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Managing business risks in SMSEs

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Managing business risks in MSMEs

What we will cover….

- Perspectives on risk and opportunity
- What is different about MSME's to larger businesses
- The risk population - what are the key business risks
- Why do we need to manage business risks
- Risk assessment
- Strategies to manage and control risk
- An understanding of control components and how to adopt them for MSMEs
- Basic internal controls and reporting for MSMEs
- Strategy and planning for MSMEs
- Top 10 tips

Perceptions of risk

- "Opportunity and risk come in pairs"
  – Bangambiki Habyarimana, The Great Pearl of Wisdom

- "If you haven't had a major fail in your career or business — you aren't trying hard enough." – Sallie Krawcheck, Chair of Ellevate.

- "If you don't take risks, you'll always work for someone who does." – Nora Denzel, board director of Ericsson, AMD and Outerwall.

- Whenever you see a successful business, someone once made a courageous decision." - Peter Drucker

- "The big risks bring the big rewards. Don't be afraid to fail, instead develop a healthy fear of losing because you were afraid to take a risk." – Karen Stuckey, Senior Vice President, Softlines and General Merchandise Sourcing, Wal-Mart Stores Inc.

What is risk

- "Risk is the effect of uncertainty on objectives"
  – Definition of risk, ISO 31000
- Therefore risk can have positive impacts, not just negative
- It is not just preventing something bad from happening, but also exploiting new opportunities
- Problems always represent opportunity – the opportunity to do something better, faster, cheaper, quicker, newer than your competitors or future competitors

Is business risk different for MSME's than large corporates

- All businesses are effected by risk

Strategic risks	**Operational risks**	**People risks**
Financial risks	**Information technology**	**Compliance and legal risks**
Marketing and sales risk		**Catastrophic risk**

- What is different about MSME's
  - The owners money, wealth and reputation is at stake
  - Often involves other family members
  - Limited resources, finance, staffing, systems, know how
  - Can take a long term view of business and have different measures of success

The risk population

Strategic risks	Financial risks	Marketing and sales risks
Corporate governance risk	**Capital and financing**	**Market competition risk**
Competitive risk	Asset value risk	Sales price and margin risk
Innovation risk	Interest rate risk	Demand risk
Economic risk	**Exchange rate risk**	Sales forecast risk
Technological change	**Liquidity risk**	Product development risk
IP risk	**Credit and counter-party risk**	**Customer relationship risk**
Reputational risk	Investment risk	Brand value risk
Project and change management risk	**Fraud and error**	Publicity risk
Ethics risk	Concentration risk	Large account risk
	Tax risk	**Location risk**

The risk population

Operational risks	Information technology	People and HR risks
Infrastructure risk	**Information security risk**	**Workplace safety**
Maintenance risk	**Technology quality risk**	Employer reputation
Product failure risk	**Technology continuity risk**	Employer liability
Product liability risk	Data quality risk	Employment law compliance
Operational quality risk	Technology platform risk	**Talent management and retention**
Production shortfall risk		**Recruitment risk**
Logistic risk		Compensation and benefits
Procurement risk		Employee privacy
Climate risk		Employee fraud

The risk population

Compliance & legal risks	Catastrophic risks
Compliance risk	Fire, flood, earthquake
Mandatory reporting risk	**Force majeure**
Liability risk	**Political risk**
Regulatory and government change risk	

Why manage business risks?

