COURSE GUIDE

PAD 410
GLOBALISATION AND NATIONAL POLICIES

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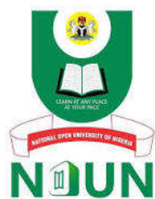

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COURSE GUIDE

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MODULE 1

UNIT 1: GLOBALISATION/INTERNATIONAL INSTITUTIONS

Unit Structure

1.1 Introduction
1.2 Intended Learning Outcomess
1.3 New International Economic Order
 1.3.1 International Trade
 1.3.2 Technology Transfer
1.4 Regulation and Control of the Activities of International Institutions
1.5 International Institutions using Indian economy as a case study
1.6 Summary
1.7 References/Further Readings/Web Resources /Web Resources
1.8 Possible Answers to Self-Assessment Exercise(s)

1.1 INTRODUCTION

Today, organisations are conducting their businesses in a global environment. Many large firms have become multinationals, doing business across national boundaries. Even small firms source their production inputs overseas. Overseas firms are producing their products here. The supply chain for many goods is global. For instance, U.S. firms are acquiring firms abroad. The vogue is to shift to the international market and acquire as much market share as possible. Globalisation goes with trade liberalisation among nations and the removal of all trade barriers. so that commerce and industry can flourish smoothly around the world without hitches and impediments.

1.2 INTENDED LEARNING OUTCOMES

By the end of this unit, you will be able to:

- demonstrate the understanding of global business
- discuss the new international economic order
- explain foreign trade and comparative advantages.

1.3 New International Economic Order

The demand for a New International Economic Order (NIEO), especially by developing nations, goes back to the first session of the UNCTAD in 1964. The various resolutions adopted in the subsequent sessions of the UNCTAD contain a systematic account of the various elements of a NIEO. At the root of the call for a New International Economic Order lies the dissatisfaction of the LDCs with regard to the trading, financial, technological, and other policies pursued by the developed countries towards the LDCs. The developed nations have oppressed the LDCs, discriminated against them, drained their income and denied them access to advanced technology. Such policies have hindered their development efforts, perpetuated inequalities in wealth and income, and increased unemployment and poverty in them. There were three phenomena that gave an impetus to the demand for a new international economic order in the early 1970s. These were

a. A severe energy crisis
b. The breakdown of the Bretton Woods System in 1973
c. The disappointment with development aid which was much below the United Nations target of 0.7% of Gross Domestic Product (GDP) of developing countries.
d. The formation of the Organisation of Petroleum Exporting Countries(OPEC) in 1973 and its success in raising oil prices.
e. The existence of high rates of inflation and unemployment in LDCs

Specific proposals for the NIEC were put forward at the Summit Conference of Non-Aligned Nations held in Algiers in September, 1973. The success of OPEC led the developing countries to call the Sixth Session of the UN General Assembly in April, 1974. This session adopted, without a vote, a declaration and a Programme of Action on the Establishment of New International Economic Order based on equity, sovereign equality, interdependence, common interest and cooperation among all states, irrespective of their economic and social systems which shall correct inequalities and redress existing injustices, make it possible to eliminate the widening gap between the developed and the developing countries and ensure steady acceleration of economic and social development and peace and justice for present and future generations.

In December 1974, the UN General Assembly approved the Charter of Economic Rights and duties of States. These three Resolutions constitute the documents of the New International Economic Order. The most important objectives of the New International Economic Order based on the proposals of the UN Resolutions include; international trade,

technology transfer, regulation and control of the activities of multinational corporations, reformation of the international monetary system and special aid programme, and interdependence and cooperation

1.3.1 International Trade

The New International Economic Order lays emphasis on a greater role of LDCs in international trade by adopting the following measures which aim at improving the terms of trade of LDCs and removing their chronic trade deficits;

(i) Establishment of LDC sovereignty over natural and especially mineral resources for export,
(ii) Promoting the processing of raw materials for exports,
(iii) Increasing the relative prices of the exports of LDCs through integrated programme for commodities, compensatory financing, establishment of international buffer stocks and creation of a common fund to finance stocks, and formation of producers, associations,
(iv) Providing proper framework for establishing prices of raw materials and primary products so as to stabilise export income earnings,
(v) Indexation of LDC export prices to rising import prices of manufactured exports of developed countries,
(vi) Increase in the production of manufactured goods, and
(vii) Improving access to markets in developed countries through progressive removal of tariff and non-tariff barriers and restrictive trade practices.

