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RISK MANAGEMENT IN INDUSTRIAL ENTERPRISE- SMEs IN CYPRUS

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Bachelor of Science in ACCOUNTING, BANKING AND FINANCE

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RISK MANAGEMENT IN INDUSTRIAL ENTERPRISE- SMEs IN CYPRUS

Dissertation

Advisor

Dr. Michailina Siakalli

Abstract

This study investigates the concept of risk management in the small and medium enterprise sector. The literature review conducted reveals the definition of the concept of risk management, its application in various areas of organizational management and its growing importance considering the rapidly evolving external business environment. The primary data collection has been conducted using quantitative data collection techniques using a questionnaire and collecting data by sending out to the owners of small and medium enterprises through emails. The data analysis has been conducted by the use of statistical and graphical representation tools of excel. The analysis of the results of the primary data collected from a sample of 100 small and medium sized enterprises in Cyprus revealed that majority of the enterprises currently in operation identified risk management as an essential organizational function in lines with production and marketing. Majority of the organizations feel that there is need for a scope of improvement of the risk management function in the Small and Medium business sector. The majority of the organizations current rely upon the insurance policies undertaken as a part of their risk management process. The Government policies implemented in the recent times have played an important role in bringing about improvement and opening up of the capital markets for the businesses operating in the small and medium business sector and thereby reduce their financial risk levels.

Keywords: RM = Risk management, SME= Small and Medium Enterprises.

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INTRODUCTION

With the high degree of uncertainty involved for organizations operating in the given business and economic environment coupled with a number of unforeseen operational events, most managers would agree to the growing importance of risk management required at the enterprise level. Risk management, historically has revolved around the health and safety risks involved in the heavy industrial and manufacturing organizations wherein corporate focused upon the formation of a list of risks, its classification, and steps taken for the purpose of risk mitigation. However, nowadays there exists a need for the organizations to expand the scope of the risk management done within the organization extending it beyond just the measures taken to minimize the safety and health risks associated with the operations of a company (Verbano, 2013).

Thus, in today's economic environment and in times of crisis, companies are required to monitor their current costs as well as future expenses that might be incurred by an organization due to unforeseen events. It is required that managers understand that a degree of risk is involved in each and every activity undertaken by the organization. Thus it is of essential importance that managers understand and possess the knowledge required for the purpose of identifying the potential risks, recognizing the scale of measurement, devising steps for mitigation of risks, and ensuring monitoring and follow up of the risk management programmes implemented. Risk management is therefore essential for the purpose of guaranteeing the survival of companies in the long run and enables them to generate sustainable value for the stakeholders of the organization (Alquier, 2006)

It especially holds true for the small and medium sized enterprise and the entire SME (Small and Medium Enterprise) sector as they tend to be the most exposed to the harmful effects of unmanaged risk taking as they tend to have access to limited resources and organizational structure features available to support risk management. This is one of the reasons as to why the chosen area for conducting of the thesis for this paper has been small and medium sized enterprises. SME's tend to require larger amount of time to respond to internal and external threats because of lack of sufficient resources which may eventually lead to large potential losses for the organization and thereby pose a threat on their survival in the long run.

Another factor contributing towards the choice of the area of conducting studies in risk management within the SME sector is the rise in the number of startups that are built upon innovative ideas and involve decision making with a great degree of risk involved with it. Thus, organizations should be equipped to detect and manage the project related risks in order to be able to carry out innovative projects successfully and enable its implementation at all stages (Altman, 2007).

The choice behind focusing upon the scope of risk management in the SME sector was also driven by the growing number of small and medium sized enterprises all over the world with these enterprises playing a very important role in the society from the social and economic point of view. Statistics reveal that in Europe 99.8% of the total companies operating belongs to the SME sector which currently employs 67.4% of the total work force and generates revenue and goods and services comprising 58.1% of the total gross value added (edinburgh, 2014). Moreover, the paper shall focus upon the growing SME sector in Cyprus in which 99.9% of the companies employ workers which are less than 250 in number along with the overwhelming majority of 95% of all the operating organizations having a total workforce of less than 10 persons (edinburgh, 2014). Thus, it is a market clearly characterized and dominated by the SME sector which would make the analysis of the risk management of SMEs in the given area interesting and useful. Currently, the Government of Cyprus has been implementing policies that are conducive to the creation of enterprise and innovation driven entrepreneurial climate. It is adopting policies to promote competitiveness in all areas of economic activity. Therefore, the analysis of risk management and appropriate framework as well as identifying the determinant risk factors shall enable small and medium sized enterprises with limited resources to deal with unknown threats and business environment risks in a more efficient and prompt manner in order to survive in the highly competitive and rapidly changing business environment as well as make organizations operationally more flexible to adapt to change in a much quicker fashion (mcit.gov, 2015).

For the purpose of conducting the research, both primary and secondary sources of data shall be utilized in order to collect data for the purpose of analysis and drawing of appropriate conclusions. The secondary data sources shall include review of journal articles upon risk

management in small and medium enterprises as well as specific characteristics of the SME sector in Cyprus which makes it separate from the rest of the world. This shall help in establishment of a foundational base for the research. The primary data collection shall involve an investigative study through the use of quantitative data collection techniques such as a survey conducted upon the SME sector of Cyprus with the help of a consisting of a set of questions relating the current risk management programme being implemented in the organizations. It will focus upon the areas that require improvement in order to bring about operational efficiency and quicker decision making considering less chance of failure. The questionnaires shall be directed towards the owners and managers of the SMEs that are currently operating in Cyprus and shall be emailed to them along with a detailed email explaining the purpose of the research and ensuring confidentiality. The primary data collected through the survey will then be organized and subject to analysis which shall include graphical representations of the data in order to gain information from the primary source and draw meaningful conclusions (Arnold, 1999).

