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RISK: A PRAGMATIC APPROACH

By Krysta Fox & Sally Mitchell-Wolf

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‘RISK’: HOW DO YOU FEEL ABOUT THIS 4-LETTER WORD?

Risk is a concept which we, as humans, have an interesting relationship with.

If you pause to contemplate it, a great many value and character judgements made in relation to individuals and circumstances where this small, four-letter word is applied, will no doubt come to mind.

In some parts of society and stages of life, risk, is condemned and seen as irresponsible or a sign of immaturity. In other instances, risk is pursued, providing excitiment and adding intensisty to experience. In some circles, ‘pushing limits’ and embracing risk is admired.

Within the corporate world, perceptions, attitudes and emotions regarding risk also vary. A very brief survey of articles addressing risk in business, suggests they fall largely into two camps.

There are those articles which consider risk in relation to decision making and assessing opportunity. Typically they pause to celebrate the ‘vision’, and ‘daring’ of certain business luminaries and discuss a ’stunning’ success of a project or investment which has retrospectively becomes viewed as the result of a ‘brilliance’ or, perhaps, ‘calculated’ risk taken by an entrepreneur or business leader.

Then there those articles of a more somber, less inspirational ilk.

Here risk is approached with acronyms, diligently classified into categories, and an at-risk-of-being-overwhelmed reader is marched through increasingly complex and theoretical analysis aimed at an almost mysterious lifesaving thing called ‘mitigation’!

> What are the things that trouble you as you're driving to work in the morning? Those are the things that are, typically, risks in your business.
>
> Brett Llewellyn
>
> - Executive Coach & Transformation Advisor

Now, this article *is* going to discuss that less inspirational type of risk, processes for its identification, assessment, and mitigation.

However, the goal is to remind readers, true to the Changeosity way, that this need not be an onerous and overwhelming process.

Further, knowing that most growing businesses manage to do so, initially, without really looking at their risks, the article draws on the depth of experience that Changeosity's Consultants have to share and includes some anecdotes which serve to emphasise the very real importance of facing that little four-letter-word and doing something about it!

Readers may also be surprised that there are also unexpected benefits which arise from embracing, rather than avoiding, a risk management process.

WHAT IS 'RISK'?

In a business context, risk is often defined in financial terms, in relation to investment decisions, financial health, profitability and ongoing solvency. But risk, particularly in a family-owned enterprise or SME, is much, much more than purely financial.

Therefore, an effective risk assessment and management approach incorporates a range or dimensions.

When approaching risk management, keeping it simple helps immensely.

Our experience has, unfortunately, included seeing some terrible situations and horror stories. They too often arise because Founders and CEOs just hadn't thought at all about the risks that they were entering into and hadn't put any real plans in place to either prevent those risks or mitigate those risks if they happened. One that comes to mind is a founder who had set up a nursery. Things had not gone well on the build side, and he hadn't really put in place any proper contracts or mitigations for if the build didn't go as fast as planned or there was overspending. To witness the stress on somebody's face when they realize that they've got themselves in so deep into a situation that they could have potentially prevented if they just thought about it in advance, you realize the importance of risk management.

For many people, when asked to think about 'risk', doing so doesn't come naturally to them. It's actually really challenging (not to mention confronting) to just be asked "What do you think would be a risk to your business?" and come up with a coherent answer!

The approach Changeosity has found most successful in the consultation process, of greatest help to the groups that we work with, is giving them a structure which we refer to as a framework. It's actually quite extensive and provides a method for systematically examining potential risk across the following dimensions:

- strategic
- financial
- operational
- regulatory, legal & compliance
- reputational
- health, safety & environmental
- quality of product/service
- organisation & employee
- technology & data
- market & competitors
- societal

One thing about risk is that the issue that you're identifying doesn't have to be something that has actually happened, or even perhaps will happen, but it's something that could happen.

Indeed, businesses are sometime lucky and continue to grow without encountering devastating risks. We believe you'll agree luck isn't a great strategy.

One of the things that often happens with SMEs is that they're daunted by the enormity of the work that they perceive they would have to do in order to analyse their risks, work out their plan of action to address their risks, and then put in place a business continuity plan.

Consequently, they don't do it.

A VERY GOOD PLACE TO START

To get started on this process Changeosity's Consultants begin by asking:

What if. . . ?

Each risk dimension is considered, guided by questions such as:

- What could be the strategic risks to the business?
- What might be the financial risks?
- What risks might we face just as a result of our operations?
- What are the health and safety risks that that could come to bear?

The next step, following identification of potential risks, generally tends to be a brain storming process.