It is important to recognize that foreign trade is of great importance to both developing and developed nations of the world. Trading activities occur between nations because it brings about specialisation, and specialisation increases output. Because the United States can trade with other countries, it can specialise in the goods and services it produces well and cheaply. Then the U.S. can trade its goods for goods and services produced cheaply by other countries.

International differences in resource endowments, and in the relative quantity of various types of human and non-human resources, are important bases for specialization. Consider countries with lots of fertile soil, little capital, and much unskilled labour. They are likely to find it advantageous to produce agricultural goods while countries with poor soil, much capital, and highly skilled labour will probably do better to produce capital intensive, high-technology goods.

Self-Assessment Exercise

Enumerate three phenomena that gave an impetus to the demand for a new international economic order in the early 1970s.

1.3.3 Technology Transfer

The proposals of the New International Economic Order stress the establishment of a mechanism for the transfer of technology to LDCs based on the needs and conditions prevalent in them. In this context, particular emphasis is placed on the (i) establishment of a legally binding international code regulating technology transfers; (ii) establishment of fair terms and prices for the licensing and sale of technology; (iii) expansion of assistance to LDCs in research and development of technologies and in the creation of indigenous technology; and (iv) adoption of commercial practices governing the transfer of technology to the requirements of LDCs.

1.4 Regulation and Control of the Activities of Multinational Corporations (MNCs)

The New International Economic Order declaration also emphasizes the formulation, adoption and implementation of an international code of conduct for multinational or transnational corporations based on the following criteria: (i) to regulate their activities in host countries so as to remove restrictive business practices in LDCs; (ii) to bring about assistance, transfer of technology, and management skills to LDCs. (iii) to regulate the repatriation of their profits and (iv) to promote the reinvestment of their profits in LDCs.

1.4.1 Reformation of the International Monetary System and Special Aid Programme

The New International Economic Order declaration proposes to reform the international monetary system on the following lines:

(i) Elimination of instability in the international monetary system due to uncertainty in the exchange rates;

(ii) maintenance of the real value of the currency reserves of LDCs as a result of inflation and exchange rate depreciation;

(iii) Full and effective participation by LDCs in the decisions of the IMF and the World Bank; (iv) achievement of the developed-country target of 0.7% of GNP for LDC development assistance,

(v) Debt re-negotiation on a case-by-case basis with a view to concluding agreements on debt-cancellation, moratorium or rescheduling;

(vi) Deferred payment for all or parts of essential products;
(vii) COMMODITY assistance, including food aid, on a grant basis without adversely affecting the exports of LDCs.
(viii) more favorable credit terms for goods and technical assistance to accelerate LDC industrialisation,
(ix) favorable investment in industrial and development projects

1.4.2 Interdependence and Cooperation

Above all, the New International Economic Order declaration lays emphasis on more efficient and equitably managed interdependence of the world economy. It brings into sharp focus the realization that there is a close relationship and interdependence between the prosperity of developed countries and the growth and development of LDCs. For this reason, there is a need to create an external economic environment conducive to accelerated social and economic development of LDCs. Furthermore, it requires the strengthening of mutual economic, trade, financial, and technical cooperation among LDCs, mainly on a preferential basis.

1.5 International Institutions using Indian economy as a case study

In our study of international institutions, we are going to use the Indian economy as a case study. We shall be looking at the objectives and achievements of Indian plans and how these plans affect the national and international institutions within the Indian economy.
History; Planning as an instrument of economic development in India goes back to the year-long programme of planned economic development of India. This pioneering work created a keen interest in academic circles in the cult of planning. As a result, some more books appeared on the subject by other prominent writers in India.

