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RISK MANAGEMENT IN THE PROCESS OF THE FINANCIAL ACTIVITY OF THE CORPORATION

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Abstract

Currently, the business environment is subject to variability caused by economic and political circumstances. It sheds new light on the issue of risk management in business. The relevance of the problem is due to the fact that the presence of risk management systems as a mandatory control system is one of the main functional features of corporate structures in modern economic conditions. Significant amounts of financial and other types of resources, a wide range of territorial, sectoral areas of development cause risks of critical impact and as a consequence the probability of considerable losses. Thus, it can be noted that for corporations risk management is necessary to implement an effective management system. The purpose of the article is to develop theoretical propositions for the study of the degree of risk impact on the financial activities of the corporation, to analyze the problems and main prospective areas of development of corporate risk management systems. The leading approach to the study of this problem is the classical approach which allows to identify the methods of financial risk management. The main results of the study include working out proposals for risk management in the process of the financial activity of corporations, consideration of the features of risk management in Russia and abroad, revealing problems that hinder the development of effective risk management in the corporation financial activity, working out proposals for the formation of risk management in the corporate management system.

Keywords: Risk, corporation, risk management, financial activity.

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1. Introduction

Financial activity of a corporation is associated with many risks, the degree of influence of which on the results of its activity increases significantly in conditions of global economic instability. Risk management in corporate finance has expanded significantly over the last two decades. This expansion has led to the more complex view of the benefits of an appropriate risk management programme. The risk management literature mostly focuses on the use of derivatives, forwards, futures, swaps and options in hedging corporate risks of interest rates, exchange rates and commodity prices (Kot & Przemysaw, 2015). But the range of risk management instruments is much wider.

The dynamic development of this sphere of management in corporations is confirmed by the research data of KPMG company, according to the results the leaders of most companies consider risk management systems mainly as management tools aimed at creating the company's value. 65% of the surveyed companies have formed a separate structural unit, responsible for coordination of risk management processes which is almost two times as more as five years ago (Rykhtikova, 2018). Thus, it can be noted that for corporations' risk management is an obvious need to implement an effective management system (Hampton, 2009).

Development and implementation of an effective risk management strategy includes several steps:

1.Identification and quantification of risk exposure,

2.Developing the potential risk management tools and assessing their effectiveness,

3.Assessment of potential benefits and costs of risk management

4.Choosing and implementing a strategy.

This article mostly focuses on the basic theory of mechanisms by which risk management can increase the profitability of a corporation. This is a very important step in developing an effective corporate risk management strategy. For example, there is not a certain opinion as to how to measure the exposure of the financial activities of the corporation to risk: to direct all the energies to funds management, increasing of market value the company or maximizing a profit?

Any activity of the corporation, one way or another, exposes the existence of the corporation to risk. Managers of the corporation are not able to predict all the revenue and expenses of the corporation in the future but are able to predict them with certain degree of probability.

In its work an enterprise sets a certain goal – to receive certain income at a given level of costs, therefore, it plans its activities. But while choosing a particular development strategy, the company can lose its funds, i.e. to get an amount less than it was planned, due to the uncertainty of the situation in which the company is placed. The concept of risk is manifested in this situation (Hunjra, Niazi, & Akbar, 2011).

Effective risk management allows the organization to get significant benefits, including:

- reducing the number of sudden shock situations and unpleasant surprises;
- more efficient use of resources;
- improving the quality of services;
- reducing the amount of time, managers spend on «putting out fires»;
- increasing the probability of successful implementation of changes.

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The purpose of the author of this study is to summarize the actual data about the use of risk management tools in the financial activity of the corporation. The author tries to attract the readers' attention to the importance of this issue in the modern approach to risk management in business and to summarize the actual data about the use of risk management tools analyzing many documents, referring to a series of analyses and comparisons, based on practical knowledge in this area. The financial activities of the corporation require a precise and effective approach in the area of risk management.

In this regard, the study in the field of risk management in the financial activity of the corporation is relevant and practically meaningful for the development of an effective corporate strategy.

2. Problem Statement

A risk is an undesirable opportunity, this opportunity can be realised in the future, so the methods of analysis and risk management are based on the methods of forecasting of the corporation future development.

