



Evaluation and Management of Risk Situations

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ABSTRACT

Risk management and crisis management are essential aspects for the survival and success of organizations in a volatile environment. By identifying, evaluating, and efficiently managing risks, organizations can minimize the negative impact on their activities. In the light of a proactive and integrated approach, investments in technology and human resources become priorities for adapting to changes in the business environment. Open and transparent communication, collaboration between departments, and involvement of all members of the organization are crucial for coordinating and effectively implementing risk and crisis management strategies. Adopting an organizational culture focused on prevention and anticipation can transform risks into opportunities for development and continuous improvement. Continuing investments in organizational capabilities, improving communication, and engaging with stakeholders are necessary for effective crisis management.

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1. Introduction

Risk management aims primarily at facilitating and understanding the risks to which a society is exposed. Risks are analyzed in terms of the moment in relation to the event. For this reason, in economic theory, there are two types of goals: pre-event (before the risk materializes), when the aim is to avoid the occurrence of the risk; post-event (the risk has already materialized), when the aim is to ensure business continuity and the survival of the society.

Risk management encompasses all relevant scenarios related to highlighting a gain or loss. This aspect refers to a precautionary stance and belief in the probability of a risk materializing. Based on this aspect, a relevant decision is made to eliminate or minimize damages. Thus, the process of identification evolves into risk management, which outlines an analysis and response to potential occurrences within an organization, within an informational system. An example would be that when all attention is focused on information security, it is referred to as security risk management. In general, effective risk management is discussed as an opportunity to expand organizations' market segments, enhance corporate reputation, save money, and build important relationships.

2. Literature review

The primary advantage of risk in management programs is economic efficiency. Company directors are aware of any issues to which the organization is exposed and manage them appropriately so that they do not materialize. There is a strong concern for defining this type of management. Definitions vary, emphasizing one aspect or another in critical situations for managers. The U.S. Public Affairs Council defines risk management as a solution used in various scenarios by companies. For this reason, to increase their knowledge in the field of public policy-making processes and to increase the level of complexity and effectiveness, there is a need for significant involvement in this process. R. A. Bucholz defines "public policy as a concrete action undertaken collectively by society or a legitimate representative of society, aimed at solving a certain problem of public interest, reflecting the interests of society or a certain segment of society".

For Barry Jones and W. Howard Chase, they characterize "risk management as a tool that companies should use to identify, analyze, and manage emerging risks and react to them before they become public information," while for Kerry Tucker and Glen Broom, they assert that "it is the managerial process whose purpose is to help maintain markets, reduce risk, create opportunities, and manage the image (the corporate reputation) as an asset of the organization, for the benefit of both the organization and its key stakeholders".

3. Research methodology

The skepticism of authors Michael Regester and Judy Larkin is related to several aspects, such as the situation of financial risk, the weak connection between risk management and the outcome. In this case, long-term risk management may yield profits, but short-term risk management results are uncertain. Communication during risk situations is just one of the tools used, along with research, corporate planning, change management, and media activities. The diversity shown in this type of management makes defining and evaluating it independently difficult, especially since people involved in risk management come from various backgrounds, including not only public relations but also law, analysis, research, etc. The characteristics and competencies of the working group include: decision-making experience, resource allocation, plan implementation control; access to information for decision-making, easy access to scheduling meetings and creating an information network, the ability to combine skills with decision-making and quick action; producing a minimum number of documents to avoid bureaucracy and information leakage.

Representatives from the working group have a series of responsibilities in the core activity field, such as data observation or analysis, establishing a network of opinion leaders, defining/authorizing studies, presenting data at symposiums, meetings, workshops, administrative working groups, etc. Those in the administrative field predominantly deal with authorities for data delivery, situation/monitoring of approvals/authorizations, analysis/evaluation of approval processes. Legal representatives focus on planning and impact assessment, defining obligation-related consequences, and reviewing strategy through legal counseling. The marketing domain supports information and sales agent training through product education for agents, competitive analysis, and addressing sales and marketing support center locations and materials. Communication domain representatives establish media contacts and gather information by preparing for media relations, documentation for briefings and media workshops, drafting and disseminating articles in the press, and supporting risk communication.