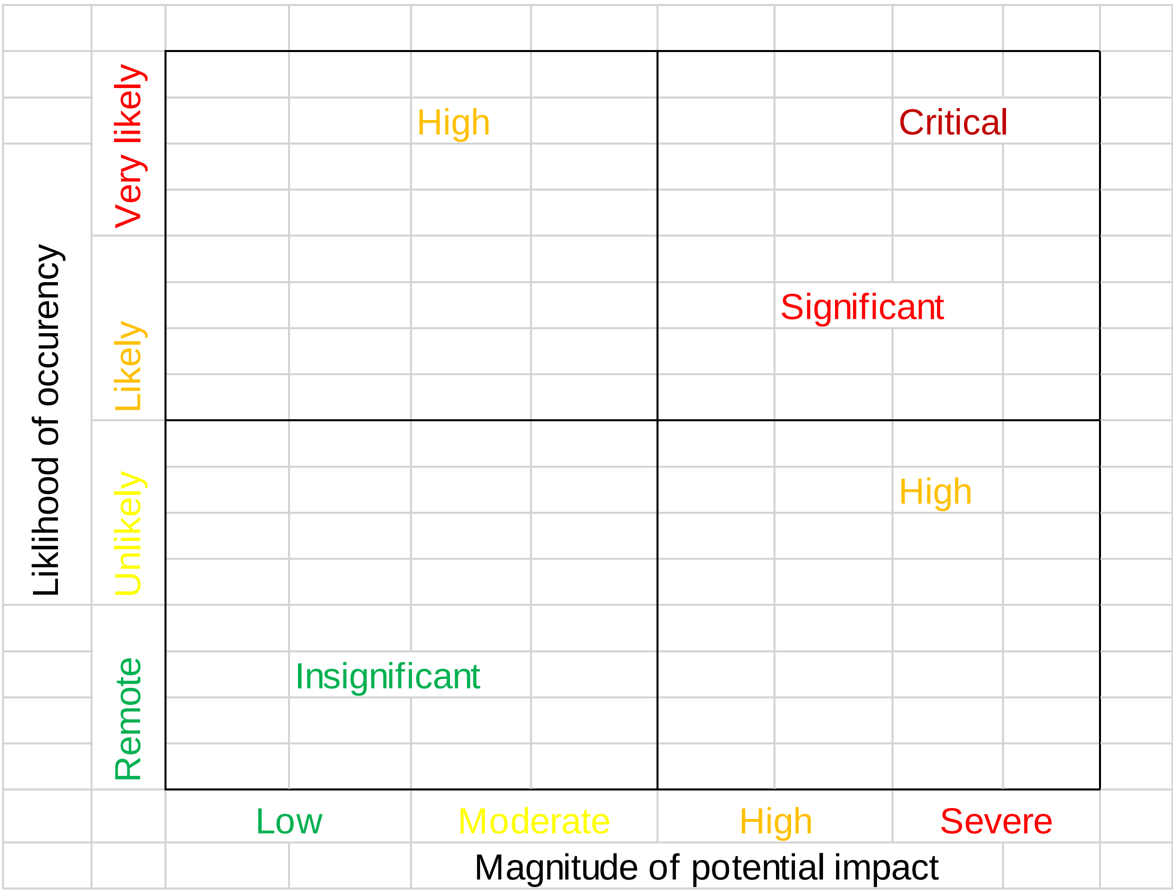
- Business needs to take risks to grow and survive in changing and challenging markets
- One person's risk is another persons opportunity
- Owners need to develop business strategies and plans to achieve their objectives
- Risk management is about identifying, understanding and prioritizing risks and then minimize, monitor and control those business risks
- Identify the risks and opportunities you may encounter in striving to achieve your objectives
- Determine the risk/reward pay off from trying to manage identified business risks and exploit opportunities
- Risk management
  – provides transparency
  - provides accountability
  - aligns risk with the business strategy
  - allows certain risks to be reduced or the potential impact mitigated
  - enables preparation for risk events
  - allows risks to be monitored and the business react accordingly
  - supports sustainability of the business

Risk assessment

- Different risks will impact on individual businesses differently
- Some are entity specific, others are related to a certain industry, geographic area, global economic conditions
- Businesses have to assess what are the most significant risks in terms of potential **magnitude of their incidence** on the business and their **likelihood of occurrence**
- Then consider what options are available to monitor, avoid, eliminate, reduce, mitigate or transfer those risks
- Analyse and understand your business – identify the critical business activities, customers, suppliers, employees, services, tangible and intangible assets
- Ask the ‘what if?’ questions – what could wrong if something bad happened or you had multipile events in a worst case scenario
- Brainstorm with your team and advisers

