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FROM TRADITIONAL TO DYNAMIC: EXPLORING NEW DIMENSIONS IN BUSINESS RISK MANAGEMENT

Dr.Abdullah Khalid
Business Finance and Economics, Assistant Professor,Maulana Azad University, Jodhpur

ABSTRACT
Business involves a large variety of decisions in an environment of uncertainty which, in turn, involve a Variety of business risks. Such risks occur as per arise uncertainties concerning the occurrence of a loss which may be due to
(i) variability in future outcomes,
(ii) possibility of an adverse deviation from that hoped for and/or
(iii) variation in possible outcomes that exists in a given situation'. There can be a variety of loss exposures like loss exposures for property, liability, business income, human resources, crime, employees' benefits and foreign loss exposure. These are due to exposure of the business enterprises to a variety of risks, such as, competitors risk, economic risk, environmental risk, resources risk, technological risk and financial risks including counterparty, funding, currency and interest rate risks.

INTRODUCTION

The competition risk extends from pricing and marketing of products/services to the speed at which others emulate one's ideas or innovations. It has been accentuated by opening of the national frontiers for trading with rest of the world, technological advancement and changing of strategic alliances. The economic risk is inherently due to cyclical fluctuations in business activity levels which are generally characterized by a wave-like fluctuations alternating between expansion and contraction phase without any regularity in amplitudes and severity with a powerful combination of upside greed and downside fear.

The environmental risk for business may arise on account of need to comply with environmental or safety regulations, higher cost or shortages of raw materials from suppliers hit by environmental problems or costs and disruptions resulting from the need to clean up to accumulated pollution. The importance of obtaining, processing and circulating information can be hardly overemphasized any because business will be as good as the information on which the decisions are based including those about costs, liabilities, markets, resources, technology and finances.

The legal risk for the business may assume the form of
(i) documentation risk resulting from errors or omission in documents,
(ii) jurisdiction risk arising from the possibility of the plaintiff taking action against the business in an overseas court,
(iii) litigation risk arising risk from any reference made in statutory report and accounts or other communications about the legal actions as it may involve huge costs, both financial and time, (iv) discovery risk resulting from opponents' right to inspect the internal files and record of the business and thereby discovery certain facts which may go against the business, and
(v) environmental/ health and safety legislation risk controlling manufacturing processes, emissions, pollution, recycling and health/ safety at work.

The operational risk may arise due to information technology and other system failures and deficiencies, confidentiality or security breaches, failures of internal control/ supervision, physical disasters involving people, premises or equipments whether natural (earthquakes/ floods) or man-made (fire/bombs), manufacturing/ delivery failures, failures in compliance for health and safety regulatory requirements, staff resource deficiencies and dependence or third party contractors on outsourcing.

The political risk for business may be as per the potential impact of decisions taken by national governments, government agencies and other regulatory bodies empowered to control trade or set prices and industry standards. Such risks may rise due to taxation quotas, tariffs and other trade barriers, currency exchange controls/ in convertibility,if the business is involved in export trade and it may arise to the busi- ness involved in domestic trade due to interest rate variations, grants and subsidies, granting of licenses, nationalization/ expropriation and others.

The resource risk may be about the continued availability to the business of the various resources like raw materials, water, power, labor plant and machinery or transportation at reasonable prices. Busi- ness may also face technological risks due to threat that new ways of doing things will reduce or destroy the demand for existing products, public relations through media and other pressure group may also pose serious reputation risks by trying to bring down the image of the busi- ness in public eyes.

THE BUSINESS RISK

The business risks, in essence, refer to the uncertainties concerning the occurrences of losses and may be categorized as
(i) objective risk which refer to the variation of actual losses from the expected losses, and
(ii) subjective risks which reveal the uncertainties based on the state of mind of the decision makers. The business risks may also be classified as
(i) pure risks which indicate risk situations having the possibility of loss or no loss such as risk of unemployment, risk of insufficient income, etc. and
(ii) speculative risks which refer to the risk situation in which either profit or loss is a possibility. Beside the various other types of business risks, the counter party risk and funding risk kinds of financial risks belong to pure risk category, whereas the interest rate risks and currency risks of financial risk come under speculative risk category.