4. Findings and Discussion

In a synthetic sense, problem management consists of "the process of identifying the problems faced by an organization and managing the organizational activities dedicated to these problems". It must be perceived and realized in close interdependence with crisis management. Moreover, due to its proactive nature, stemming from the fact that problems are anticipated and addressed before they escalate into crises, problem management is considered the first and most potent weapon against crisis situations. One of the important activities specific to this management approach in problem control is a research function aimed at identifying and monitoring developments and events that could worsen, evolving into crisis situations. Primarily, considering the definition of the Problem Management Council, this managerial endeavor consists either of meeting the expectations of relevant publics or adequately educating these expectations. For example, if there are customer complaints about a product, the manufacturing company can either modify the product so that the reasons for the complaints disappear or educate its customers about the reasons the product has those characteristics (features enabled by new technologies, new trends in the field, new raw materials with better properties, etc.). Regarding this educational aspect, it must be specified that problem management completely excludes the temptation to manipulate public expectations. On the contrary, it should demonstrate the organization's willingness to respond to public expectations, a measure by which it assumes social responsibilities.

Additionally, it is noteworthy that problem management is not limited to communication or public relations activities but has a broader scope, ranging from organizational activities to financial measures. However, in most cases, it also includes public relations activities aimed at facilitating agreement on the organization's policies, actions, products, and commitments with public expectations. Moreover, one of the essential objectives of problem management is to reserve or even strengthen the organization's reputation, an objective that can be achieved primarily through specific public relations actions. To be successful, problem management must start from the idea that the organization must be concerned about the social consequences of its actions. Therefore, it should be oriented especially toward collaborating with relevant publics to address identified problems, rather than focusing on attempts to influence the public regarding how they perceive the issues.

W. Timothy Coombs regards crisis management as a continuous process. In his conception, crises occur frequently, and no organization is immune to crises; therefore, all organizations must learn as much as possible about crisis management. In this context, defining crisis management is particularly important because how we define a subject indicates how we will approach it. Coombs' definition specifies that "crisis management consists of a set of factors designed to combat crises and reduce crisis damages". Analyzing this aspect, we can affirm that crisis management is a proactive/reactive/interactive tool.

M. Nudell and N. Antokol emphasize the anticipatory nature of crisis management. From their point of view, crisis management involves a set of anticipatory measures that allow the organization to coordinate its responses to a crisis. The organization can achieve maximum benefits through effective crisis management that maximizes opportunities and reduces dangers.

The crisis management plan developed by Combalbert contains a list of crisis team members and their replacements. Another important element is a map of all crisis situations considered, as well as a detailed description of response and action plans. Another element of the plan is the description of business continuity and a description of the crisis team and its functioning. At the core of the plan is the organization of the crisis management room and a documentary with available internal and external resources. The schema reveals how risks that can lead to crises are perceived, their accurate perception based on the analysis of all available information to the organization, the attitude towards these risks, from the perspective of consciousness, decision-making, and measures depending on the management's ability to manage risks and crises. Superficial analyses and ignoring some consciousness, from their evolution perspective, can surprise the organization and can have extremely negative consequences in many situations. Potential risks should never be dismissed except after thorough and comprehensive analyses of all factors involved in their emergence and evolution. The flip side to effective decisions followed by effective specific measures, which make crisis avoidance possible, is the inability to make effective decisions, making a crisis almost imminent. Therefore, in the current period, specialization and professionalization of organizational structures analyzing risk factors, their evolution in the organizational and extra-organizational environment, and making decisions to prevent crises are imperative. M. Nudell and N. Antokol, analyzing various crisis management approaches by organizations, highlight the major elements that could guarantee the success of crisis management, such as: leadership involvement in the development of strategies and crisis management plans, identifying dangers and opportunities (pre-planned scenarios allow for the rapid recognition of significant dimensions of dangers), defining response forms; creating a conducive working environment for the crisis management team, limiting damages (material damages, damages related to image and reputation), crisis resolution; returning to normalcy (defining steps and measures necessary to resume normal activity rhythm); avoiding event repetition.