Risk map

- Can help in identifying those business risks that need managing

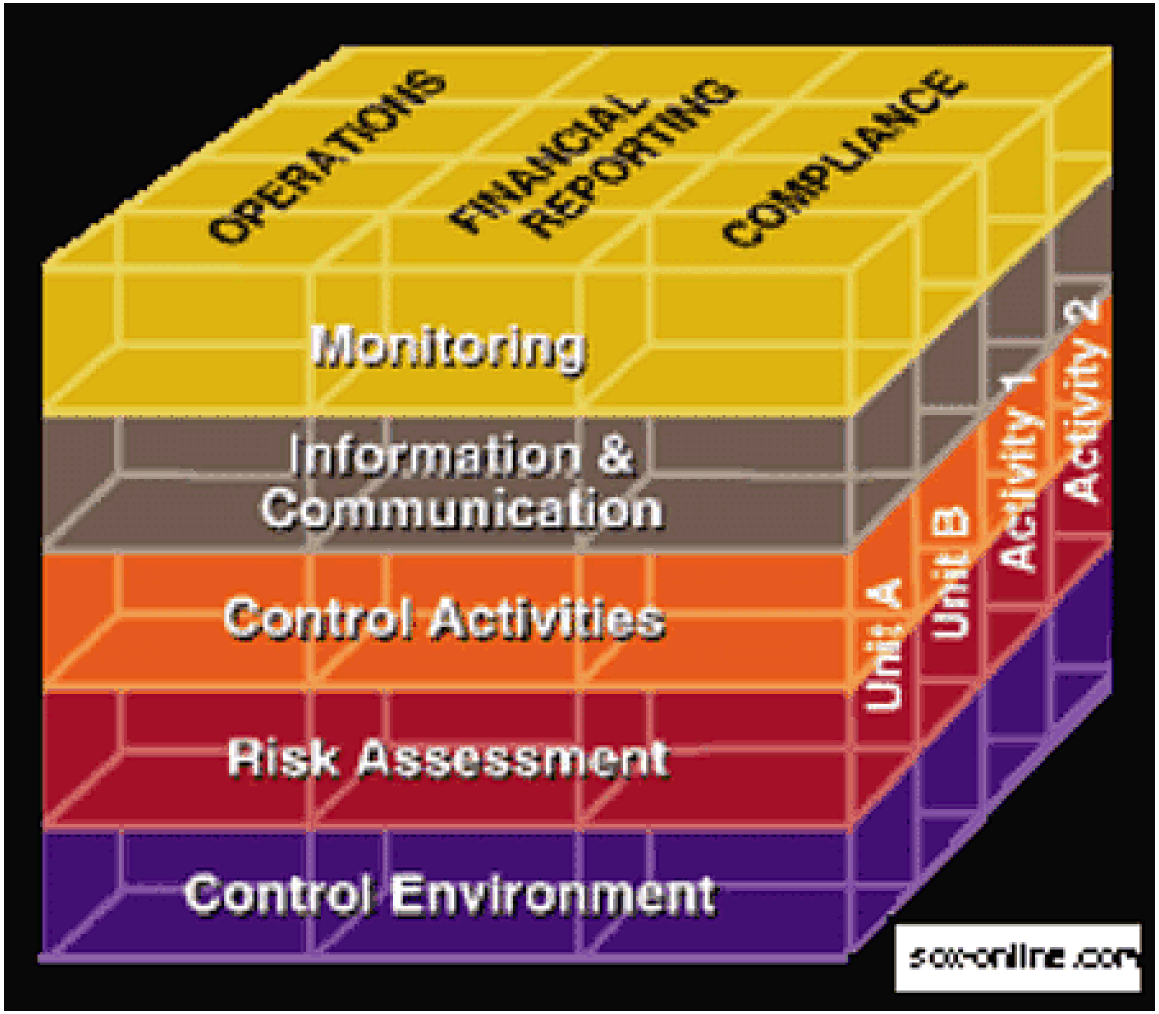


Strategies to mitigate risk

- Once you have identified your significant risks, you need to assess how you are going to manage and mitigate the potential impact
- Then consider what options are available to avoid, eliminate, reduce, mitigate or transfer those risks

