Need for Risk Evaluation

Meaning of Risk Management

Risk management is the identification, evaluation, and prioritization of risks followed by coordinated and economical application of resources to minimize, monitor, and control the probability or impact of unfortunate events or to maximize the realization of opportunities.

Risks can come from various sources including uncertainty in financial markets, threats from project failures (at any phase in design, development, production, or sustaining of life-cycles), legal liabilities, credit risk, accidents, natural causes and disasters, deliberate attack from an adversary, or events of uncertain or unpredictable root-cause. There are two types of events i.e. negative events can be classified as risks while positive events are classified as opportunities. Risk management standards have been developed by various institutions, including the Project Management Institute, the National Institute of Standards and Technology, actuarial societies, and ISO standards. Methods, definitions and goals vary widely according to whether the risk management method is in the context of project management, security, engineering, industrial processes, financial portfolios, actuarial assessments, or public health and safety.

Strategies to manage threats (uncertainties with negative consequences) typically include avoiding the threat, reducing the negative effect or probability of the threat, transferring all or part of the threat to another party, and even retaining some or all of the potential or actual consequences of a particular threat. The opposite of these strategies can be used to respond to opportunities (uncertain future states with benefits).Risk management is the process of identification, analysis and acceptance or mitigation of uncertainty in investment decisions.

- Risk is inseparable from return in the investment world.
- A variety of tactics exist to ascertain risk; one of the most common is standard deviation, a statistical measure of dispersion around a central tendency.
- Beta, also known as market risk, is a measure of the volatility, or systematic risk, of an individual stock in comparison to the entire market.

- Alpha is a measure of excess return; money managers who employ active strategies to beat the market are subject to alpha risk.

Risk Involved in an International Business

Every country presents its own investment opportunities. Before expanding your company overseas, however, be aware of the additional risks of the foreign trade market. In general, the risks of conducting international business can be segmented into four main categories: country, political, regulatory and currency risk.

1. Country Risk

Weigh the benefits of your company doing business abroad against the potential pitfalls. Poor infrastructure such as roads, bridges and telecommunications networks can make it expensive to operate a business in another country. Economic conditions such as high unemployment or a largely unskilled labor force can be barriers to entry. Rogue nations may have untapped potential, but may also pose risks such as terrorism, internal conflict and civil unrest. Anti-foreign sentiment among citizens, workers and government officials may also make doing business abroad especially challenging. Other country risks include crime and corruption.

2. Political Risk

Determine the political climate of the country you hope to enter. An unstable or ineffective government will be unable to protect your business interests. Lack of a strong foreign trade policy means that your business will have to navigate through the nuances of allying with government officials who may fall from power. An incoming government may not be business-friendly, and may decide to increase tariffs or impose quotas.

3. Regulatory Risk

A sudden change in trade laws or a poor legal system exposes your business to regulatory risk. For example, a country without clearly defined intellectual property laws make it difficult for foreign software companies to protect their investments. Changes in banking laws may limit your company's ability to repatriate money to your home country or may limit access to funding.

4. Currency Risk

Fluctuations of a foreign country's currency can diminish profits when converting back to the home currency. Analyze the risk and rewards of making an investment in another country. The currencies of stable governments are less volatile than those of less-developed countries. Hedging strategies could mitigate some of the currency risk; however, your business is still at the mercy of the vagaries of the local currency market. Sudden changes in monetary policy will also affect currency rates.

5. International Trade Association

If you are planning to do business overseas, contact the local office of the International Trade Association, or ITA, in your state. The ITA is one of many agencies within the U.S. Department of Commerce and is responsible for providing small- and medium-sized businesses with customs and trade facilitation support in foreign markets. The ITA has Commercial Trade Service professionals in more than 100 U.S. cities and nearly 80 countries.

Ways to Manage Risk

Let’s face it, however confident you are that your project will be a success, there is always a chance that something might go wrong. The things that might go wrong are called project risks, and a wise project manager identifies them early at the beginning of the project so that he or she can do something about them. Of course, risk management is an ongoing activity, so you should carry on identifying and recording new risks as they come up.

Creating a list of risks is a good starting point, but it isn’t enough in itself. You also need an action plan per risk in order to be able to manage them effectively.