In 1938, the first attempt was made to evolve a national plan for India when the National Planning Committee was set up under the chairmanship of Pandit Nehru. The work of the committee was interrupted due to the Second World War and the political disturbance following the resignation of the Congress ministries. It was only in 1948 that the Committee could release a series of reports on planning in India. In the next few years, eight leading industrialists of Bombay became convinced of the need for planning and took the initiative of preparing a plan of economic development for India. It was published in January 1944, a year plan envisaging an expenditure of 10,000 rupees. It was aimed at doubling the per capita income and trebling the national income during this period. It proposed increasing agricultural output by

130%, industrial output by 500%, and service output by 200% over a fifteen-year period.

Objectives and Achievements of Plans

India embarked on the path of planned economic development on April 1,1951. Since then, she has gone through ten Five-Year Plans. A critical appraisal of the overall achievements and failures during this period of planning is attempted below:

Objectives: There are various objectives that run through one or the other plan. They are:

i. To increase national income and per capita income
ii. To raise agricultural production
iii. To industrialise the economy
iv. To achieve balanced regional development
v. To expand employment opportunities
vi. To reduce inequalities of income and wealth
vii. To remove poverty
viii. To achieve self-reliance

In a broad sense, these specific objectives can be grouped into four basic objectives; growth, modernization, self-reliance and social justice. We critically evaluate the performance of Indian Plans in the light of the following objectives

a. **Growth**

One of the basic objectives of planning in India has been rapid economic growth. This is measured by the overall growth rate of the economy in terms of real GDP. The overall growth rate of the economy from 1950 to 2006 in terms of GDP at factor cost at constant prices has been characterized by extreme variations from year to year. Consequently, the targets of growth rate fixed for various plans were not achieved except for the first, fifth, sixth, seventh, and eight five-year plans. In the first plan, a growth rate of 3.7% per annum was achieved, which was higher than the estimated growth rate of 21%. During the second plan, the actual growth rate was a little less than 4.2%, as against the targeted growth rate of 4.5%. In the third plan, the actual growth rate of 2.8% was much lower than the targeted rate of 5.6%. The Fourth Plan also showed a large decline in the actual growth rate, which was 3.4% as against the estimated rate of 5.7%. But the Fifth Plan achieved a higher growth rate of 5% than the targeted rate of 4.4%.

The Sixth Plan had set a target growth rate of 5.2% but achieved a higher growth rate of 5.5%. The Seventh Plan achieved a growth rate of 5.8% against the envisaged target of 5%. The Eight Plan achieved a growth rate of 6.8% as against the target of 5.6%. The Ninth Plan had a

growth rate of 5.5% against the target rate of 6.5%, and the Tenth Plan had a growth rate of 7.6% against the target of 8%. But except for the year 2002-2003, the growth rate was 8.6% for the remaining four years of the tenth plan.

Modernisation

National Income: The sectorial distribution of national income reflects the structural transformation of the Indian economy. The composition of GDP shows significant changes over the period 1950-2006. In 1950-51,59% of GDP came from the primary sector (agriculture) which dropped to18.5% in 2006. This is a concomitant result of the development process, in which the primary sector gives way to the secondary sector (industry)and the tertiary sector (services) in the economy.

Agriculture: Modernization and structural changes in agriculture have played an important role in the process of planned development. The country has made giant strides in the production of foodstuffs, especially grains, cash and horticultural crops, to meet the consumption requirements of the growing population, the raw material needs of the expanding industry and for exports. The phenomenal increase in the output of food grains by four times has been due to the spread of high-yielding varieties of inputs; the extension of irrigation facilities and water management programmes; the establishment of a system of support prices; procurement and public distribution; the promotion of agricultural research, education, and extension; and institutional arrangements to suit small and marginal farmers.

Industry: The main component in the drive for structural diversification has been towards modernization and diversification of industries. Over the past 50 years, India has achieved a broad-based industrial development. Apart from a quantitative increase in the output of industrial products, the industrial structure has been widely diversified, covering the entire range of consumer, intermediate, and capital goods. Chemicals, engineering, transport, petro-chemicals, synthetics, electronics, etc. have made rapid strides. In most of the manufactured products, the country has achieved a large measure of self-reliance.