A risk is usually defined as the possibility of occurrence of some, more often unfavourable for the business event. This event can be both external to the business and internal, and in practice, there are many different classifications of the risk types faced by a modern company, but more often market, financial (including credit and investment), operational and other risks are mentioned. Researchers from the University of Navarra published an annual report on the revenue earned on “risk” in 88 countries. Among the results, attention should be paid to high rates in such countries as Greece (15%), Argentina (11,8%), Egypt (12,9%), the Ukraine (13,9%) (Fernandez et al., 2014).

Risk management in the corporation is an important element of an effective system of corporate management. It is defined as a set of activities and strategies that result in reducing the negative impact of different types of risks – financial, operational and strategic – on the planned results of the activities and the value created for shareholders and other stakeholders of the company (Adam, Chitru, & Golubeva, 2015).

Currently, investors are ready to take risks but continue to accumulate the capital. The rich and diverse experience has remained unchanged over the years. Thus, it is necessary to keep to the basic methods of risk management. According to the quarterly survey conducted by McKinsey company, 79% of the surveyed corporations have cut costs due to the financial crisis and only 53% of the highest-ranking authorities believe that these efforts have been a success. This suggests that many companies operating during the period of destabilisation have concentrated their efforts on reducing costs (Hoang & Ruckes, 2017).

Efficient risk management is based on the fact that while developing the strategy, the company also develops a risk management strategy. Developing a strategy, the company should specify the purpose of risk management, identify the risk, determine its scope, suggest ways to reduce it, monitor and control the risk and create a uniform risk management system. The concept of integrated risk management is often defined as enterprise risk management, and it is increasingly gaining popularity. It allows us to consider “opportunities” and “threats”, a wide dynamic range of external and internal risk factors, taking into account not only the possible losses, but also the chances (which corresponds to the paradigm of the integrated concept) (Kim & Chance, 2018). Moreover, this concept forms the basis for creating a dynamic

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risk profile of the company, allows you to specify and update the strategy of the company and the main risks associated with its implementation. The overview of corporate risk management, awareness of the presence of risk in international business are deeply rooted in the minds of top managers. The purpose of risk management is to manage a risk rather than to eliminate it. This approach determines the need to develop a detailed methodology and adapt it for organisational decisions. Monitoring the effectiveness of risk management system should include the following element: - precise definition of the risk structure. Identification is among many risks, the purpose of this process is to discover the most important risks by answering the question: What are the main risks that can hinder the achievement of the company’s goals (Beans, 2010)? It is recommended to create interdisciplinary teams at different levels of the organisation during the risk review in deeper perspective; - This is the explanation of risk management rules. It is extremely important to make sure that the strategic procedures are complete and are implemented quickly, because during the annual analysis the following elements are evaluated: risk management in the previous period and its change in the analysed period; significant changes that have occurred in the previous period, control of risk management by its control committees and its audit, external consultants and rating agencies (Brzeziski, 2011).

Further in the article we will consider risk management in Russia and in the West. Most Russian managers still associate the word “risks” only with the word “insurance”. However, managers are little by little abandoning the traditional approach for our country to minimize the risk of economic activity by occasional insurance of some types of property. Along with the development of corporate management in the USA, UK, Germany and other European countries, which has been “pushed” recently and impressively by major scandals in such companies as Enron, WorldCom and Parmalat, the concept of risk management culture is gradually entering corporate life. This concept is associated with the so-called best practice (best practice), which is effectively popularised by market regulators in the United Kingdom, and with the concept of an integrated risk management system, which has long been enshrined in German legislation (KonTrag). Russian business leaders are also interested in creating complex risk management systems which approximate to the risk management systems of large credit institutions. Many companies employ Risk Director (chief risk officer - CRO), an executive responsible for business risks (Hoyt & Liebenberg, 2011).

At present the modern development of management depends directly on the shocks of the world economy, political trends, rapid development of innovative achievements. The need to form a corporate strategy of diversification is one of the most relevant and popular concepts of corporate strategic management today. Thus, large corporations are very likely to choose a course of diversification, having all the reasons for this, and it is the most profitable option for investing and minimising the degree of risk (Bruce, 2014).