RESEARCH AIM AND OBJECTIVES

The purpose of conducting the given research has been summarized below:

- to understand the growing importance of risk management in the business sector
- identifying unique characteristics of the small and medium enterprise sector
- identifying the risk factors for the small and medium sized enterprise
- discussing the areas in which SMEs implement risk management and controls and the areas that require improvement

CHAPTER 1: LITERATURE REVIEW

This Section of the research involves review of journal articles and other forms of secondary sources of data relating to research management and characteristics of small and medium sized enterprises. The purpose of the literature review shall be to develop a foundation for the understanding of the give topic and provide information to facilitate the primary data analysis.

RISK MANAGEMENT

One of the earliest definitions of risk can be identified from the year 1738 which was described by Bernoulli who had proposed that the risk be measured by a geometric mean and then be spread across a set of independent events. The traditional definition of the term risk involves measurement made across two variables which are the frequency with which the risky event occurs i.e. determining the number of times the risky event takes place over a specified period of time and the extent of the magnitude or consequences of the occurrence of the risky events that is considering results of all risky events (Arnold, 1999).

As per authors Chapman and Cooper (1983) risk can be understood as the possibility of incurring financial, economic or physical/ material loss due to the inherent assumption of uncertainty associated with proposed action to be taken (Verbano, 2013).

The earlier definitions of the term risk reflected only the negative effects associated with the occurrence of a risky event. However, later definitions identified the relation to the term risk in management literature and considered both the possibility of positive and negative consequences of occurrence of a risky event which has an impact upon the operational, strategic and financial objectives of an organization (Verbano, 2013).

In order to take into consideration the magnitude and complexity of the kinds of risks that is faced by companies and other organizations all over the world, scholars have divided the types of risks basically under two categories which are static risk and dynamic risk. Static risk also known as pure risk refers to those risks that only have negative consequences associated with it and refers to those accidental events that lead to economic, financial or physical loss without

providing any opportunity for any form of earnings associated with the occurrence of the event. This category of risks directly falls within the scope of insurance policies involved in providing protection from such static or pure risks faced by organizations. The other category of risks referred to as dynamic risk or speculative risks can be referred to as those type of risky events the occurrence of which have the probability of leading to create positive as well as negative consequences that is it may lead to losses or provide opportunity for earnings. This category of risk falls in line with the entrepreneurial risks and related consequences faced by individuals and organizations such as investments made in a particular project or stock which failed to generate the profits expected. It generally deals with planning and management of a business and different functions associated with it that includes production, marketing, sales and others (Cheng, 2009).

The undertaking or occurrence of events that are associated with a high degree of risk can be triggered through a number of factors that could be divided into those that have been internally generated and those that are generated influenced by the external environment of the organization. As identified by COSO (Committee of Sponsoring Organization of the Treadway Commission) the internal factors include human resources, infrastructure, technology and the business processes that are used by the company. The external factors include social, political, environmental, economic and technological factors (Crockford, 1986).

Risk management can be understood as a process that is implemented by organizations for the purpose of safeguarding the assets of the company against the losses that are incurred by the organizations when hit by unforeseen events that tend to occur on the use of various instruments. Another definition relating to risk management identified include the process of planning, directing organizing and controlling the resources of an organization in such a manner that enables it to achieve the organizational objectives when good or bad events occur unexpectedly that have a direct or indirect impact upon the organization (Davidson, 2004).

The ISO which is the International Standard Organization have set out the principles of Risk Management which states that it should be able to create value, should be integrated into the businesses processes of an organization, should form part of the decision making process of an

organization as it involves a high degree of uncertainty. In addition to the risk management process should be well thought out and based upon the organizational structure suitably and therefore should be well structured and systematic. Besides the aforementioned Risk Management should be based upon the best information available, make the employees and the human resources of an organization as a part of the risk management process, thus the RM (Risk Management) process should be transparent and inclusive, should be dynamic, responsive and adaptable to change, and thus should be reviewed on an ongoing basis to bring about improvements and enhancements based upon the changes taking place in the internal and external environment of an organization (Ellegaard, 2008).

Thus, adoption of the appropriate Risk management methodology by an organization shall bring down the level of uncertainty faced by the organization in relation to their productivity and also in relation to trading done in the concerned market. It brings down the risks associated with failure and thereby brings about improvement in an organization's internal and external image in the long run. Thus, risk management ensures generation of value for an organization through maximizing of profits and minimization of costs associated with it (Head, 2009).

Risk management process can be shown in a stage wise process. The first step in the multiple step process can be referred to as the preparatory step which involves developing a description of the risk management plan which should be planned out in a manner that it is consistent with the strategic long term business objectives of the organization in the picture. Thus, while developing a detailed plan for the purpose of risk management the first step involves identification of all the types of risks that the organization is exposed to. The next step involves the identification of the frequency and the probability of the occurrence of risk events identified in the first step along with the magnitude of the positive or negative impact each of the risks identified is likely to have upon the organization in terms of their operations as well as its financial impact. This will enable the organization to determine the priority of the risks that need to be dealt with first in order to enable the organization to deal with uncertainty in a more efficient manner. While determining the impact of potential risks being faced by the organization, it would be appropriate that the management establish an agreed upon an

accepted level of threshold against which the risks shall be measured based upon the risk consumption appetite of the organization as determined by the top management as well as the resources available for the purpose of risk management. The third stage of the risk management process involves identification of the unacceptable risks of the organization that fall beyond the threshold limit established in the earlier step by the management. The step involves identification of the treatment of the unacceptable risks that shall be implemented as part of the risk management process of the organization in order to minimize or reduce the risk. On evaluation of management literature, it was identified that authors have defined the first two steps of the risk management process that involves identification, evaluation and analysis and clubbed it together to refer it to as the risk assessment process. The risk management methodology for an organization should be identified as a long term dynamic process that shall be reviewed and evaluated on an ongoing basis in order to ensure that it is in line with organization and its long term objectives and suits the organizational structure in terms of its size and availability of resources for the purpose of management of risks (Henschel, 2009).