Social Services: Modernisation is also reflected in the spread of social services. There has been a significant increase in development expenditure on social services, whose share of GDP grew from 3% in 1950 to 28% in 2006. There has been a marked expansion of health services. The number of doctors, nurses, and hospitals has increased substantially, and villages have been electrified. Drinking water has been supplied to many villages. There has been a spectacular spread of

education in rural areas. The number of secondary schools, colleges, universities, medical and engineering institutes has multiplied manifold.

Self-Reliance: Self-reliance implies foreign aid, diversification of domestic production, and a consequential reduction in imports for certain critical commodities, as well as the promotion of exports to enable us to pay for imports from our own resources. A major constraint towards achieving the objective of self-reliance has been an unfavourable balance of payments. The deficit in the current account balance continues to increase till the end of the seventh plan. It started declining after the Eighth Plan.

Self-Assessment Exercise 2

Identify the basic objectives of planning in India has been rapid economic growth.

1.6 Summary

The vogue is to shift to the international market and acquire as much market share as possible. Globalisation goes with trade liberalisation among nations and the removal of all trade barriers so that commerce and industry can flourish smoothly around the world without hitches and hazard. International operations go with cultural differences, which must serve international firms and businessmen for success in the international markets.

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1.8 Possible answers to self-Assessment Exercise

Answers to SAEs 1

f. A severe energy crisis
g. The breakdown of the Bretton Woods System in 1973
h. The disappointment with development aid which was much below the United Nations target of 0.7% of Gross Domestic Product (GDP) of developing countries.

Answers to SAEs 2

One of the basic objectives of planning in India has been rapid economic growth. This is measured by the overall growth rate of the economy in terms of real GDP. The overall growth rate of the economy from 1950 to 2006 in terms of GDP at factor cost at constant prices has been characterized by extreme variations from year to year. Consequently, the targets of growth rate fixed for various plans were not achieved except for the first, fifth, sixth, seventh, and eight five-year plans.

UNIT 2: GLOBAL POWER AND WEALTH DISTRIBUTION

Unit Structure

2.1 Introduction
2.2 Intended Learning Outcomess
2.3 Global Power and Wealth Distribution
 2.3.1 Instrument for Wealth Distribution
2.4 Problems of Global Power in Wealth Distribution
2.5 International Institutions using Indian economy as a case study
2.6 Summary
2.7 References/Further Readings/Web Resources /Web Resources
2.8 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

Since the mid1980s, Politics throughout the world has been rocked by dynamic and unpredictable developments. The most visible changes were set in motion from bipolar politics into uni-polar diplomacy, and revolutions of 1989 in central and Eastern Europe that led to the disintegration of much of the communist world. This also influenced economic diplomacy and wealth distribution across the globe. By the end of 1991, the soviet, once a formable superpower, had collapsed into fifteen troubles republics, including a much humbled Russia (William A. Joseph 2007).

Post-cold war political and economic changes and transformation of the global balance of power have produced new forms of international cooperation and competition _ a new source of international tension and violence and new method of wealth distribution across the globe.

The grime but predictable bipolar world of superpower rivalry between United States and Soviet Union, new Russia reinforced by NATO and Warsaw treaty organisational (Warsaw Pact) alliances has been replaced by the uncertainties of more fragmented map of global power.

These global changes have had far-reaching consequences for the economic redistribution of wealth in Asia, Africa, and Latin America. The issues of debt rescheduling and conciliation, technological transfers, and other means of wealth redistribution have created problems and removed strategic leverage in economic world politics. Economic diplomacy has provided a unique laboratory for the study of global powers and issues of wealth redistribution across nations. The instruments for wealth redistribution include:

a. Technological transfers
b. Bilateral agreement
c. Signing of economic pacts

d. Regional economic means
e. Gifts,
f. The use of multination corporations.

The above represents instrument for redistribution among comity of nations today.