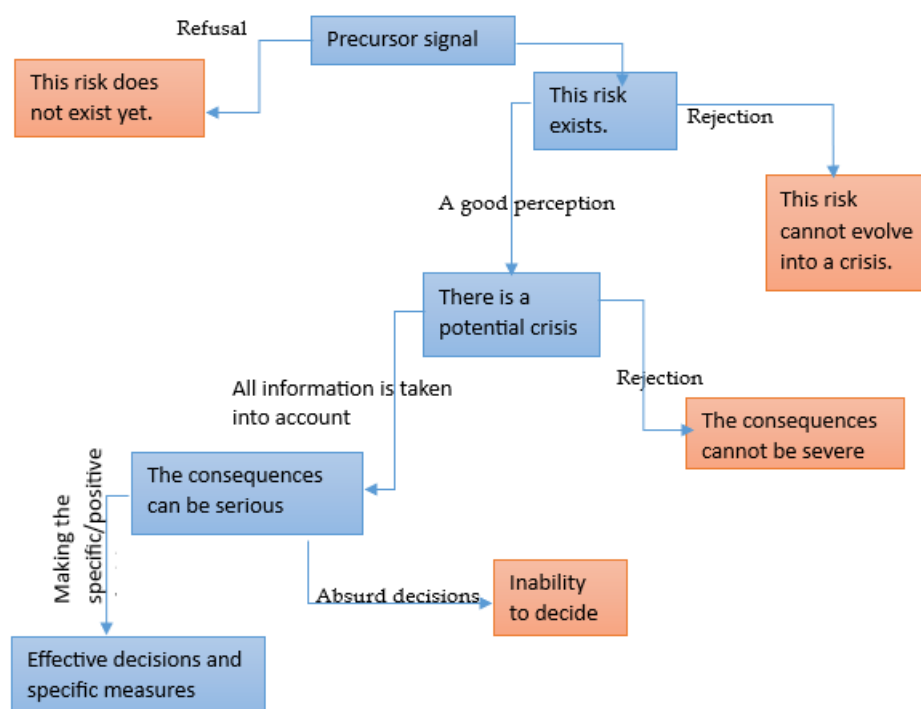


Figure 1.1 Evolution of Risk into Crisis Schema

Source: Created by the author based on research developed by L. Combalbert

Since we are in a critical period, to manage the crisis situation easily, banks in Romania are supervised by the ECB to increase profitability and reduce the crisis state. As a result of the Russo-Ukrainian war, banking institutions under banking supervision have shown very strong resistance. In 2022, global economic growth recorded a decline to 3.4%, compared to the level of 6.4% recorded in 2021. This decrease was influenced by factors such as geopolitical conflicts generating global uncertainty. Additionally, inflation has experienced an increase, and financial conditions have tightened. This decline has been felt across all economies, whether developed or emerging.

(annual percentage changes)

