FACING RISKS IN MANAGEMENT ACTIVITIES

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Abstract: Risk is an event that can meet a man almost in each situation. Risk includes uncertainty of future event and it is important to stress not only negative but also positive side of the risk. This paper deals with risk identifications related to enterprise managing activities and emphasises the reality that ability of managers to understand the risks and know to work with them is not only competitive advantage but necessary condition of successful managerial work.

INTRODUCTION

Risk is inescapable in business activities. As Peter Drucker said as far back as the 1970s, the one thing, that is certain about the future, is its uncertainty, its risks. A world in which companies take no risks is a world where you make no money [1]. The management activities in enterprises are becoming more and more complicated and demanding process because the elements of single environments are in continuous development; they are changing and mutually connected and can unexpectedly interact. The specific environments differ among themselves in so called environment uncertainty that is given by two dimensions – rate of changes and degree of environment complexity [2]. Actual business environment is often indicated as chaotic, turbulent and discontinuous. However the chaos does not mean disorder but impossibility to forecast future development following the former and present situation since it is influenced by a lot of factors that cannot be all defined.

BUSINESS AND PURE RISKS

Business risks include both upside and downside. Business risk is often defined as danger that the really achieved economic results of business activity will differ from supposed results whereby these deviations can be desirable or undesirable and their range can be various.

Business risk can be characterized by means of three components [3]:

$$R = \{S_i, H_i, P_i\}$$

where: R … risk,

S_i … situations of development of decision making object and his environment,

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H_i… values of evaluation criterion for single situations,

P_i … probabilities of occurrence of single situations,

$i = 1,2...n$, where n … number of risk situations

Pure risks encompass only danger of undesirable situation occurrence or unfavourable deviations from desirable objective, situation that include preservation of property, human lives and health. Pure risks usually refer to losses and damages to property, people and health. They include e.g. losses of lives caused by natural events (floods, fires, earthquakes), technical systems and their failures (machinery accidents, car accidents, failure of safety devices), people acting (thefts, malversations, strikes). These events include only loss, hazard and adverse consequences.

SYSTEMATIC AND UNSYSTEMATIC RISKS

Systematic risks are systematically changing in dependence on total economic development. The sources of systematic risks are e.g. changes of monetary and budgetary policy, changes of tax system, total market changes (price changes of basic energy kinds), war conflicts, inflation, political events, etc. These risks are threatening all economic units or business activity spheres approximately in the same way. Taking into consideration that systematic risks are considerably dependent upon total market development, they are also indicated as market risks. These risks cannot be reduced by diversification and that is why they are known as un-diversifiable, too. In respect of their character, the systematic risks present macroeconomic risks.

Unsystematic risks are risks specific for single enterprises. They are caused e.g. by important producing or technological innovations in certain manufacturing field, market entry of new competitor, breakdowns of machineries, etc. In respect of their character, the unsystematic risks present microeconomic risks [5] .

INFLUENCEABLE AND UNINFLUENCEABLE RISKS

Uninfluencable risks are not possible to be influenced by manager in favourable course. Therefore it is necessary to concentrate on such measures that reduce the negative impacts of the risk in case of future occurrence of considerably unfavourable risk situations. They include a great part of risks as e.g. prices of raw materials and other materials at the foreign market, political situation in certain regions.

Influenceable risks can be influenced by manager in certain way for his benefit. Business risk reducing can be achieved by acting on its causes to prevent occurrence of the unfavourable situations in the future, e.g. through the products quality, guarantee conditions and service quality can affect the sale level and achieved sale price.

Internal risks fall into the group of more likely to be influenceable in contradistinction to external risks that are more likely to be uninfluencable.

STRATEGIC AND OPERATIVE RISKS

The uncertainty level for strategic risks is higher than for operative since the time framework of strategic risks impact is higher.

Strategic risks are connected with strategic movement of the enterprise, they are often function of uncertainties that arise as a result of government policy, competition, judicial decisions or changes in requirements of interested parties.

Operative risks result from inadequate or incorrect human activities, internal processes and systems in enterprise and also from external reasons. They are hidden in all activities and have mostly short time duration. Their impacts can be also extensive and catastrophic.

EXTERNAL AND INTERNAL RISKS

The source of external risks are external factors that are split into macroeconomic (macro environment in the form of political, economic, legal, ethical, technological, social and global environment) and microeconomic (other business subjects, competition).

Internal risks relate to specific internal environment of the enterprise the decisive elements of which are: organizational structure, enterprise resources and enterprise culture. According to [2] there are seven dimensions describing enterprise culture: attention paid to details, orientation on results, orientation on people, orientation on teams, aggressiveness, stability and orientation on innovations and risks.