Considering the need for diversification of any large company, it is worth pointing out the important role of the depth of corporate management penetration which determines the goals which will have a priority. At the same time the level of depth is determined by the ability to assess and make unconventional decisions. At the same time the goal-setting process, organised by top management in every corporation and in every industry, is implemented with its original data, i.e. in its fixed conditions which are likely to be individual. As a rule, the main purpose of determining the need for diversification

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is how much it will affect the increase in the level of profit and efficiency of the organisation as a whole. But it should be noted that the goals of diversification of production also directly depend on having the necessary set of strategic potential: financial security, production capacity, key competencies (Dima, Man, Grabara, & Ciurea, 2010).

The implementation of diversification strategy in each case can be justified, first of all, by the distribution of risk between different types of economic activity, the correct and timely management of processes. Large companies have a clear set of goals and rigid centralisation of business processes does not always allow them to show greater freedom of choice without assessing all the risks. Conservative top managers, adherents of the first group of reasons for the transition to the diversification, are the supporters of clear signs of the production stagnation. If the corporation achieves the set goals, the possibility of diversification is not accepted or even considered. An example would be a situation when top managers have experience in only one industry or an organisation. The above-mentioned means that the economic benefits for the corporation form the basis for further thought of diversification implementation. The increased competition, weakening the impact of crisis factors, the exchange of innovations, reducing the risks and costs of the main type of the business, as well as political changes and challenges, facing the industry, are active drivers in this case. As a result, it is now popular in many corporations.

Effective risk management is considered as a leading competitive advantage that determines the survival and success of the company in the uncertainty of global environment.

Thus, the purpose of this research is to study the degree of risk impact on the financial activity of the corporation.

3. Research Questions

What does risk management in the corporation financial activity represent nowadays? How are risks managed in Russia and in the West? What effective tools are used for this?

4. Purpose of the Study

The objectives of the study are:

To study the impact of risks on the financial activity of the corporation.

To summarise the actual data about the use of risk management tools in the corporation financial activity.

5. Research Methods

To achieve the objective of the study, such methods as analysis, synthesis and logical deduction, facts from scientific and professional publications, periodicals and non-periodicals are used.

6. Findings

The article states that currently, due to the volatility of financial markets, the business environment changes every time. An organisation operating in international markets cannot function effectively and be

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competitive in continuous recalculation of risk. Companies are beginning to treat risk management as a regular part of the corporation policy (Tao & Hutchinson, 2013; Heywood, Layton, & Penttinen, 2010).

To manage an organisation effectively, corporations, especially those operating on different continents, in different social, political and legal environment develop specific mechanisms and tools to assess the effectiveness of risk management. Identifying and assessing risks that can prevent the company from achieving its goals, allow to determine the ways of risk management and, thus, to build a risk reduction strategy. Determining the level of individual risks makes it possible for politicians to make decisions within the limits of legal and economic risks, without the risk of negative impact on the stability of the company.

7. Conclusion

This article presents the results of a small risk management study. Summarising the above mentioned, it can be noted that organisations have to develop and adapt to remain competitive in today's dynamically changing world. Not all organisations need to manage risks in the same format. It is necessary to take into account the environment of the organisation, the size, the activity profile when implementing risk management.

Analysis and generalisation of Russian and foreign experience in risk management allows us to propose the following sequence of risk management formation in the corporate management system:

- identification of risks, preparation of risk maps (determining technical directions of the company activities which are at risk);
- determining critical risks (risks of destructive nature);
- developing risk management strategies.

Organisational mechanisms to minimise risks:

- restructuring of a commercial organisation;
- mandatory risk insurance.

Budgeting of risk management system:

- determining (forecasting) economic benefits from the functioning of the system;
- risk management;
- creation of reserves to cover losses.

In conclusion we briefly formulate the features of risk management in conditions of new industrialisation:

- it is recommended to form a risk portfolio of a certain corporation which is characterised by:
- values which are under threat;
- the dangers that can cause the loss of these values;
- financial consequences of loss of values.

In addition, the results showed that in practice the identification and comparison of risks in corporations can help in the implementation of corporate risk management. It is due to the fact that consistent assessment of risks that an organisation may face helps it to avoid threats as they appear, before they appear and when they are managed. Therefore, risk management is an integral part of the organisation, as it ensures that there is a good corporate management practice that is designed to

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encourage the organisation to be more efficient in terms of revenue, profitability and reputation or an image.

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