  - avoid a risk by not commencing a new project
  - eliminate the risk of IT failures by having back up and duplicate recovery systems
  - reduce the risk of employee fraud through recruitment screening, code of ethics training, strong control environment, employee engagement
  - mitigate the impact of loss of a key customer by having exposure limits in place
  - transfer the risk of loss through insurance contracts
- Some risks cannot be controlled (ie climate, natural disasters, general economic conditions), but businesses can still take steps to mitigate the potential impact by proper advance planning
- PPRR risk model – Prevention, Preparedness, Response and Recovery. Particularly relevant for disaster recovery and business continuity situations

COSO controls framework



COSO control framework

Components	Principles	No. of Points of Focus
Control Environment	1. Commitment to integrity and ethical values	4
	2. Independent board of directors oversight	5
	3. Structures, reporting lines, authorities, responsibilities	3
	4. Attract, develop and retain competent people	4
	5. People held accountable for internal control	5
Risk Assessment	6. Clear objectives specified	5
	7. Risks identified to achievement of objectives	5
	8. Potential for fraud considered	4
	9. Significant changes identified and assessed	3
Control Activities	10. Control activities selected and developed	6
	11. General IT controls selected and developed	4
	12. Controls deployed through policies and procedures	6
Information & Communication	13. Quality information obtained, generated and used	5
	14. Internal control information internally communicated	4
	15. Internal control information externally communicated	5
Monitoring Activities	16. Ongoing and/or separate evaluations conducted	7
	17. Internal control deficiencies evaluated and communicated	4

Applying COSO control principles in an MSME

Control environment

- Board and management – ensure you have the right people and seek external, independent advice or feedback
- Lead by example – display appropriate ethics, competence, consistency in dealing with staff and other stakeholders
- Clear authority guidelines and reporting structures
- Recruit, train and develop good people – always do thorough reference checks

Risk assessment

- Have a business plan
- Do a SWOT analysis
- Do a heat map of your key business risks and how you are going to address them
- Ask yourself the "what if" questions

Applying COSO control principles in an MSME

Control activities

- Have an appropriate level of segregation of duties and clear authorization levels
- Implement review and approval processes for key processes
- Reconcile all your bank accounts and promptly follow up unmatched transactions – minimum monthly, preferably more frequently
- 3 way matching of orders, goods receipt and invoice prior to payment.
- Controls over completeness and accuracy of invoicing
- Reconciliation of control accounts and clearing accounts within an accounting package
- Regular stocktakes
- Credit control and monitoring /follow up of aged debts
- Reconciliation of supplier invoices
- Utilise electronic payment systems
- Controls over payroll
- Controls over data and systems

Applying COSO control principles in an MSME

Information and communication

- Ensure your accounting systems are appropriate for the business
- Consider cloud accounting solutions – cheap, easy to use, secure, current
- Produce timely monthly financial reports and other operational data relevant to decision making
- Monitor performance against expectations and hold people accountable

Monitor

- Perform regular reviews against objectives and operation of controls
- Get independent assessment and review
- Ensure compliance with statutory obligations
- Get feedback from customers and suppliers on interactions with your company and staff

Business plans for MSMEs

Now, Where, How

Our current situation:

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-
-

Our vision comprises the following key objectives:

-
-

The critical things to December 2013 are:

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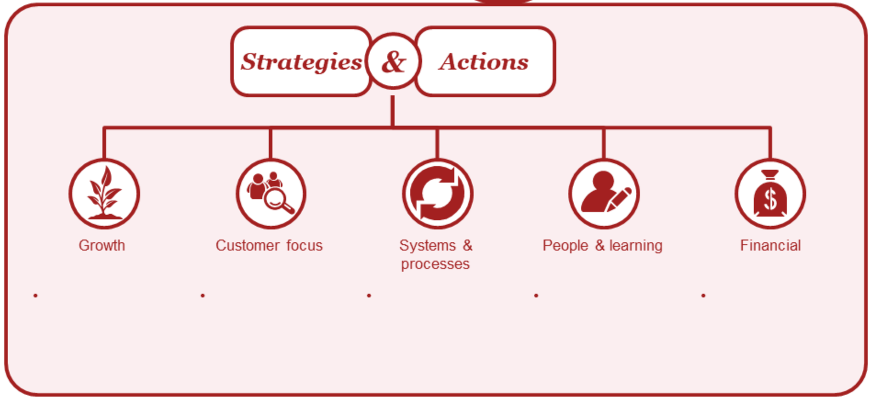
-