PATHS OF RISK MANAGEMENT AND ITS APPLICATIONS

The last few decades the world business community has been witness to a number of events in relation to social and economic systems relating to safety of workers risks, natural or clinical risks which have further intensified the importance of risk management process in organizations. The same period has shown growth and work done in the development of the theoretical background and proliferation of the risk management process through the development of various models, techniques and specific methodologies coming from different fields and in relation to various cultural contexts. On the review of the literature and related empirical studies conducted revealed that the applications of risk management could be broken down under the following streams:

- Strategic risk management: These are the risks inherent to the long term strategic objectives of an organization that are essentially set by the top management. Thus, strategic risk management is an application area which involves implementation of a continuous and integrated process of identification and assessment of strategic risks of an organization covering the scope of brand, human, technological, competition, stagnation and project management risks which are basically considered hindrances or obstacles in enabling an organization to reach its operational and financial goals (Iskanius, 2009).
- Financial risk management: This is another important area identified in relation to the scope of risk management as it involves managing the financial risks of an organization. It is identified as a process that involves creation of value for an organization by implementation of financial techniques so as to be able to manage the financial risks to which the organization is exposed such as credit risk, inflation risk, foreign exchange risk etc (Cheng, 2009).
- Enterprise risk management: This area of application of risk management involves a process that identifies events that might be risky and have a negative impact upon an enterprise and thereby ensures that all the risks such as financial, strategic, human or technological category of risks fall within the tolerance level set by the top management and ensures that the enterprise is able to achieve its objectives in the long run (Henschel, 2009).

- Project risk management: This type of risk management focuses upon the risks associated with a particular project that needs to be implemented. Project risk management is a process that is integrated to the life cycle of the project undertaken by the organization, and involves defining the objectives of the project, identifying the sources of uncertainty involved in relation to the identified project, analyzing the uncertainties identified and thereby work upon developing appropriate responses by the management in order to strike an appropriate balance between the risks and opportunities available to the organization in relation to the project. The types of risks associated with the project management include technical, organizational, operational, contractual, economic and political in nature (Head, 2009).
- Insurance risk management: As discussed in the earlier paragraphs insurance policies are an instrument to manage risks that are static or pure in nature. A pure risk management process in relation to a firm where the insurance risk identified could be social, environmental, technological and personal in nature. This involves taking up insurance policies for the firms depending upon various risk categories which are developed based upon the observations made in relation to the losses incurred as a consequences of the occurrence of the damaging events. It involves application of premiums and the assessment done based upon the assessor's experiences and the competency as well as resources available with the organization (Henschel, 2009).
- Supply chain risk management: This type of risk management involves developing a shared risk management process that is implemented with the suppliers as well as all those who are a part of the supply chain system of an organization and shall help in identification and dealing of risks associated with the supply chain management process in order to reduce uncertainty levels and achieve greater operation and financial efficiency by establishing controls and achieve cost reduction in the long run. With the introduction of the open innovation phenomenon many small and large organizations have now started focusing and building upon strong supply chain partnerships with various members of the company's supply chain that includes manufacturers, suppliers, distributors as well as customers and consequently by implementing the supply chain risk management process the risks derived from these

identified relationships shall ensure that the organization build strong relationships along with the achievement of operational efficiency (Cheng, 2009).

- Disaster risk management: Disaster risks fall within the category of pure risks that are supposed to have only negative consequences with no provision of any opportunity for earnings for the organization facing the disaster risks. Natural phenomenon and related events fall within the category of disaster risks. Thus disaster risk management process provides with a holistic and flexible approach towards management and governing of the community and making it better equipped in dealing with disaster related risks by implementation of a series of action such as programs, projects and implementation of tools and techniques to bring about reduction in the disaster related risks such as natural disasters, terrorist attacks, industrial accidents and epidemics and ensuring the mitigation of the spread of the effects of these disasters through the rigorous implementation of the disaster risk management processes (Ellegaard, 2008).
- Engineering risk management: it is identified as a complex and continuous process implemented that is involved in the management of planning, operation, design and evolution of the engineering system. It aims to develop the process that involves identification and choose responses that are appropriate to the problems identified in relation to the risk factors that are the technical and operational risks through the use of an approach that is systematic and proactive in nature (Altman, 2007).
- Clinical risk management: This is another area of application for risk management process wherein the approach involves improvement in the health care quality of patients wherein the process identifies processes that may put patients in situations of harm and thereby come up with techniques or systems that involve implementation of acts that are able to prevent or minimize the harm associated with the health of patients and establish controls that address the risks associated with the human and organizational factors as well as technical aspects associated with clinical health. The aim of implementation of the clinical risk management process is to minimize the risk related to patient healthcare as well as bring about improvements associated with the quality of care provided along with minimizing the impact of the identified risks and

the reduction of costs associated with it that are required to be borne by hospitals (Crockford, 1986).

SME ECONOMIC CONTRIBUTIONS

In today's times the role played by the SME in the growth of a nation is considered vital. The governments of various nations are also coming out with various new policies that promote and support the growth and development of the small and medium enterprises in their respective nations. The Government of Cyprus where the size of an overwhelming majority of the enterprises in operation fall within the category of small and medium enterprises, is carrying out policies that shall enable such enterprises to prosper and grow despite the global market being dominated by the large multinational companies. It aims to provide the small and medium enterprise operators with better access to capital that is essential for businesses to function and operate smoothly and has long been seen as one of the major barriers for organization prosper and grow in the SME sector (Arnold, 1999).