2.2 Intended Learning Outcomess

By the end of this unit, you will be able to:

- discuss the interaction of states within the economic international order.
- explain the role of states and super powers in global economic management
- examine the role technological transfer and other instrument in wealth redistribution.
- show that political economy and development is more conflicting that it reveals
- prove that wealth distribution is based on the national interest of global powers, not merely on the interest of nation expecting development.

2.3 Global Power and Wealth Distribution

There are many strategies in the hands of state in the global political economy, as regards wealth distribution in modern diplomacy.
Emergence of globalization began as an attempt to examine the way in which states or global powers responds to and attempted to manage the process of globalization and wealth distribution. The instrument of competitive strategies, did not favour less developed nations. The role of less developed nations in the global political economy in wealth distribution is in decline, and globalization had become a mysterious, omnipotent and incontrollable force, somehow rendering wreathing in its wake powerless (RonewPalan 2009).
In the word of Francis Balle (2009) in technological and economic terms, the world is a village; nevertheless, the world remains a mechanism for cultural, economic and political difference.

Under the combined effect of the globalization of the economy and distribution of wealth revolution, have led to Americanization or the balkanization of culture as regards wealth distribution has promoted

forced standardization. This was also queried by Charles Ziagber (2007) great power are not the avatar of development but a new stage in resource allocation. The danger of the 21st century is not of a forced march towards Americanization, but rivalry between economic powers and the globalization of markets and distribution of economic resources.

The global power has attempted and still attempting to distribute wealth in the society. The wealth of nations is not evenly distributed. Some nations are rich in natural resources. Others are rich in both human and natural resources, but lacked technological expertise. The global powers like the USA, Britain, France, Russia, Germany have formed a cartel or grouping as regards use of wealth and how it is distributed across the globe. Most third world nations have resources, e.g. Nigeria has oil or crude oil but cannot exploit them because she depends on advanced nations to use its natural resources.

Self-Assessment Exercise 1

Which countries are regarded as global powers?

2.3.1 Instrument for Wealth Distribution

Although much of the wealth of nations is naturally situated, its distribution is centrally controlled. The wealth owners can hardly have effective control of their wealth because the global powers have signed agreements or given aid as a way of controlling the natural resources or wealth of less developed nations.

The use of multinational corporations The global powers have used and are still using multinational corporations as a means of distributing wealth because they have linked with their home government to repatriate dividends and export both finished and raw materials to anywhere deemed appropriate by the global powers.

We have experienced numerous conflicts and violence as a result of the use of multinational corporations as an engine of growth and for wealth distribution.
Another instrument for wealth distribution is through cartels and the use of threats and loan demons to deal with less developed nations where natural resources are endowed.

For example, the superpower has used threats of assassination and coups to deal with less powerful adversaries developed nations to bow to their whims and caprices. David Allende of Chile was destooled because he refused the USA and its allies control of their natural resources.

Besides, the global powers also use joint ventures and technical exports as a way of distributing wealth to areas where they are not located. The joint venture enables poor nations to be assisted in their wealth exploration and distribution. Most of the Arab world's wealth is found in poor nations that invite the USA and its allied superpowers because they use joint ventures to entice them.

Another instrument for wealth distribution is through globalisation, where the world is a global village, where transactions are concluded through the internet, e-market, and so on. Globalisation has provided ways of making wealth distribution easy. The superpowers have used their technical know-how to improve the distribution of wealth across nations.

Furthermore, the above, via the instrument of regional bodies, Great powers have formed NATO, WARSAW, and European Union's as a way of maximising advantages in wealth utilisation and distribution. Regional bodies have assisted in the distribution of wealth across the globe.

2.4 Problems of Global Power in Wealth Distribution

The place of global powers in wealth distribution has continued to generate confusion and conflicts among great powers that have technological expertise and power, and those nations that have resources without technological advantage. Political instability, violence, and war have resulted from wealth distribution in modern world diplomacy and economic relations.

