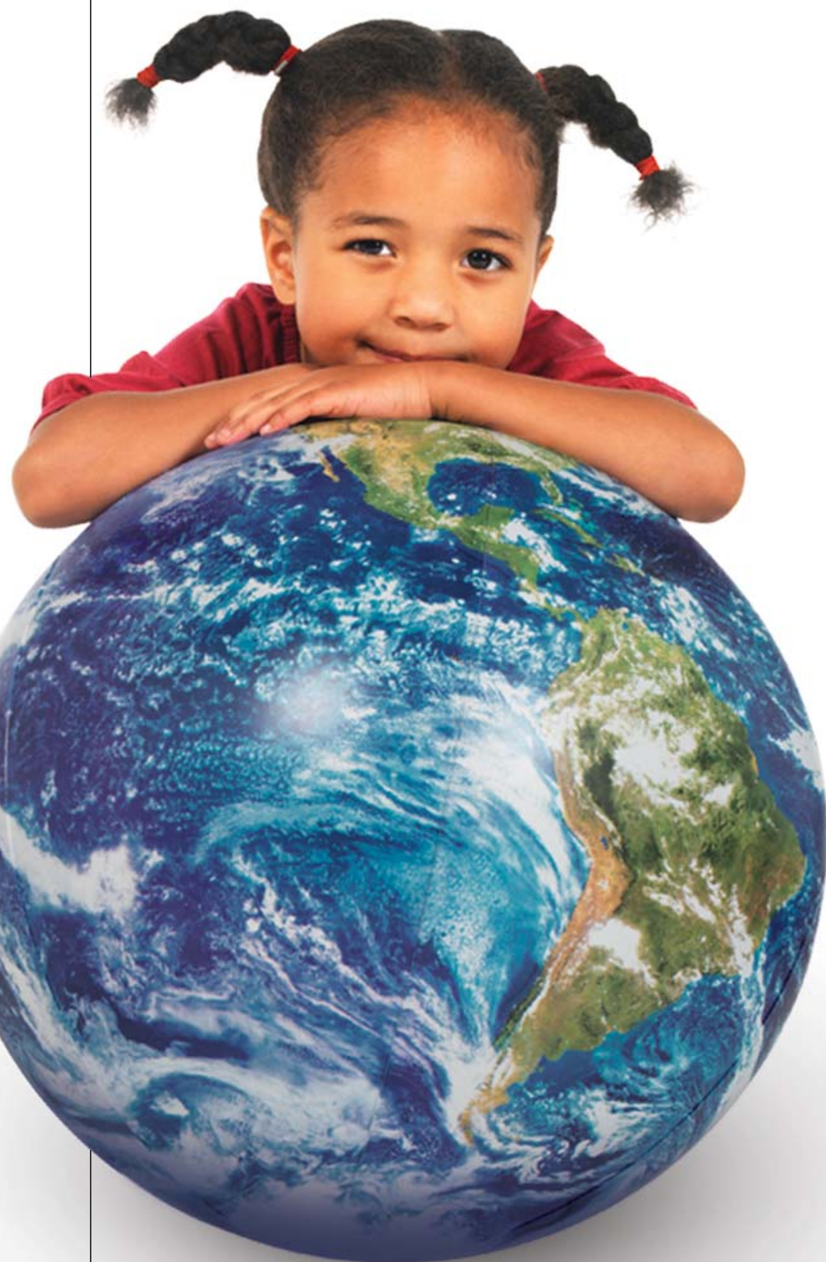
Managing Business Risk Down the Curve

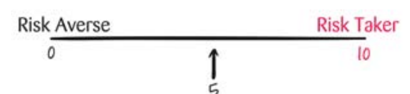
Shirlaws



The concept of Risk/Return is well understood in investment circles; the higher the risk the higher the potential return (and importantly but normally forgotten by the investor; the higher the risk the higher the potential losses). For the business manager Risk is often the "hidden variable" in many business decisions. Often the case of "cost versus return" is considered by the manager and the variable called Risk is often not discussed at the Executive Team table.

Is it possible that the Board has a measure, and that the business itself has a Business Risk Profile?

The term "Risk Profile" is also heavily used in investment circles. The Financial Adviser will often want to measure a client's Risk Profile before investing their funds. It is often a score out of 10; with zero indicating highly conservative and 10 indicating 'willing to take any bet'.



And so is it possible that a manager can have a Business Risk Profile? Is it possible that an Executive Team can score their profile? Is it possible that the

Board has a measure, and that the business itself has a Business Risk Profile? What is the likely Business Risk Profile that a CEO will carry all the way through a Raging Bull market? And what happens to that score when the market suddenly goes south into the Growling Bear? And how do you measure Business Risk profiles, and how do you manage this against Riskbased decisions in a business? Let's look at how some conflicts can show up:

The Management Team/ shareholder group:

- A CEO has a Risk Profile that is significantly different from that of his Board or key shareholder.
- A CEO and his Executive Team all hold different Risk Profiles that create conflict over management decisions; some wanting to take risks while others want to slow down and be conservative.
- A CEO's natural risk profile is different from that of the Business's as a whole, or indeed different from that needed during a phase in an economic cycle.

Client/Supplier relationships:

- The business has different risk profiles to their clients - creating conflict with sales and product development.
- The management team carries a different risk profile to suppliers - this will show up in this climate right now with some management teams wanting to aggressively grow, while their Financial supplier i.e. the Bank is conservatively not wanting to loan any further funding for growth initiatives.

More often than not what happens during a downturn economically is that the Entrepreneur/Manager reduces their Business Risk Profile without awareness. The big mistake made unfolds when the market starts to move; at this point the manager needs to aggressively start to reinvest into the business to get the uplift in the next phase of the market.

How do you measure Business Risk profiles, and how do you manage this against Riskbased decisions in a business?

But many will hold off "until the market has moved, in fear (called lower Risk Profile) that they may invest too early and not get the revenue uplifts. The language often used by the manager is "when the market improves then I will........" It is these fears that naturally evolve from the recession that ultimately holds the business back.

How do you fix this?

1. Measure the Board and entire Management Team's personal Business Risk Profiles;
2. Agree a Business Risk Profile;
3. Workshop out where the conflicts in the business are likely to show up so that you can manage these;
4. Implement a Risk Management strategy that enables the management team to measure risk on each key decision moving forward; and
5. Have the Board mandate the Business Risk Profile and Risk Management processes to ensure that all future decisions are made by looking at cost, return and business risk. ■

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