In terms of contribution that can be made by SMEs in the growth of the nation, it can be clubbed under two categories, which the first one contributes internally and the other one is external in nature. While the internal contributions are with regards to the survival, success and growth of SMEs in a country, the external contribution made by SMEs is that it generates employment opportunities for workforce. It also generates revenue thereby contributing to the improvement of the financial health of the economy. Thus, SMEs tend to play a crucial role in contributing to the wealth and stability of the economy of a nation by creation of new businesses and jobs and therefore is considered the important source of reduction of unemployment and also identified as an area that is considered as a very important source of innovation. Considering the workforce of Europe that consists of 17 million people of which 70% were employed by SMEs while 7 million people were still search of jobs. Thus, this factor indicating that about only 10% of the total workforce was actually engaged in long term employment with large organizations (Gilmore, 2011). Now considering the US market, which is considered as a super power and a developed nation, it considers SMEs as the backbone and the driving engine behind the growth of the US economy, which contributes towards the generated of about half of the total gross national product and currently employing over half of

the total workforce, considered as the principal source of new jobs, and accounting for 80% of the total employment growth witnessed by US. Considering United Kingdom and the role SMEs play in the contribution towards economic growth is that it contributes approximately 38% towards the GDP of the country, and employs 90% of the workforce while playing a role of an important determinant for the generation of new jobs and employment opportunities for the country (Gilmore, 2011). While for Canada, SMEs contribute towards 40% of the total gross domestic product, employs half of the total workforce and is responsible for 60% of the new jobs and employment opportunities created in the country (Roach, 2011). Thus, from all the information and statistics laid out above, it can deduced that in the current business environment and economic situation, small and medium sized enterprises are considered as an important part of the financial and industrial sector contributing towards economic growth as well as generating substantial employment opportunities which is one of the key economic drivers of any nation and is therefore considered a very favorable organizational structure.

CHARACTERISTICS OF SMEs

There are certain distinct features and characteristics of small and medium sized businesses and organizations that set them apart from the multinational companies. The characteristics of SMEs include the number of employees that are employed within the organization, volume of sales, scope for innovation through the launch of a new and unique product or service, flexibility in operations and day to day functioning of the organization, and since it is small in scale it provides scope for providing more complex and better quality customer service, and SME organizations have access to limited resources which is the reason behind the small scale of business and thus have limited financial, human and physical resources (Head, 2009).

The critical factors that contribute towards the success of the small scale enterprises are the ability to have centralized decision making as well as quick decision making as the levels of authority existing within the organizational structure is limited. Another success factor for SMEs in the recent times has been the introduction of policies by Governments in favor of as well as in order to support the small and medium sized enterprises enabling them and

providing them faster clearances for the purpose of exports as well as providing greater access to the capital markets for the purpose raising funds (mcit.gov, 2015).

Other characteristics that have been identified to be unique to the SME sector is that since the number of employees is limited and the organizational structure is relatively flat in comparison to large scale organizations, it enables the workforce especially the managers to carry out face to face communication with the rest of the staff which is the best form of communication that helps in avoiding misleading and misinterpretation of information being communicated within the organization. This form of organizations also helps promote innovation and new products and services being introduced into the market with establishment of SMEs as the scope of incurring losses if the product or service fails is reduced. Thus, in this form of organizations, the management implements the low risk strategy given the uniqueness and level of innovation involved which may or may not be accepted by the market and in turn fails to create the required demand for the product as anticipated. Generally, to set up a small scale business or enterprise the owners who are generally themselves the managers of the organization utilize their personal savings or borrow from banks in order to bring in the initial capital required to kick start the business operations as they are not large enough to go public and raise capital through the issue of shares (Crockford, 1986).

Thus, from the discussion of the traits of the SMEs above it is evident that though small in scale and scope with limited amount of capital involved in these organizations, the degree of risk associated with the operations of such organizations is high. As well as the risk of market failure is relatively higher in comparison to the large scale organization given the degree of innovation and uniqueness of the product which might fail to find a place in the market and clock in the sales required to make the business profitable. Thus, highlighting the need for identification of risk areas within the organization and importance of implementing a risk management process (Verbano, 2013).

CHAPTER 2: RESEARCH METHODOLOGY

This section of the dissertation shall focus upon the research design and methodology as well as the sample size chosen for the purpose of conducting of analysis upon the primary data collected followed by the research analysis and findings with a detailed conclusion.

RESEARCH DESIGN AND METHOD

The research design that has been chosen for the purpose of research and analysis for the given paper is the investigation based research design in which the purpose and the scope of the research is established beforehand along with identification of dependent and independent variables of the research in relation to the topic and analysis is done to draw conclusions regarding their relationship through various analytical and statistical techniques. The method chosen for the purpose of data collection are quantitative data collection techniques where primary data shall be collected through the conduct of a survey with the help of a questionnaire designed to include questions regarding risk management in SMEs and based upon the data collected and analysis done, the appropriate conclusions shall be drawn.

The purpose of using quantitative data collection techniques as opposed to collecting data through qualitative techniques such as the use of a questionnaire is that it shall be less time consuming given the limited time frame and resources available for the conduct of the research. In order to develop the questionnaire relevant literature reviewed helped in the formation of questions. The questionnaires were mailed to all the participants attached with an email clearly explaining the purpose of the research and seeking their consent.

DATA COLLECTION AND SAMPLE SIZE

For the purpose of collection of primary data for the given research study a questionnaire has been used which has been attached to the appendices of the given paper. The population for the given research is the SME sector of Cyprus and those that are currently operating in the given sector in order to obtain their views with regards to the risk management in the organizations. The sample size chosen for the given research shall be 100 SMEs from a total population of 61,041and shall be selected based upon the availability of the owner/ manager who shall be reached out through an email in order to ensure that the analysis is not affected and only those companies that are currently in operation shall form part of the sample. In order to ensure representation from all sectors of the industry, the 100 sample chosen shall be screened to ensure sufficient representation from all types of organizations in order to avoid any form of biasness. The sampling method chosen here was random sampling where all the SMEs that responded had equal probability of becoming a part of the sample.