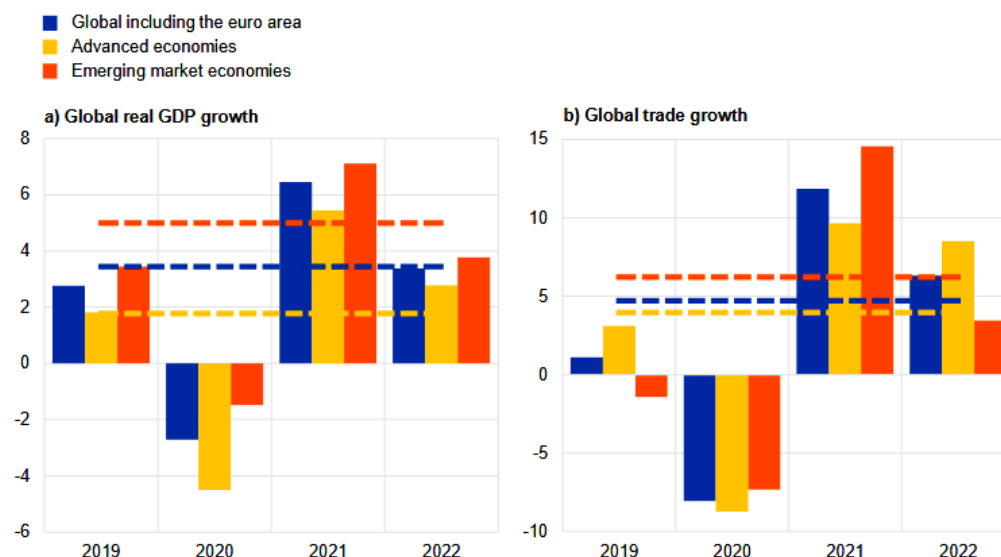


Chart 1.1 Global GDP and International Trade Flows

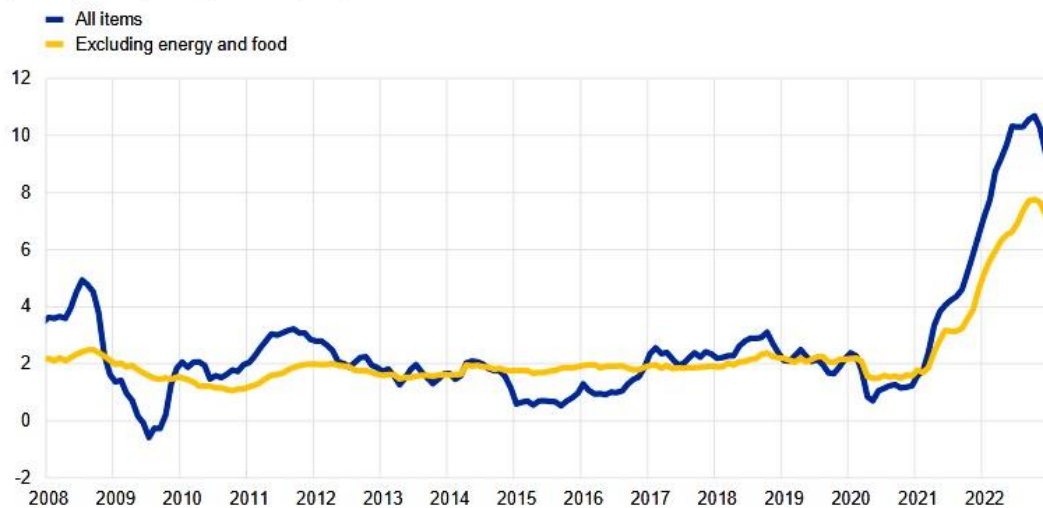
Source: Adapted from ECB, available online at <https://www.ecb.europa.eu/pub/annual/html/ecb.ar2022~8ae51d163b.ro.html#toc4>, accessed on 05.02.2024

This deceleration occurred after a strong recovery period in 2021, primarily driven by the easing of pandemic restrictions and increased global demand. The beginning of 2022 was marked by a major impact on the global economy caused by the conflict in Ukraine. This led to significant volatility in commodity prices and affected food security, especially in emerging countries. The rise in energy and food prices exacerbated global inflationary pressures, reducing disposable incomes for households and prompting central banks to adopt restrictive monetary policies. Against the backdrop of rising interest rates, declining capital markets, and increased risk aversion, global financial conditions tightened significantly.

During 2022, the dynamics of international trade experienced a decline but remained above the historical average. This decline was largely attributed to modest activity in the manufacturing sector. In the first part of the year, international trade maintained some resilience, although the effects of the war in Ukraine and persistent issues related to global supply were partially offset by the recovery of tourism and transportation services amid the relaxation of pandemic restrictions. However, in the latter part of the year, international trade experienced a significant slowdown, with a focus on declining imports from emerging economies. Since the global financial crisis, integration into global value chains has stagnated, and the pandemic and geopolitical changes have prompted businesses to reassess their strategies, including reshoring domestic production and diversifying suppliers. This trend could lead to a fragmentation of global value-added chains in the future.

In 2022, global inflationary pressures recorded a significant increase, reflected in both total inflation measures and those excluding energy and food products. These pressures were fueled by high and volatile commodity prices, global supply bottlenecks, prolonged effects of the economic reopening after the pandemic, and restrictive conditions in labor markets. In OECD member countries, the inflation rate reached 10.7% in October before starting to decline. At the same time, inflation excluding energy and food products reached 7.8% in the same month. The significant inflation increase in the first part of the year in most countries was primarily driven by rising commodity prices. Subsequently, the rise in inflation excluding energy and food products indicated a generalization of inflationary pressures in both developed and emerging economies. Inflationary pressures on core inflation were also fueled by intensified wage pressures, as labor market conditions in major developed economies remained tight despite the global economic slowdown.

(annual percentage changes, monthly data)



Graph 1.2 Inflation Rates in OECD Countries

Source: Adapted from ECB, available online at <https://www.ecb.europa.eu/pub/annual/html/ecb.ar2022~8ae51d163b.ro.html#toc4>, accessed on 05.02.2024

Prices of energy products experienced a significant increase during the year 2022 but saw a slight decline towards the end of it. Oil prices registered a 6% increase, mainly due to supply chain blockages, especially following Russia's invasion of Ukraine, leading to a strong price surge in the spring of 2022. Supply blockages in oil were partially offset by a decrease in demand, as a result of the global economic growth slowdown and isolation measures in China.