The business risk management refers to the process of identifying the loss exposures to the business and selecting the most appropriate technique for treating such loss exposures. It may have twin objectives viz
(i) pre-loss objectives, and
(ii) post-loss objectives. Under the former the efforts are made to prepare the firm for potential losses in the most economical way like installation of safety devices, disposal of hazardous wastes, meeting legal obligations, etc. Under the latter it aims at making efforts for ensuring survival of the firm, stabilization of earnings, continued growth of the firm and minimizing the effects of loss on other persons and society."

For business risk management a four-pronged approach may be followed
(i) identifying the potential losses,
(ii) evaluating the potential losses,
(iii) selecting the appropriate techniques for treating loss exposures, and
(iv) implementing and administering the risk management programmes. The potential loss exposures may be in regard to
(a) properties, like buildings, plants other structures furniture's, equipments, computer software, supplies, inventories accounts receivables and valuable records
(b) liabilities, like those supplies of defective products, environmental pollution, law suits and others
(c) business income, such as loss of income, extra expense, contingent business incomes, etc.
(d) human resource, like retirement or disability of key employees, job-related injuries or desees experienced by workers
(e) crimes, like holdups, robberies, burglaries, thefts, fraud and embezzlement by employees and misuse of internet or computer by the employees
(f) employees benefit, such as, failure to comply with government regulations, violation of fiduciary responsibilities and failure to pay promised benefits, and
(g) foreign losses in respect of plants, business properties and inventories abroad, foreign currency risks or political risks.

For this, there are several sources of information for identifying the loss exposures which may be mobilized through
(a) risk analysis question nearer to be filled up by the risk managers
(b) physical inspection of plants and operations,
(c) flowcharts of production and delivery of goods,

(d) financial statements analysis reveling profitability, liquidity, solvency ect.
(e) historical loss data showing department losses over time.

After identifying the potential loss exposures, the business risk management evaluates and measures the impact of such loss where the loss frequency refers to the probable number of losses that may occur during some given time period and loss severity refers to the probable size of the losses that may occur. On estimating the frequency and severity of loss for each type of loss exposure, these are ranked according to their relative importance. Thus, a loss exposure for potential bankruptcy of the firm is relatively high as compared to an exposure with a small loss potential. Moreover, the relative frequency and severity of each loss exposure must be ascertained, so as to select the most appropriate techniques for their nailing. Although the loss frequency and loss severity both are considered but severity is attached more importance, as a single catastrophic loss could wipe out the firm.
The business risk management, after evaluating the potential losses may proceed to selecting the most appropriate techniques for treating the loss exposures. The techniques may either be
(i) risk control techniques that reduce the frequency and/ or severity of losses, and
(ii) risk financing techniques that provide for the finding the losses and the risk management may use a combination of techniques for treating each loss exposures.

Risk control comprise the techniques
(i) loss avoidance,
(ii) loss prevention, and
(iii) loss reduction. Under loss avoidance, certain loss exposure is never acquired or an existing loss exposure is abandoned. Thus, a plant is never established in a food prone area or the drugs with dangerous side effects are withdrawn from the market. The potential loss may be reduced to zero. However, in real world situations it may not be feasible or practical to avoid all losses or exposures to losses. The risk control may also be attempted through loss prevention which refers to measures that reduce the frequency of a particular loss, such as, for preventing accidents, strict shirt enforcement of safety rules and for reducing the law suits from defective products installation of quality control checks. The risk control through loss reduction refers to measures that reduce the severity of a loss after it occurs, such as, segregation of exposure units like having warehouses with inventories at different locations, rehabilitation of workers with job related injuries and limiting the volume of cash in hand.