RISKS ACCORDING TO SCOPE OF ACTIVITIES

Technical - technological risks arise especially during research and development of new products and technologies and their application into practice. They can bring great successes but also great losses. They include such risks as e.g. insufficient technical solution, technical failures during start up a new production, using out of date technologies, etc.

Production risks are connected to processes in the company (management, operational and supporting) with which it creates values for consumers, and using the values in practice[6]. The risk factors of manufacturing risks can be internal, e.g. organizational factors (human factor), machinery reliability, respecting the quality of manufacturing process and also external factors, e.g. shortage of resources and raw materials, environmental standards. These risks are sometimes indicated also as operative.

Economic risks present wide range of risks arising especially on the basis of the price changes of single cost items, e.g. increasing the prices of raw materials, materials, energies, and services. They also include risks resulting from the cost structure, i.e. from ratio between fix and variable costs and risks connected with foreign business activities.

Market risks are connected with position of products and services on home and foreign markets. They are very closely connected with competition activities, customers' behaviour and with the way and speed of market saturation. They usually have form of sale or price risks. They are affected by marketing, price and position factors. They include also risks resulting from international commerce e.g. mentality difference, language barrier, legal systems difference, great distance between contractual sides.

Financial risks are very important for analysis of business plan and strategic decision making. They are connected with accessibility of financing resources, payment inability, enterprise indebtedness, unfavourable changes of interest rates, exchange rates, protectionism in international commerce, etc.

Legislative risks are connected with economic and legislative government policy. They include e.g. changes of tax laws, acts for protection of natural environment, decrease of protection of home market, monetary and budget policy, insufficient protection of intellectual property.

Political risks are caused by bad economic and political situation in the country. They include strikes, national and race riots, civil wars, wars, revolutions, terrorist actions, etc. that are the source of political instability and political systems changes.

Environmental risks are connected with deterioration of natural environment. They can have a form of costs for remedy of natural environment damages caused by air, water and soil pollution, costs for ensuring accordance with natural environment protection standards, etc.

Risks connected with human factor result e.g. from insufficient educational level, unfavourable physiological and psychological presuppositions for assigned work, from insufficient practical experience and abilities, negative attitudes and access to work, weak motivation, bad working discipline and insufficient sense for responsibility. Risks of managers, their way of management and quality of interpersonal relations at the working place play an important role.

Information risks can be divided into three groups – data, software, hardware. They result especially from information systems failure, data and software securing against abuse by internal and external subjects.

Acts of God connected with risks of accidents, natural disasters as floods, windstorms, landslides, earthquakes, fires.

ENTERPRISE RISK MANAGEMENT

Practical application of risk analysis and risk management can be realized with help of many relevant documents, e.g. Slovak standard STN 01 0380 Risk Management, the Australia /New Zealand standard AS/NZS 4360:2004 Risk Management, in Great Britain A Risk Management Standard © AIRMIC, ALARM, IRM:2002 and standard BS 6079-3:2000 Project management. Guide to the management of business related project risk, Canadian standard CAN/CSA Q850-97 (R2002) Risk Management: Guideline for Decision Makers, in USA the COSO Enterprise Risk management – Integrated Framework: 2004, etc.

Figure 1. COSO - Enterprise Risk Management- Integrated Framework [4]

Following the COSO Enterprise Risk management – Integrated Framework [4], the risk management in enterprise can be very concisely characterized by a cube that symbolizes a direct relationship among the components of the enterprise risk management, the objectives the enterprise strives to achieve and its organizational structure (figure 1).

The four objectives categories - strategic, operations, reporting and compliance – are represented by the vertical columns, the eight components of enterprise risk management - internal environment, objective setting, event identification, risk assessment, risk response, control activities, information and communication, monitoring - by horizontal rows and enterprise units by the third dimension.

This approach emphasises that the enterprise risk management is not another added function in organizational structure but it is part of management activities of all managers and also scope of employment of all employees. Everyone in an enterprise has some responsibility for enterprise risk management in accordance with established directives and protocols. Enterprise risk management is a multidirectional, iterative process in which almost any component can and does influence another.

CONCLUSION

Although the risks form an integral part of business from ancient times, the importance of business' risks, their analysis and management draw attention of managers only in the last ten years especially now in the traumatic years of the global economy. Discussions about risks and their management need to happen in each company, now more urgently than ever.

Risk understanding and its management should become part of everyday work of managers because the enterprise value is created, protected or disrupted just by their decisions in all activities, from strategy setting to every day company operation. In leading organizations, risk management is viewed as a management competency that enables the enhanced management of uncertainty and volatility, effectively minimizes threats and capitalizes on opportunities.

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