The invasion of Ukraine and the reduction in gas deliveries to Europe led to unprecedented increases in gas prices on European markets, with an increase of over 240% from the beginning of the year immediately after the conflict erupted. This significant rise in natural gas prices significantly influenced energy product prices in Europe, contributing to the rise in wholesale energy market prices. Natural gas prices slowed down in the last quarter, due to increased imports of liquefied natural gas (LNG) and gas-saving measures, which led to high stocks accumulation in the EU at the beginning of the cold season. Thus, by the end of 2022, natural gas prices largely stabilized at pre-invasion levels but were about 14% higher than at the beginning of the year.

Following the analysis conducted by the ECB on banks in Romania, we can state that starting from 2020, the country has been subjected to severe risks such as the COVID-19 pandemic and the conflict between Russia and Ukraine. Another significant impact was the depreciation of the euro against the US dollar, which recorded a higher degree of stability. In 2022, the euro depreciated by 6% against the US dollar, but registered a higher degree of stability in nominal effective terms (+0.8%), despite significant fluctuations throughout the year. The US dollar appreciated against most other currencies, amid tighter monetary policy by the Federal Reserve System and reduced global risk sentiment. The euro came under pressure due to high energy prices and the deteriorating economic outlook in the euro area. However, the euro appreciated against other major currencies, including the British pound, Japanese yen, and Chinese renminbi.

At the end of 2022, the main risks to global economic growth prospects included more severe repercussions of the conflict in Ukraine, contagion effects caused by the significant slowdown in the Chinese economy, and tighter financial conditions due to the rapid withdrawal of monetary stimulus in major advanced economies. There are concerns that these conditions could lead to more significant capital outflows from emerging economies, causing dysfunctions in financial markets. Also, international commodity markets remain sensitive to supply chain risks. Rising commodity prices and the spread of inflation to consumer prices could erode purchasing power and affect global demand. Additional pressures on global supply chains and increased fragmentation of the global trading system could slow economic growth and fuel inflation.

5. Conclusions and recommendations

Risk management and crisis management are crucial aspects for the survival and success of an organization in a volatile and unpredictable environment. Analyzing and managing risks, both before they occur and after they materialize, are complex and essential processes that need to be integrated into the culture and strategy of the organization. By identifying risks and adopting proactive-preventive strategies, organizations can strengthen their resilience and capacity to adapt to changes in the environment. Through risk management, organizations can identify, evaluate, and manage potential threats that could affect their objectives and performance. Additionally, crisis management involves the ability to respond quickly and efficiently to unexpected events and minimize their impact on the business and the organization's reputation.

Given that risk and crisis management require a comprehensive and integrated approach, it is vital for organizations to develop customized strategies adapted to their specificities and the environment in which they operate. Organizational leadership plays a central role in promoting a risk-oriented organizational culture focused on identifying, evaluating, and efficiently managing risks.

Crisis management plans are essential to ensure the resilience and adaptability of organizations in the face of emerging risks and challenges. It is vital for organizations to adopt a proactive approach in identifying, evaluating, and managing risks, including involving leadership in developing crisis management strategies and plans. Careful risk analysis and the adoption of effective and specific decisions can help limit damages and return to normalcy after a crisis. Furthermore, specialization and professionalization of organizational structures in risk analysis and the adoption of preventive measures are crucial for crisis prevention. In the context of the global economy, supervision and guidance of financial institutions by organizations such as the ECB are essential for maintaining stability and resilience in the banking system in the face of challenges, such as geopolitical conflicts and economic fluctuations.

Overall, the analysis presented highlights a global economic situation characterized by multiple challenges and risks from 2019 to the end of 2022. The impact of the conflict in Ukraine, inflationary pressures, slowing dynamics of international trade, and the trend towards the fragmentation of global value chains are significant aspects influencing the evolution of the global economy. These trends indicate an increased need for adaptation and resilience from economic actors, as well as a heightened importance of international cooperation for risk management and promoting sustainable economic growth. It is essential for economic policies and business strategies to be oriented towards consolidating stability and resilience in the face of uncertainties and changes in the global economic environment.

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