Assessing Vendor Stability

THE GROWING IMPORTANCE OF VENDOR RISK MANAGEMENT IN FINANCIAL SERVICES

Ease the Compliance Burden & Protect Your Business

At a time of widespread evolution in the global financial markets, market participants find themselves facing increasing regulatory oversight and pervasive compliance stress. A growing list of regulatory requirements and heightened focus on self-preservation and risk management are driving deep operational changes at financial institutions worldwide.

Counterparty risk has emerged as a major area of focus: Regulators are charging financial services firms with knowing more about the financial stability of counterparties that buy their services; with which they invest, trade and clear; and from which they buy services and technology. To that end, mandates like the Office of the Comptroller of the Currency’s (OCC’s) Bulletin 2013-29, “Third-Party Relationships” — which outlines the need for “ongoing monitoring of the third party’s activities and performance,” and “documentation and reporting that facilitates oversight, accountability, monitoring, and risk management” — are directing firms to adopt new risk practices and to migrate to new operational infrastructure.

Technology product and service providers are particularly critical due to the nature of financial firms’ businesses — transaction processing and reporting is central to their ability to serve clients and generate profits. The federal banking agencies, through the Federal Financial Institution Examination Council (FFIEC), have set standards to underscore this criticality in the Information Technology Examination Handbook. The handbook reads: “Financial institutions should oversee the quality of service, financial condition, and control environment of the companies providing them with critical IT services.” Regulators are now holding institutions accountable for mitigating the impact of potential shocks from their technology vendors that could harm their operations and ultimately their customers.

These dynamics are driving many firms to devote additional resources to vendor and supplier management. Firms are increasingly adopting the use of detailed financial assessments to measure vendor stability, and using that data to inform both the request-for-proposal process and ongoing management throughout the lifecycle of service and delivery. A growing number of organizations now use financial operating results to measure their vendors’ long-term viability and predict the impact of future risks on their own business continuity.

Financial institutions need to demonstrate insight into the financial stability of their vendors and other counterparties as the regulatory environment continues to tighten. They need to establish robust processes to monitor and mitigate vendor risk, not only to meet emerging regulatory requirements, but also to maintain operational stability and ultimately profitability. And they need irrefutable audit trails for everything they put in place.
A leading Wall Street broker-dealer, guided by FFIEC standards, identified the need to improve consistency and diligence across its vendor management workflow. The firm’s vendor management team needed to focus its attention on developing and executing smarter risk mitigation strategies rather than dedicating resources to financial health assessments. The team engaged Rapid Ratings to filter its vendors by criticality and provide deep assessments of their financial health and operating efficiency, as well as tailored automated commentary and customized quarterly reports.

Risk management efforts such as these are most effective when an entire organization is committed to their success. In this case, each of the firm’s individual businesses units committed to the need to obtain and analyze financial data from vendors, and use that data to consider ending relationships with vendors that might put the firm at undue risk.

**Results:** With this program in place, the firm now has the ability to easily identify companies that are high risk or that exhibit warning signs of decreasing stability. Its analysts can then conduct deeper qualitative evaluations of those higher-risk vendors, and in certain cases, obtain committee approval to continue the relationship. This has created major efficiencies by allowing analysts to focus on identifying and mitigating potential risks before problems occur and developing contingency strategies as needed, and to leverage Rapid Ratings’ trusted analysis rather than spending their own time and resources on risk calculations.

### About Rapid Ratings International

Our solutions allow financial institutions to assess their global suppliers, vendors, and other counterparties most effectively. We provide the same depth of analysis on public and private companies by using a methodology proven to be far more predictive than traditional ratings tools that rely on payment history or qualitative judgments. Our proprietary, quantitative Financial Health Rating (FHR®) system has earned a reputation for the early warning it provides on a company’s deterioration or improvement. It saves companies time and money, improves efficiency in their relationship management workflows, and helps financial services firms protect their operations and meet mandates for risk monitoring, documentation and reporting.

### What We Offer

Our research reports and analytics provide a deep dive into the financial health of a company. We map a company’s current and historical risk trend over time, including its strengths and weaknesses compared to its industry peers, and its full financial statements. Our system applies 62 different financial and operating ratios to 27 elements of a company’s quarterly and annual financial reports; these ratios address the company’s debt service management, leverage, working capital efficiency, sales, cost structure and overall profitability. We then employ these ratios according to the proprietary weightings assigned to each of 24 unique industry models. The weightings, in turn, result from exhaustive and continuing analysis of our singular database — financial reporting from more than 300,000 companies of all sizes in more than a dozen countries over the course of more than 30 years of operating history, companies that have succeeded as well as those that have not. The sum of these weightings becomes the rated company’s individual FHR (zero/worst to 100/best).

### How Our Clients Benefit: A Case Study

A major financial services organization uses our ratings, information we collect on its behalf, and our customized reports as key inputs in its vendor management program. When a federal regulator visited the client’s offices to review its approach to vendor risk management, our client showed the inspectors our customized individual company reports as well as our national corporate reports to illustrate that it was also focused on country risk. The inspectors commended the organization, whose approach they called “best in class,” stating that they would “love to see others doing the same.”

Rapid Ratings continues to be recognized by its clients, major media outlets, and the financial services industry as a trusted resource on the topic of assessing the financial stability of vendors and counterparties.