VALIDITY AND RELIABILITY OF THE DATA COLLECTED

It is essential that steps be taken to ensure that the primary and secondary data collected on the basis of which research analysis shall be carried out and conclusions drawn are valid and reliable so as to avoid misleading the readers due to invalid data used for the purpose of drawing conclusions. In order to avoid such a situation all the filled in questionnaires received checked to ensure that those chosen to be part of the sample have been completed in all aspects and have not been filled out frivolously as that may impact the findings made. Moreover, in order to make the process of data collection reliable, the email sent to the respondents clearly stated the purpose of the analysis proposed to be conducted. Also it was included for the reason behind the research proposal along with ensuring the fact that the data collected by the questionnaire were confidential and the anonymity of the participating firms would be maintained as well as all the data destroyed once the research report is ready and the analysis was over. Upon receipt of the completed questionnaires of 150, 10 were found to be incomplete, and a random sample of 100 was chosen from the remaining 140 questionnaires.

LIMITATIONS AND ETHICAL CONSIDERATIONS

Every research study conducted has some degree of limitations and ethical considerations involved which needs to be identified and addressed for the benefit of the readers of the paper. The limitations and ethical considerations in relation to the given research paper has been identified below:

- the time horizon that is available for the research study to be conducted is limited and therefore requires appropriate allocation of the resources available in order to conduct the research smoothly and present the findings and results within the time frame provided
- since the risk management concept is relatively a new concept along with the sprouting of SMEs being a relatively new phenomena therefore the sources of secondary data available for the purpose of conducting the literature review was limited which can be considered another limitation to the scope of the research
- The primary data proposed to be collected from the owners and managers of the small and medium enterprises shall be collected after obtaining their consent for usage of data collected via the questionnaire for the purpose of the proposed research. Therefore in order to obtain the consent of the proposed participants the starting portion of the questionnaire shall include a consent form seeking their permission to use the information in the questionnaire for the purpose of carrying out conduct of their analysis.
- Another limitation is the knowledge and level of experience of the researcher which should also be addressed to understand the possibility of mistakes and enabling the readers to utilize their own judgmental abilities to determine the degree of reliability that can be placed upon the findings to be drawn in the paper.

CHAPTER 3: RESEARCH ANALYSIS AND FINDINGS

This chapter shall focus upon the analysis conducted and conclusions drawn from the primary data collection through the questionnaire. This wil enable to determine new findings and conclusions in the area of risk management and the SME sector which could further be utilized for the purpose of extended scope for research in the same area in the future.

ANALYSIS AND FINDINGS

Based upon the data collected via the questionnaires, analysis has been done and findings have been drawn with the help of graphical representations of the responses received from the managers and owners of the SME sector of Cyprus which has been discussed below.

RISK MANAGEMENT: ESSENTIAL ORGANIZATIONAL FUNCTION

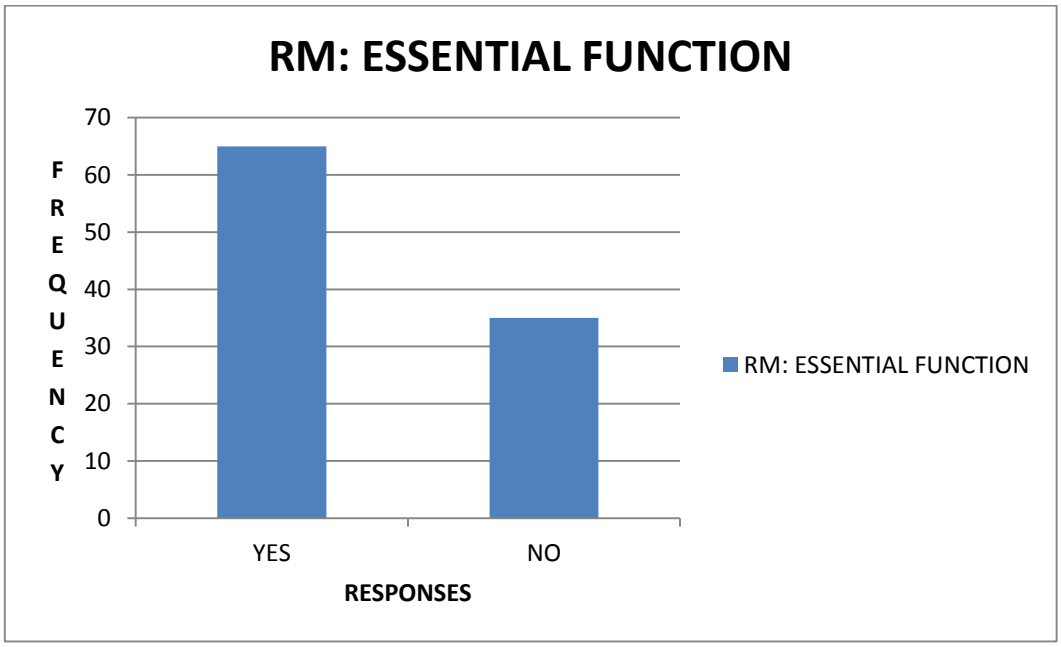

Figure 1

Based upon the graphical representation shown above in relation to the responses received from the respondents of the questionnaire, it can be seen that the times have changed where earlier risk management was considered as an additional responsibility or function undertaken

by organizations to safeguard their interests and protect it from the negative consequences of occurrence of unforeseen events, it is now viewed as one of the primary functional areas in an organization falling in line with key functional areas such as production, finance and marketing within an organization.