Key performance targets

	12-2013	06-2014	06-2015
Free cash flow trend			
Net profit per customer			
W/Cap			
Revenue			
Number of sales			



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TOP 10 tips for risk management by MSMEs

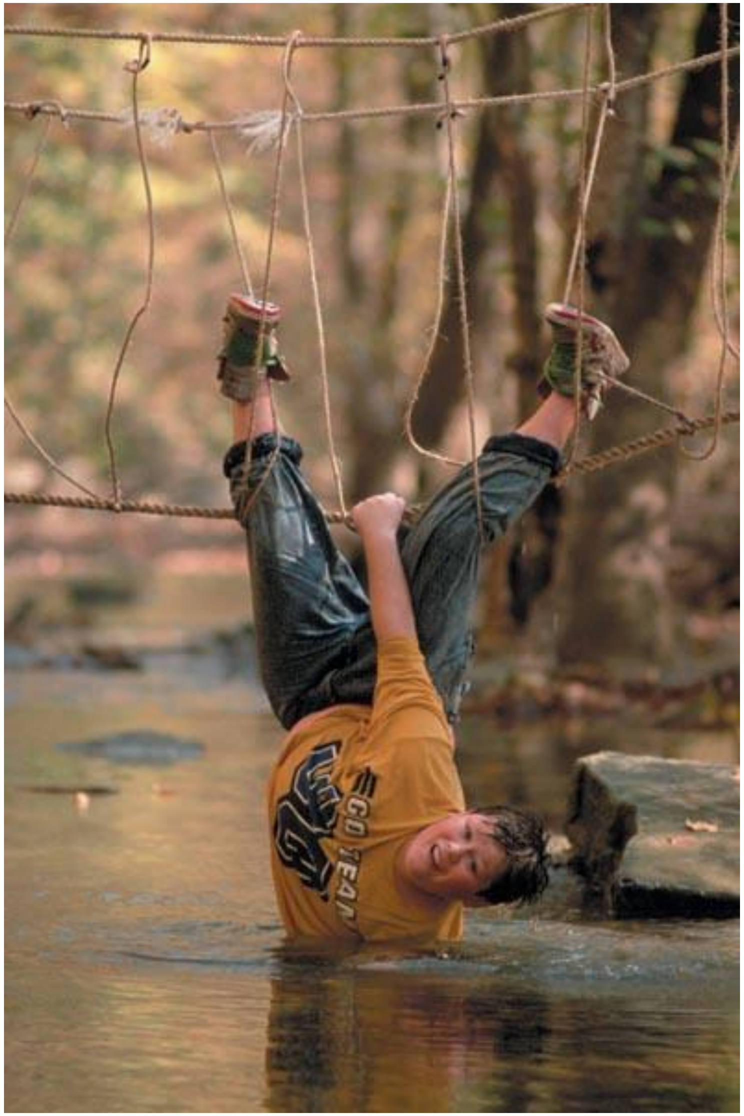
1. Understand your business risks (and opportunities) and determine what risks you are prepared to accept, avoid, transfer or mitigate and how you can best manage those risk. Always ask the "what if" questions.
2. Prepare a business plan and regularly revisit and monitor against it, and update as circumstances change
3. Ensure you have timely and reliable management information – financial and operational
4. Put in place basic internal controls over purchasing, payments, payroll, sales, receipting and inventory, and do regular monitoring.
5. Ensure you have insurance for risks you want to transfer.
6. Don't forget risks to your IT systems and data. Consider cloud storage and cloud accounting solutions.
7. Cash is king – manage and monitor you cash flow, working capital and access to finance. Keep your bankers informed and on-side.
8. Don't just delegate and forget – it is your business.

TOP 10 tips for risk management by MSMEs

9. Ensure you remain compliant with your tax and IPA requirements. It can be costly when the taxman comes knocking.

10. Separate the private from business
    - non-business expenditure
    - untaxed withdrawals
    - family and wantok involvement

There is no adventure or challenge without risk



But good risk management can keep you out of trouble!

Question time