RISK FINANCING TECHNIQUES

Risk financing techniques for treating the loss exposures consist of
(i) loss retention,
(ii) non-insurance transfers, and
(iii) commercial insurance. Under loss retention, the firm retains part all of the losses that can result from a given event. It may be
(a) active, if the firm is aware of the loss exposure and or plans to retain it partly or wholly, and
(b) passive, if the firm fails to identify the loss exposures fails/ forgets to act accordingly. This techniques is affectively used if
(i) no other method of treatment of losses is available,
(ii) the worst possible loss is not serious, and
(iii) losses are highly predictable like compensation claims to workers, loss due to damage to automobiles, shoplifting losses. Based on past experience, the probable rage of frequency and severity of actual losses can be estimated and can be budgeted out of the firm's income. The retention levels may be decided as a given percentage of annual earnings before taxes from the current operations, or of net working capital. The losses may be paid out of current net income, funded or unfounded reserves or from a credit line established with a bank,"

These losses can also be paid by captive insurers which are owned by the parent firm for the purpose of insuring its loss exposures. These captive insurer may be (i) a pure captive insurer which is owned by only one parent firm, and
(ii) an association or group captive insurer which is owned by several parent firms. These captive insurers are formed due to
(a) difficulty in obtaining insurance,
(b) lower costs,
(c) greater stability of earnings,
(d) easier access to re- insurers, and
(d) formation of a profit centre.

The loss retention by any means may prove advantageous, as it may save money in the long run if actual losses turn out to be less than the loss component in insurer's premium. Some expenses may be reduced, like loss adjustment expenses, general administrative expenses, commissions and taxes. This may encourage loss prevention and cash retention as payment to insurers premium will not be needed. However, the possibility of higher losses, expenses and taxes can also not be overruled."

Another risk financing technique for managing the loss exposures is the non-insurance transfer, which involves a transfer of a pure risk and its potential financial consequences to another party through contracts for losses and hold-harmless arguments (e.g. in publishing business this agreement makes the author, not the publisher, legally liable if the publisher is sued for plagiarism. This is advantageous as the firm can transfer some potential losses that are not insurable. It costs less than the insurance and is handled by the person who can exercise better loss control. However, if the person, whom the potential loss is transferred, fails to pay the loss, the firm continues to remain responsible for the claim.

have a low probability but a high severity of loss. For this the firm may also rely on insurance against loss exposures that selects the insurances coverage and insurer and negotiates the terms of insurance and this information is disseminated and the whole insurance programme is reviewed periodically. Under this technique of risk financing, the firm will be indemnified if the loss occurs and thus, the uncertainty is reduced. Moreover, insurance premia are deducible business expense and therefore, results into tax saving. However, payment of premia is a major cost and negotiating the insurance coverage requires considerable time amend efforts. Moreover, this may provide less incentive to follow a loss control programme.

ADMINISTERING RISK MANAGEMENT PROGRAMMES

It requires a policy statement which outlines the objectives and the policy decision regarding treatment of loss exposures. It increases the awareness of top level executive about risk management and gives more powers to risk managers and provides standards for judging the risk managers performance. It may also help in developing the Risk Management Manual which details the objectives, responsibilities and available technique for handling loss exposures. The Risk Management may seek assistance from other functional

Department for identifying and treating exposures as follows:-
1. Accounting- Internal accounting controls may reduce employees' fraud and theft of cach.
2. Finance-It may show how losses disrupt the projects and cash flows and the effects losses may have on the balance sheet and profit and loss account.
3. Marketing- It may show that accurate packaging can prevent the liability of lawsuits and safe distribution procedure can prevent accidents.
4. Production- It may shows that quality control can prevent production of defective goods and liability of lawsuits. Effective safety measures can reduce accidents and injuries.
5. Human Resource - This may run employees benefit programme, pension programme and implement recruitment/ selection, promotion and dismissal policies which may Assist in identifying, avoiding preventing or retaining the loss exposures.