One of these problems is the problem of financial insecurity experienced by the majority of developing countries. The problems are three factors, namely hasty and disorganized financial liberation, excessive debt, and lack of capital flow into underdeveloped nations from the liberalization of financial markets without the slightest examination of countries in transaction. The IMF orders the liberalization of financial markets without evidence that it stimulates growth and economic development in countries adopting it. This was the case in Nigeria and Russia (NeijibMekache 2007).
An influx of capital into an economy with an immature and insufficiently regulated financial system can do more harm than good. The influx and sudden withdrawal of capital in Southeast Asia and Latin America brought the 1999–1998 crisis and uprising in the Arab world recently.
Another problem resulting from great power wealth distribution is the increased debt of less developed countries that have natural resources

but lack adequate technical know-how and expertise to distribute the wealth.
Many nations have fallen into debt, which has crippled their economies. The G8 initiative, adopted at the Gleneagles summit in June 2005, for the cancellation, in full, of the debt of countries benefiting from the programme for payments of transfer (PPT) with respect to the IMF. The G8 initiative should be extended to non-PPT countries with similar levels of revenue and poverty. Many nations have suffered and are still suffering from debt incurred due to wealth distribution.

Furthermore, political instability has come into the purview of a nation. For example, they have experienced and are still experiencing violence and bomb blasts due to resource distribution and power acquisition. Political hegemony remained the last resort for wealth distribution.
The global power through the IMF introduced privatisation and commercialization of public enterprises. The only access to wealth is through political office. Many were interested in those who could not reach the corridors of power and used violence to change things. The Nigerian state is gradually bleeding into death.

Self-Assessment Exercise 2

What are the problems in wealth distribution?

2.5 Summary

We looked at global powers and the instruments they used to pursue wealth distribution. We also examined some of the problems inherent in wealth distribution based on the focus and louis of global powers. This tendency has resulted in violence, financial crisis, indebtedness of third world nations, and lack of development across the globe.

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2.7 Possible Answers to SAEs

Answer to SAEs 1

The global powers like the USA, Britain, France, Russia, Germany have formed a cartel or grouping as regards use of wealth and how it is distributed across the globe.

Answer to SAEs 2

i. financial insecurity
ii. increased debt of less developed countries that have natural resources
iii. political instability has come into the purview of a nation

UNIT 3 MEANING AND NATURE OF RISK

Unit Structure

3.1 Introduction
3.2 Intended Learning Outcomess
3.3 Meaning of Risk
    3.3.1 Nature of Risk
    3.3.2 Uncertainty and Risk
3.4 Summary
3.5 References/Further Reading/Web Resources
3.6 Possible Answers to Self-Assessment Exercise

3.1 Introduction

Risk is inherent in all human activities, including business ventures, engineering projects, farming, hunting, and operations in self-employed endeavors, among others. Above all, risk is associated with our lives. Therefore, there is more reason why people, for instance, insure against grave happenstance which may jeopardize their existence, incapacitation, or infirmity. Different people have different views regarding the perception of risk. The fundamental consideration is the implication of risk for the corporate existence of business undertakings because of their impact on the economy as a whole. Hence, the discussion in this initial study unit is on the conception of risk.

3.2 Intended Learning Outcomess

By the end of this unit, you will be able to:

- explain the meaning of risk; risk
- describe the nature of risk
- differentiate between uncertainty and risk.

3.3 Meaning of Risk

There are many definitions of the term "risk," which are examined herein so that you can appreciate the nature of risk. An array of definitions is reviewed below to establish a framework for the discussion of risk.

According to Harrington (1999), the term "risk" has a variety of meanings in business and everyday life. At its most general level, risk is used to describe any situation where there is uncertainty about what outcome will occur. Life is obviously very risky; even the short-term future is often highly uncertain.

In probability and statistics, financial management, and investment management, risk is often used in a more specific sense to indicate possible variability in outcomes around some expected value. In a similar vein, Kaye (2001) sees risk from the perspective of an event. Therefore, Kaye opines that risk will be looked at from the viewpoint of whether an incident is likely to occur. It is also necessary to consider how often such an incident could happen and how damaging the incident would be if and when it occurred.