The individuals in the group, leadership as well as others across the organization, answer a questionnaire and start to identify

> Done is better than perfect. If you can put something simple in place that at least gives you a starting point, then you are in better shape than if procrastinating, or set on achieving perfection and never actually doing anything
>
> Krysta Fox – CEO & Founder Changeosity

some of the issues and concerns that they have.

Here, the focus first is on describing what it looks like if this negative thing happens.

Then we dig a little deeper to ask:

- What would cause that to happen?
- What is either the trigger or underlying issue that could cause it to happen?

When an organisation undertakes a more advanced risk management process, risks are also described in terms of having an ‘internal’ or an ‘external’ cause.

Even for a modest scale process, this distinction can be helpful when owners and leaders of an SME start to think about how they want to address risks.

Honestly, there are some external things that you cannot possibly do anything about. Therefore, why would you spend your time and effort attempting to develop a process around them?

An eye-opening realisation came to pass early on when we started working with a successful family-owned enterprise on risk management. They had never thought about risks arising from the fact that they are a family business. The key leaders in that business all go on holidays together. Asking ‘What if…?” highlighted that, if something untoward and unexpected happened while on holidays, the potential for the whole business to basically stop because the risk for loss of all the knowledge, all the know-how, all the executive decision-making responsibility, existed.

Using the framework to do the risk exercise and the dawning realization that this really is a problem, empowered the family to make some significant changes to their delegation of authority. They also made changes to the way they enable people to access information and put a very simple business continuity plan in place.

This was so powerful for that company, and it didn’t take a lot of effort to address that particular risk. The knowledge and comfort that, if something occurred, it wouldn’t trigger an avalanche of worst-case outcomes for the company, employees and others was fairly easy to achieve.

Internal things tend to be more solvable in the short, medium and long term.

Additionally, a focus on internal causes is likely to address some of the things on an owner's mind during daily commutes, or which niggle in brief moments of late evening quiet.

RATING RISK

Analysis of the identified risks is process of asking:

- What is the impact of this thing?
- How great is the impact?

and

- What is the probability that it would actually happen?

Probability and impact are rated on a scale, which can be presented in a range of different, visual, formats.

Typically, we decide the ratings through a collaborative workshop or surveys.

It might be tempting to implement complicated formulas and scientific methods to reach probabilities and impact scores but in our experience the effort is not worth the result.

It is much better to use the experience in the room and reach a 'closer enough' answer.

Ratings for risks identified can be presented in various visual forms, including as a matrix.

If the probability is 'very low' or 'extremely low', and the impact is 'medium' then you probably don't need to do anything about it.

Or, the probability might be 'medium' and the impact on the business, if this thing happened, 'extreme'. In this case it would be something the organisation wants to really focus on dealing with.

We calculate all those risks and identify what the final risk factor is.

THE 4 'Ts'

Once the risks are identified and rated, decisions about which are to be addressed in what priority can be made. Then the naturally arising question is

How. . . ?

The 'Four T's', which readers may already be familiar with, is a sound place to begin.

In relation to each of the priority risks identified, a decision from among possibilities expressed as a continuum from **Tolerate** through **Treat**, **Transfer** or **Terminate** can be made.

If 'yes' is the answer to the question:

- Is it something that's just either inherently part of doing this business?

and

- Would the effort involved in resolving it would be too great?

the decision is likely to be to Tolerate.

Remember that tolerating is not ignoring it or sweeping it under the carpet, so to speak. Having awareness brings the capacity to keep an eye on such a risk. This is far better than to being blind to it!

In the event that it becomes necessary to do so, a decision to 'tolerate' can be reviewed in future and a different action taken.

If the decision is to Treat, then developing a plan about how to do that follows. First, the leadership team identifies an action with an 'action owner' and a 'date for completion' of that action.

Once that action is completed the process involves re-evaluation and identifying what the updated risk rating now is.

It's important to ascertain, having put the action in place, to what degree has that reduced the severity of the impact of the risk. Is that enough or are further actions needed?

Another possible pathway in response to a risk, once identified, is a decision to Transfer.

Typically, actions which follow here look like taking out insurance, or if it's a foreign currency risk, taking out certain derivatives or instruments that allow that currency risk to be managed.

> *It's important to ascertain, having put the action in place, to what degree has that reduced the severity of the impact of the risk.*

It's not only corporate sponsors of sports stars and celebrities who look at terminating a relationship to protect brand identity and reputation. Even within an SME of family-owned business, terminating a relationship to reduce a risk to reputation might be necessary.
Once, we did a risk assessment process with a client which unexpectedly identified something relating to a key stakeholder. Ongoing association with that stakeholder had the potential for a massive impact on the reputation of the business with a very likely flow-on effect of clients leaving. A decision to 'terminate' was taken. In that instance, the owners of the business bought the investor out.
Although very challenging to decide and work out how to achieve, over time, that action and creating a distance placed the business in a far better, less risky,

Perhaps the most extreme or intense decision in regard to a risk would be Terminate.