There are 5 main ways to manage risk: acceptance, avoidance, transference, mitigation or exploitation. Here’s a detailed look at each of them.

1. Accept The Risk

Accepting the risk means that while you have identified it and logged it in your risk management software, you take no action. You simply accept that it might happen and decide to deal with it if it does.

This is a good strategy to use for very small risks – risks that won't have much of an impact on your project if they happen and could be easily dealt with if or when they arise. It could take a lot of time to put together an alternative risk management strategy or take action to deal with the risk, so it's often a better use of your resources to do nothing for small risks.

2. Avoid the Risk

You can also change your plans completely to avoid the risk. Avoid risk This is a good strategy for when a risk has a potentially large impact on your project. For example, if January is when your company Finance team is busy doing the corporate accounts, putting them all through a training course in January to learn a new process isn't going to be a great idea. There's a risk that the accounts wouldn't get done. It's more likely, though, that there's a big risk to their ability to use the new process, since they will all be too busy in January to attend the training or to take it in even if they do go along to the workshops. Instead, it would be better to avoid January for training completely. Change the project plan and schedule the training for February when the bulk of the accounting work is over.

3. Transfer The Risk

Transference is a risk management strategy that isn't used very often and tends to be more common in projects where there are several parties. Essentially, you transfer the impact and management of the risk to someone else. For example, if you have a third party contracted to write your software code, you could transfer the risk that there will be errors in the code over to them. They will then be responsible for managing this risk, perhaps through additional training.

Normally transference arrangements are written up into project contracts. Insurance is another good example. If you are transporting equipment as part of your project and the van is in an accident, the insurance company will be liable for providing new equipment to replace any that was damaged. The project team acknowledges that the accident might happen, but they won't be responsible for dealing with sourcing replacement kit, moving it to the right location or paying for it as that is now the responsibility of the insurance company.

4. Mitigate the Risk

Mitigating against a risk is probably the most commonly mitigation of risk used risk management technique. It’s also the easiest to understand and the easiest to implement. What mitigation means is that you limit the impact of a risk, so that if it does occur, the problem it creates is smaller and easier to fix.

For example, if you are launching a new washing machine and the Sales team then have to demonstrate it to customers, there is a risk that the Sales team don’t understand the product and can’t give good demonstrations. As a result, they will make fewer sales and there will be less revenue for the company.

A mitigation strategy for this situation would be to provide good training to the Sales team. There could still be a chance that some team members don’t understand the product, or they miss the training session, or they just aren’t experts in washing machines and never will be, but the impact of the risk will be far reduced as the majority of the team will be able to demonstrate the new machine effectively.

You can mitigate against the impact, like in this example, and you can also mitigate against the likelihood of it happening. Sometimes the actions will be broadly the same; sometimes you’ll have to have some tasks to reduce the chance that the risk happens and some separate tasks to make the impact of the risk smaller if it happens.

5. Exploit the Risk

Acceptance, avoidance, transference and mitigation are great to use when the risk has a negative impact on the project. But what if the risk has a positive impact? For example, the risk that the new washing machines are so popular that we don’t have enough Sales staff to do the demonstrations? That’s a positive risk – something that would have a benefit to the project and the company if it happened. In those cases, we want to maximize the chance that the risk happens, not stop it from happening or transfer the benefit to someone else!

Exploitation is the risk management strategy to use in these situations. Look for ways to make the risk happen or for ways to increase the impact if it does. We could train a few junior Sales admin people to also give washing machine demonstrations and do lots of extra marketing, so that the chance that there is lots of interest in the new machine is increased, and there are people to do the demos if needed.

Need of Risk Management

Risks management is an important process because it empowers a business with the necessary tools so that it can adequately identify potential risks. Once a risk's been identified, it is then easy to mitigate it. In addition, risk management provides a business with a basis upon which it can undertake sound decision-making.

For a business, assessment and management of risks is the best way to prepare for eventualities that may come in the way of progress and growth. When a business evaluates its plan for handling potential threats and then it develops structures to address them, it improves its odds of becoming a successful entity.

In addition, progressive risk management ensures risks of a high priority are dealt with as aggressively as possible. Moreover, the management will have the necessary information that they can use to make informed decisions and ensure a business remains profitable.