IMPORTANT RISK AREAS

As discussed earlier as a part of the literature review, there are a number of different types of risks that an organization has to face considering the factors that may be internal or external to the organization. Therefore, different types of risks tend to have different degrees of impact upon the financial and economic performance of an organization. Thus, in order to address the different types of risks faced by organizations the questionnaire included a list of the type of risks that are generally faced by SMEs as gathered from the secondary sources of data and management literature and the respondents asked as to which type of the risk areas do they think tend to have the maximum impact in terms of negative consequences upon the financial and economic health of the small and medium sized enterprises in Cyprus. The responses received have been summarized in the graphical representation below.

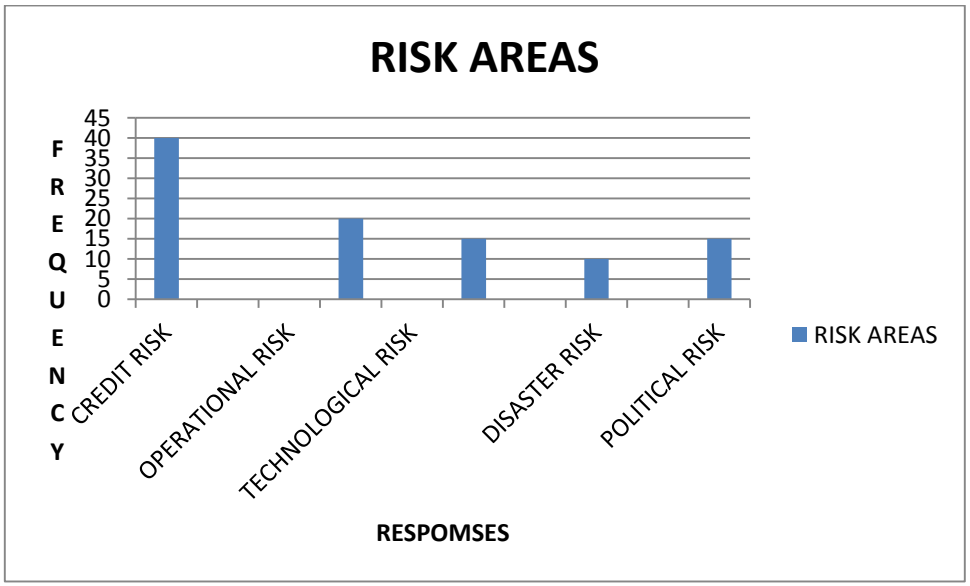

Figure 2

From the graph above, the information that can be drawn for the purpose of analyzing the risk areas associated with the Small and medium enterprises can be said that most of firms included in the sample for the purpose of the research were of the view that the biggest risk faced by SME organizations are credit risks that is the risk that the organization shall not have enough funds for the purpose of operation lacking the credibility to raise funds in the market or fail to generate revenue sufficient for the purpose of meeting the debt obligations and making repayments to the debt holders. Therefore, organizations believe that steps need to be taken by the management for ensuring minimization of credit risk which in turn has an impact upon the operations and productivity of the organization. Moreover, in recent times Government has launched various policies to create an environment that is conducive to the operations of SMEs in the domestic as well as global markets. However, the benefits of such policies are yet to be seen. The other risk area recognized is in relation to the operational risk which is identified as another area that should be looked into by the management to ensure smooth functioning of SMEs. This is identified as an important area given the fact that the SME sector lacks the availability of sufficient financial sources and availability of resources at hand to be able to deal with unforeseen events that eventually lead to having an impact upon the operations of the organization affecting the production levels and thereby impacting the margins achieved by the organization.

The third highest risk area identified in terms of responses received from the respondents was in relation to the technological risk faced by the organization which involved use of technology or information technology infrastructure that might be outdated or limited in scope considering the limited sources in hand for the small and medium enterprises. It would be worthwhile also to identify another important risk area that is inherent to small and medium scaled enterprises which are the market risk. Since, SMEs engage in production of goods and services that are unique and innovative considering their small scale, they might fail to generate interest in the target market segment and fail to generate a sustainable customer base if the product is not accepted or falls below the customers' expectations.

The lowest level of risk area in which risk management is still a concern are the political and disaster risks which are covered the government policies and programs and also the recent

steps that have been taken by the Government to provide support to the growing SME sector and enable them access to resources and finance essential for their operation.