What that looks like can vary widely, depending on the nature of the risk identified, and the dimension into which it falls. It might involve ending a business or employment realtionship, outsourcing elements and functions, or even liquidating a part of the business.

Responses and solutions don't have to be perfect or complex, and something is better than nothing.

Indeed, once leadership develops the comfort and skills for thinking about risk, and understands the principles behind the framework and matrix, refining and reviewing risk management becomes easier.

HUMAN AND CULTURAL DIMENSIONS OF RISK

Each business, influenced by its sector, context and unique story will face a particular set of risks.

Experience, optimism, motivation, and personality-based aspects, which can be thought of in relation to social styles or psychometrics, can all contribute to both perception of, and position toward, risk.

Although arguments and opinions vary, (Appleman, 2019) differences in attitudes toward risk-perception and risk-taking along gender lines remains widely accepted.

In a business context, there's some interesting research out there that concludes, for example, that during the financial crisis banks in the US fared much better if they were led by a team that had more females, and particularly, where the CEO was female.

This has been attributed to gender based differences "related to information processing, diligence, conservatism, overconfidence, and risk tolerance" which influence a range of factors including decision making and exposure to risk (Palvia et al, 2014).

> "If it had been Lehman Sisters rather than Lehman Brothers, the world might well look a lot different today
>
> Christine Lagarde – IMF

Thus, using a framework for risk assessment in the way Chageosity does can facilitate recognition of such pre-dispositions and biases by owners and key stakeholders in an SME of family-owned enterprise.

This in turn is helpful in achieving a robust and balanced risk analysis and management approach.

In a multicultural context, where many SMEs feature collaborations between stakeholders from different backgrounds, it is interesting to note also that research indicates that culture, understood in Hoefsteds terms of distinctions between 'Collective' and 'Individualistic', 'Masculine' and 'Feminine' and 'Uncertainty Avoidance' can have an impact on perception of and position toward risk.

It follow that, just as collaboration and efforts to build cross-cultural awareness bring benefits in other aspects of life and business, a risk assessment process which provides for open-minded, speculative, "What if ...?" questioning involving a range of voices from within the organisation, often offers a forum for gaining different perspectives.

Perhaps the most important message for leaders is to be open to different views, indeed, encourage them.

MAINTENANCE AND MONITORING

Given that the business environment can change, it follows that risk can change. Additionally, some things can and will be missed in the process.

A risk review process, along with testing mitigation plans and sufficiently close monitoring can identify change and oversights and avoid a circumstane where a risk has manifested.

One of the functions of a properly funtioning board, be it advisory or exeutive, is to undertake regular review of the Risk Register during board meetings.

THE UPSIDE

Although what the company is usually aiming to do is analyse risks, and mitigate risks, inevitably, because they're doing such a deep dive into their business and really looking under the hood , viewing the business from such different angles is really invigorating. One outcome, which leaders often don't expect, is the risk assessment process generating a lot of improvement ideas for the business.

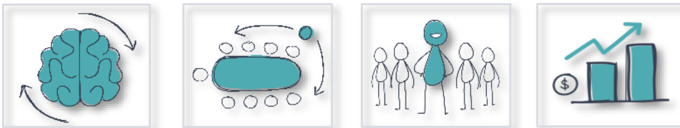
Facilitated in the right way, the process generates a lot of thinking and brainstorming. It can identify strategic initiatives that may have an impact on risk, or perhaps they actually may not.

Sometimes it's the case that they're simply continuous improvement initiatives that make the business better.

As consultants, this is the incredibly exciting aspect of risk management, and one of the things that makes such an important part of the entire strategy transformation model.

WANT TO LEARN MORE?

One advantage for an SME or family-owned business of working with an experienced mentor consultant is that many of the risks which they may face are often things that the consultant has insight into from working with other clients. That experience and a risk, especially where it is unexpected and even confronting, able to be seen through the eyes of someone outside the organisation, can lend both confidence and pragmatic advice.
If it's time you changed your approach to this 4-letter word, reach out to Changeosity, today to explore the ways in which our consultants can join and support you on your journey.



STRATEGY DEVELOPMENT

GOVERNANCE

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Keeping the risk management plan up to date can transform it from a door stop into a vital project management tool. Remember: what you don't know can kill your project.

— Bruce Pittman —

Mechanical and Aerospace Engineer NASA Ames Research Center

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