Williams, Jr. and Heins (1985), in their own view, posit that risk is the variation in the outcomes that could occur over a specified period in a given situation. If only one outcome is possible, the variation, and hence the risk, is zero. If many outcomes are possible, the risk is not zero. Therefore, the greater the variation in outcomes, the greater the risk element that will occur. In the perception of Greene and Triechman (1984), risk is described as uncertainly as loss, which poses a problem to individuals in nearly every walk of life. All human beings, regardless of their individual status, must face risk and develop ways to handle it.

For instance, if in business, a loss is certain to occur, the businessman may then plan to mitigate it in advance and treat it as a definite cost to the business. Nevertheless, in the event of uncertainty about the occurrence of a loss, risk comes into play since uncertainty breeds calamity and consequential burden on the business and its fortunes.

Self-Assessment Exercise 1

Explain the term risk.

3.3.1 Nature of Risk

Risk is regarded as naturally inherent in every human activity. And in business, risk is inherently treachery and therefore, despised by investors because of its grave consequences for the fortunes of any corporate entity. Paradoxically, risk is also appreciated by some financial analysts, managers and investors because the presence of risk in a business operation is indicative of the fact that the undertaking is profitable.

Hence, the higher the risk element in a particular venture, the higher will be the return. It implies that managers and investors regard risky venture

as a profitable venture. For instance, petroleum business in either upstream or downstream sector is extremely risky but it is one business that is very profitable around the world. The risky nature of the business, therefore, does not dissuade investors from staking the funds in it.
The following deductions underline the nature of risk:

i. Risk varies in its possible occurrence and outcomes or consequences;
ii. The occurrence of risk and its outcomes depend on chance;
iii. Risk is characterised by uncertainty as to its occurrence and magnitude of loss;
iv. Risk refers to uncertainty because it is inherently linked to uncertainty or chance of a loss;
v. Risk has been described as the possibility that loss will be greater than is normal, expected, or usual.

Hence the nature of risk has informed the rationale for its mitigation because of its unpredictable occurrence in most cases and the magnitude of the loss that do accompany it when it rears its ugly head.
You will appreciate the fact that the understanding of the nature of risk is essential towards preparing human beings and business for instituting measures for mitigating it or even precluding it from occurring.

Self-Assessment Exercise 2

Outline the salient deductions that are inherent in the nature of risk.

1.3.2 Uncertainty and Risk

In business decisions the element of future is dicey in consideration. This is due to the fact that some future circumstances cannot be predicted with precision regardless of the fact that some devices are available for assessing future events.

Nevertheless, under condition of certainty, some events or their outcomes can be determined to some extent. This is possible with the aid of statistical analysis; using statistical deductions to forecast future events or outcomes of such events. For instance, events such as rainfall, sunshine, flood, drought, famine, thunderstorm, typhoon and tornado can be predicted.

On the other hand, under condition of uncertainty, it becomes difficult to predict the future events and the outcomes of happenstance. By implication, decision makers have difficulties in assigning some probabilities to the outcomes of some future events.

Difficulty in predicting future events under condition of uncertainty can arise out of absence of information or lack of knowledge concerning the possible outcomes to expect from such events. Essentially, therefore, it becomes difficult for the decision makers to obtain statistical information and or scientific devices with which to predict the future events and their outcomes with any degree of confidence.

It implies that under condition of uncertainty, the decision makers cannot determine or measure the future events or their outcomes because their probabilities are unknown or not available. And since the possible outcomes of the future events are difficult to predict by the decision makers, it will be very difficult to measure or forecast them with any degree of accuracy.

The above scenario is a common phenomenon confronting managers in their day-to- day managerial decisions. For example, a bank manager may not be able to predict the level of acceptability of a new electronic product or service by the banking public due to the fact that no similar product has been introduced to the public before.

Uncertainty when compared to the element of risk is a subjective occurrence. Therefore, it implies that different decision makers are not likely to come up with similar opinions on the outcomes of decisions taken under condition of uncertainty. Hence, it becomes very difficult to build up unanimously acceptable techniques for dealings with uncertainty.