STEPS TAKEN FOR MANAGING RISKS

Table 1

RESPONSES		INSURANCE POLICIES			RM COMMITTEE		HIRING RISK OFFICER	
FREQUENCY			75		5			20

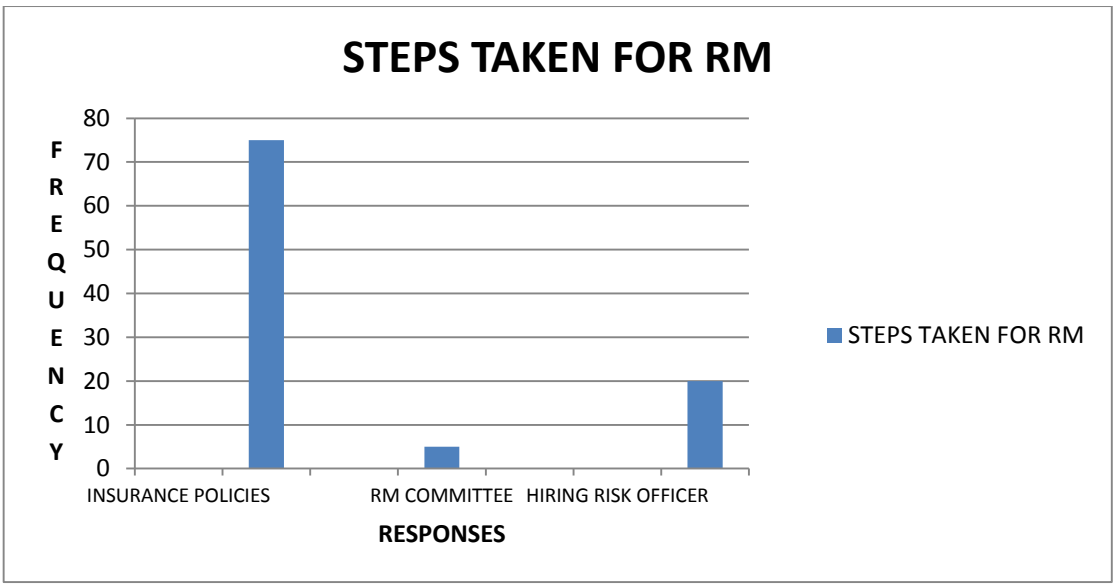

Figure 3

The common steps identified in relation to risk management are insurance policies, risk committee or hiring a risk officer. Based upon the graphical representation shown above it can be said that most of the small and medium sized companies rely upon the risk mitigation policy of taking insurance coverage for the identification of various risk areas based upon the capability of the company to make premium payments and loss coverage. Identifying the need to be better prepared for handling unforeseen events that tend to have a negative impact upon the operations of the business about 20% of the small and medium sized enterprises have hired risk management officers that are qualified in identifying and handling risks of a business and take the necessary steps required for risk reduction and risk mitigation according to the needs of the organization and tend to work closely with the top management being part of the

decision making process of the SME. Finally another step involved in managing risks was establishment of a risk committee. Generally these forms of committees are seen in large organizations wherein some members of the Board are made part of the risk management committee. The committee is then required to develop and implement the risk management program in an organization and take the steps necessary for the purpose of their successful implementation to ensure all the identified risk levels fall within the acceptable threshold of risk identified by the Board. Also they are continuously monitor the process for its effectiveness and bring about changes and improvements as and when required. However, a very few handful of SMEs invest resources in establishment of a risk committee considering the size of the organization and the effectiveness and contribution to efficiency made by the risk committee towards the operations and productivity levels of the organization considering the cost benefit analysis associated with it.

EFFECTIVENESS OF GOVERNMENT POLICIES

The Government of many nations including both developed and developing countries has been making policies for the betterment of market situation for SMEs and making finance and resources more accessible to these firms considering their contribution to the Gross domestic product and the employment opportunities and growth in the nation which is considered as one of the most powerful economic drivers (mcit.gov, 2015).

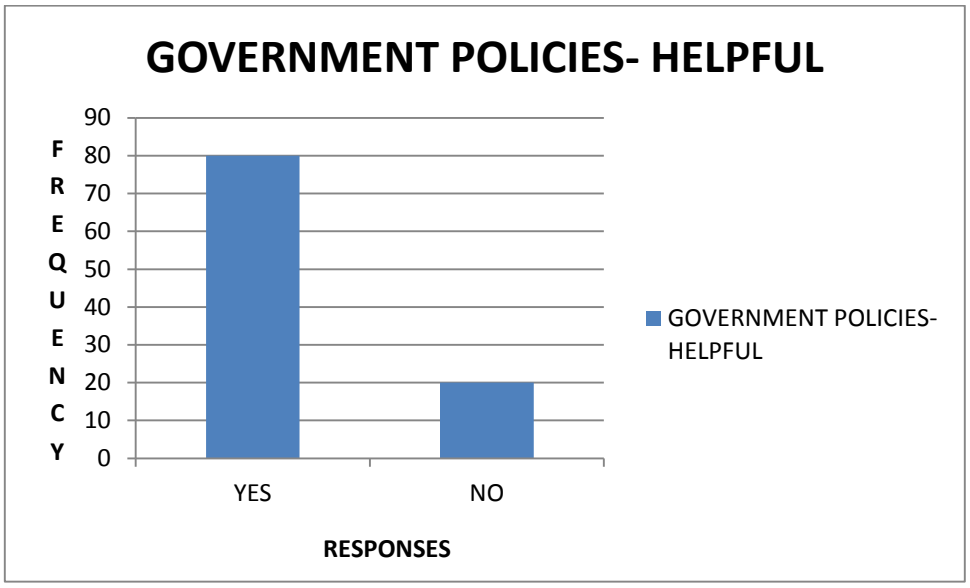

Figure 4

From the survey conducted and data collected from the respondents it is evident that the majority of the companies in the SME sector of Cyprus that agreed that government policies implemented recently have had a positive impact upon the SME sector providing them better access to the resources and capital market for the purpose of raising finances. However, 35% of the responses had a negative view with regards to the given question. They were of the view that though government has taken steps recognizing the importance of the organizations operating in the given sector, the results achieved from their implementation has been far away from being successful. The Government needs to focus upon the rigor of the policies that it aims to implement in order to make the markets open up further for the organizations.