The risk management programmes, particularly risk management costs, safety programmes and loss prevention programmes must be carefully monitored. Loss recored must also be examined to detect any change in frequency and severity and the coop oration from other departments for risk management must be scrutinized periodically.

In nineties of the past century the scope of business risk management expanded from traditional pure loss exposure management to cover speculative risk management known as financial risk management which involves identification, analysis and treatment of speculative risks, viz. counter party risks, funding risks, interest rate risks and currency risk as follows:

(i) Counter Party Risk- It arises due to possibility of failure intentional or unintentional (i.e. counter party) to a transition to honour ther obligations in regard to payment for or delivery of goods/services or repayment of borrowings, payments in advance or on delivery, letters of credit issued by banks at the request of the business as the payments by the banks to the suppliers is made against the documents presented and not against the inspection of goods supplied.

(ii) Funding Risk- the business enterprise may raise funding through quality issues and/ or preference share issues where it is exposed to risk of incurring considerable cost in completing the formalities and in not observing the

extensive regulatory and disclosure requirements. Funding may also be raised through borrowings from banks and other financial institutions as well as from the public by issuing debentures/required and repayments to made involve some financial risk. The business may resort to project financial where the servicing of the funding depends on the revenue streams of the project rather than on a charge over the assets. The projects often involve market risk, cost risk, technical feasibility risk, land various other risks about performance of contractors, suppliers and operators, income stream, time and cost over runs, etc. It may also resort to assets based financing like confidential invoice financing or factoring where if the debtor fails to pay in settlement of invoice or bill of exchange, the business has to pay.

(iii) Interest Rate Risk-This may arise on the borrowings, lending or deposits of the business. The interest to be paid or received depends on the term, volume, risk, forecast inflation, opportunity cost and market. The interest rate may be variable where the rate of interest to be paid on received changes either immediately or on 'rollover dates' with specified base and the major risk in the case is that cost of borrowing or returns from lending cannot be known in advance for it entire term and the business may also suffer from any adverse movement in the rate of interest. The rate of interest top be paid or received may remain fixed for the entire term of borrowing, lending or deposit and, in such a case, the risk is that the business will not benefit from any favourable changes in the rate of interest over the term of borrowing/lending/deposit. The business may also enter into forward rate agreement (FRA) where the counter parties commit to pay or receive the difference between the agreed rate of interest as per FRA and the market rate of interest on the specified date but here also the business cannot be sure that it will be making or receiving the payments on the settlement date,

(iv) Currency Risk-The business having foreign branches or engaged in foreign trade may face the risk of movement in the exchange rate. This may affect the value of assets and amount of liabilities. known as balance sheet risk, sales revenue and costs, known as revenue risk. In case the business expects receiving some overseas currency payments but not sure about its timing it may resort to overseas currency borrowings. In case the anticipated overseas currency payment is not received, the business may have to buy currency at spot rate to clear the deft and may suffer due to ad- verse movement in the exchange rate, since the overseas currency borrowings. There may be forward contracts about the exchange of the currency but in such situation, business may loose the opportunity of making a currency exchange gain if the exchange rate move in its favour.

CONCLUSION

The journey from traditional to dynamic business risk management has opened up exciting new dimensions in understanding and addressing risks. This shift has been driven by the evolving business landscape, characterized by rapid technological advancements, increased globalization, and a growing awareness of interconnected risks.
this study explored various emerging dimensions in business risk management. It witnessed the rise of data analytics and artificial intelligence, enabling organizations to proactively identify and mitigate risks through real-time monitoring and predictive modeling. The incorporation of big data has empowered businesses to make more informed decisions, enhancing their risk assessment capabilities.
Furthermore, the concept of risk resilience has gained prominence as organizations recognize the need to not only manage risks but also build adaptive capacities to thrive in volatile environments. This shift towards a dynamic approach to risk management involves embracing flexibility, agility, and continuous learning. It requires businesses to adopt a proactive stance, constantly scanning the external environment, and being prepared to adjust strategies and operations in response to emerging risks.

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