological innovation to produce a new reality. Banks must now come to terms with the fact that when trades and transactions enter their operating environments they trigger risk exposures that can go well beyond nominal transaction values.

The current financial crisis can be linked to accumulating risk exposures which, in a number of well publicized cases, escalated to $ billions without always finding expression in the affected banks’ financial accounting and risk reporting systems.

The Société Générale fraud and sub-prime failures are such examples. What is also evident is that such unidentified and unmeasured accumulations of risk were not attributable to any particular category of risk but a rather potent cocktail of all of them... credit, market, liquidity and operational.

These events served to heighten the awareness of banks and regulators to the need for the ongoing identification, measurement and management risks across the enterprise. The global regulatory response was Basel II complemented by a requirement from most national regulators that banks confirm, in their Internal Capital Adequacy Assessment Process (ICAAP), that all risks have been identified and measured, are subject to appropriate management and are covered by sufficient capital reserves. There is also a direct impact on internal auditors as every regulatory authority around the world that we are aware of requires that the ICAAP be subject to regular internal audit.

But if the evidence suggests that conventional financial and risk management systems are simply not capturing and reporting all of a bank’s exposures to risk, what chance does internal audit stand of identifying unreported and / or improperly measured risks during the course of their audits? The answer is quite a good one provided the audit plan is suitably risk-based and the audit team has the necessary skills and preparation. This may be easier said than done. There are two ways Risk Reward can help:
TRAINING. We have first class internal audit courses that have been developed by leading experts covering risk management, capital management and the ICAAP and our trainers are the best in the business. In the post ‘Risk Management Revolution’ era these are the skills that all your auditors must possess.

CO-SOURCING, a solution that is becoming increasingly popular with our clients. Risk Reward will provide seasoned audit professionals who are experts in risk management and specialize in the technical areas where risk exposures are likely to be prevalent, for example, Treasury. Co-sourcing ensures you have the necessary skills available in your audit team without compromising any of your managerial integrity or auditing methods. Our experts will readily adapt to your auditing methods and approaches and all working papers prepared by them are your property and form an integral part of your audit’s working papers. They can contribute to any aspect of the audit at your entire discretion… audit planning, programme writing, field work or report writing. As we are not a firm of external auditors there are no conflicts of interest. Indeed, on the occasions that there has been interaction with regulators they have positively endorsed co-sourcing.

Asset Management Solutions: for those left holding the (Money) Bag

The ‘Credit Crunch’ has brought new challenges to the Asset Management industry resulting in many participants fundamentally reviewing their business models and product offerings. Asset Managers are focusing on the future challenges and their real, as opposed to theoretical, resilience to cope with extreme or unexpected events.

Asset Management is a core Financial Services industry function but with its own unique demands, challenges and specialisms. We recognise that many of the issues and techniques required to manage and control ‘Buy-Side’ Asset Management businesses are different to other financial businesses.

Accordingly, we have designed a range of services to support Asset Managers. These are offered to:-

• Those working within Asset Management businesses, and for
• Those for whom Asset Management may be part of their wider remit or responsibility (including Independent Directors, Business Managers and Controllers, Risk, Audit and Compliance professionals).

We also offer dedicated courses and advise those who employ asset managers such as Pension Fund Trustees and Institutional Investors.

Training

Risk Reward offers a wide range of services specially tailored to Asset Managers including the following courses and in-house training:-

• Asset Management for Professionals
• Asset Management for Institutional Customers and Pension Fund Trustees
• Financial Investments and Markets
• Operational Risk Management for Asset Managers
• ICAAP Preparation and Review
• Risk Assessment Reviews
• Auditing Asset Managers
• Asset Management for Independent or Non-Executive Directors

Consultancy

Risk Reward provides support, consultancy and co-sourcing services for Asset Managers including the following:-

• Design and development of a 21st Century Risk Department for Asset Managers
• Corporate Governance and Controls for Asset Managers
• Re-organisations and Restructuring
• Mergers and Acquisitions
• Regulatory Inspection Visit Preparation