RM: SCOPE FOR IMPROVEMENT

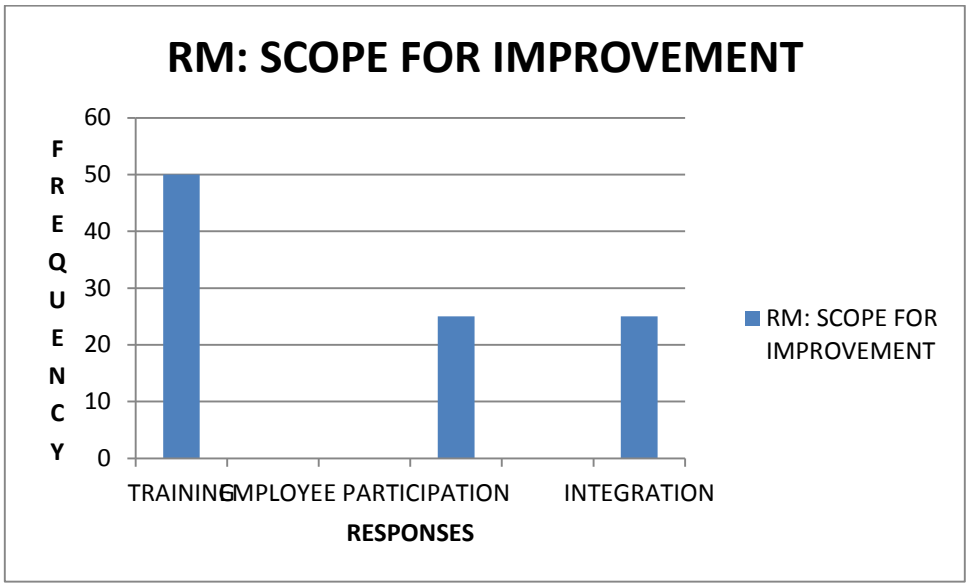

Figure 5

Considering the discussions above it can be said that there is a need to bring about improvement in risk management in the SME sector. Thus, the various steps identified in relation to improvement in risk management can be training of employees in managing risks, encouraging participation of employees in risk management process and integrating risk management with the strategic objectives of the organization.

From the survey conducted, it was found that maximum participating SMEs that are 50 percent of the respondents were of the view that the improvement in the situation of risk management in organizations could be brought about by the training of managers in risk management. The remaining 50% of the participants were equally divided between the two methods that they view that could bring about improvement in the risk management situation which were integration of the risk management process with the strategic objectives of the organization and encouraging employee participation in the risk management process.

CHAPTER 4: CONCLUSION

From the analysis conducted above, it has become evident that the role played by risk management has gained substantial importance over the years considering the impact of certain unforeseen events on the global economy and is subsequent impact upon the business organizations operating during the time. Large organizations and Multinational companies tend to be better equipped with handling unforeseen events and their impacts upon the operations of the organizations by having controls in place to handle the impact and ensure that the operation and productivity of the firms are not affected.

However, considering Small and Medium sized enterprises, they show a much greater degree of vulnerability to the risks considering that they have access to limited human, physical and financial resources and are therefore in a position to be greatly impacted by the changes occurring and events taking place both internally and in the external business environment that might be favourable or unfavourable to the organization. Thus, secondary sources of information collected also indicated that small and medium enterprises tend to have certain characteristics that make them more vulnerable to the risks faced by organizations such as the lack of abundance of resources. Along with lack of a clearly defined risk management process with appropriate controls in place to identify and implement treatments to mitigate risks, as well as since the SMEs tend to be engaged in innovative products and services having unique characteristics. They tend to have a greater degree of exposure to market risk in comparison to large scale industrial organizations engaged in bulk manufacturing of standardized products that enjoy greater market acceptance. Therefore, SMEs face a high degree of market risk and the possibility of not being able to generate demand and a sustainable customer base in the long run.

The secondary data sources also revealed the growing contribution by the SME sector towards the economy of the nations in which they operate as well as a global perspective. Thus, this information further re-established the importance of the risk management function in the operation of the SME organizations. From the primary data collection and analysis conducted, the conclusions drawn showed that majority of the organizations have now identified the importance of the risk management process and view it as an essential function which should

be integrated and fall in line with the other functional areas of the organization which include production, distribution and marketing for successful operation in the long run.

In terms of the risk areas identified in relation to the SME sector, it was seen that most of participants recognized credit risk as the key risk area. Thus financial and credit risks are the category of risks that pose substantial threat to abrupt the operations of SMEs due to lack of access to the capital market and limited access to financial resources. Moreover, other form of risks faced by SMEs in Cyprus includes technological risks in terms of lack of upgraded technological infrastructure available for the purpose of carrying out operations. The survey conducted also revealed that in relation to risk management the steps taken by an organization mostly included use of insurance policies that provided coverage from disaster related risks which are in the nature of pure risks, however, with very few organizations hiring a risk management officer to identify and implement appropriate risk management process in line with the strategic objectives of the business of the SME. The risk committees were found to be limited to very few handfuls of organizations as SMEs lacked the resources and thought it was a waste of resources considering the cost benefit analysis associated with establishment of the risk committee. In terms of bringing about improvement in the risk management situation in SMEs, the research revealed that most managers lacked the knowledge and experience in the area of risk management. Therefore, were of the view that organizations should invest in training programs that would provide the necessary knowledge to the employees to manage risks efficiently and integrate risk management. With the objectives of the organization which shall be essential for the smooth functioning and the ability of small companies to adopt to changes taking place in the external environment as well as be in a position to better deal with intense competition.

APPENDICES

COVER LETTER

Respected Sir/ Madam,

This email is with regards to an independent survey being conducted in relation to the topic of growing importance of risk management in the small and medium sized sector. The survey is being conducted through a questionnaire, so I seek your consent for participation in the survey. All the data collected will be kept confidential and the anonymity of all participants will be maintained at all costs. Therefore, I would be grateful if you could take the time out to go through the questionnaire attached to the email and fill in the answers. The filled in responses are to be emailed on the same email address within a period of 5 days.

Thanking You,

Regards,
Aslanidou Gioulianna

QUESTIONNAIRE

The questionnaire included the following questions to be filled out by respondents.

1. Do you consider risk management as an essential function such as marketing and production in an organization?
    - YES
    - NO
2. What are the most important risks areas identified while operating in the SME sector?
    - CREDIT RISK
    - OPERATIONAL RISK
    - TECHNOLOGICAL RISK
    - DISASTER RISK
    - POLITICAL RISK
3. Which is the most commonly utilized step for managing risks in SMEs?
    - taking insurance policies
    - establishing a risk management committee
    - hiring a risk management officer for the organization
4. Do you feel that the Government policies are being helpful in the growth and development of SMEs?
    - YES
    - NO
5. What are the areas that can be identified for the purpose of the scope for improvement?
    - training of management with regards to the risk management process
    - ensuring that the employees become part of the decision making and risk management process
    - establishing a risk management plan that are in line with the strategic objectives of the organization

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