Nevertheless, the decision makers who are operating under condition of uncertainty normally endeavour to produce some probability distribution of likely outcomes on the basis of their personal judgment regarding the situation under consideration.

For instance, any predication regarding the outcome of acceptance of a new electronic product being introduced by a bank, which is similar to those types being marketed by other banks, is bound to be subject. This is because analysts are likely to come up with varying views, which will be based on their personal judgment.

3.4 Summary

In this initial unit of the study material, we have observed that risk is embedded in uncertainly in terms of loss to individuals and businesses. Businesses and human beings normally plan in advance to mitigate risk and will be treat as a cost. In the event of uncertainty about the

occurrence of a loss, risk would come into play since uncertainty breeds calamity and consequential burden on the business and its fortunes. The condition of uncertainty implies that the decision makers cannot determine or measure the future events or their outcomes because their probabilities are unknown. Therefore, the decision makers who are operating under condition uncertainty normally produce some probability distribution of likely outcomes on the basis of their personal judgment regarding the situation under consideration.

In this study unit, topics covered include the following:
Meaning of Risk
Nature of Risk
Uncertainty and Risk
In the next study unit, you will be taken through the discussion on different types of risk which confront the business entities.

3.5 References/Further Reading/Web Resources

Bickechaupt, D. (1974). *General Insurance*, (9th ed.). Illinois: Richard D.

Chilellezi, O. (2006). *Risk Management for Insurance Practice*. Lagos: Inter Training and Education Services.

Oluoma, R. O. (1999). *Elements of Insurance*. Ikeja: Impressed Publishers.

Pritchet, S.T. et al (1996). *Risk Management and Insurance*. (7th ed.). New York: West Publishing Company.

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3.6 Possible Answers to Self-Assessment Exercise within the Content

SAE 1:
Risk refers to any situation where there is uncertainty or variability about the outcome of an event or decision. Risk involves loss and cost to individuals and business entities. In probability and statistics, financial management, and investment management, risk is often used in a more specific sense to imply possible variability in outcomes around some expected value.

SAE 2:

The salient deductions that underscore the nature of risk are:

i. Risk varies in its possible occurrence and outcomes or consequences;
ii. The occurrence of risk and its outcomes depend on chance;
iii. Risk is characterized by uncertainty as to its occurrence and magnitude of loss;
iv. Risk refers to uncertainty because it is inherently linked to uncertainty or chance of a loss;
v. Risk has been described as the possibility that loss will be greater than is normal, expected, or usual.

UNIT 4: TYPES OF RISK CONTENT

Unit Structure

4.1 Introduction
4.2 Intended Learning Outcomes
4.3 Types of Risk Confronting Business
 4.3.1 External Risks of a Business
 4.3.2 Internal Risks of a Business
4.4 Summary
4.5 References/Further Readings/Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s)

4.1 Introduction

Business entities function in dynamic environment with forces which do affect their operations in varied and differing proportions. Therefore, they operate in an environment that presents various types of risks because their operations are exposed hazards and hiccups as a result of situational dictates. Some business risks are inherently associated with operations. Some other risks arise as a result of the interplay of forces and upheavals of the external environment. In this study unit, therefore, such various types of risk which business organisations have to contend with are discussed.

4.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify the different types of risk confronting a business
- mention and discuss the internal risks of a business
- list and explain the external risks of a business.

4.3. Types of Risk Confronting Business

All businesses face risks regardless of its size of operations, location, types of products produced or services rendered to the public. It is instructive to note that unmitigated risks can spell enormous consequences such as collapse of operations, failure and financial losses.

Therefore, the understanding of such risks by entrepreneurs can help them determine the necessary measures to be adopted in protecting their businesses and investment generally. Business risks range from internal risks to external risks. Some of these risks are systematic risk, unsystematic risk, business risk, liquidity risk, financial risk, exchange rate risk, political risk, market risk, strategic risk, operational risk and compliance risk.

4.3.1 External Risks of a Business

These risks are associated with the dictates of the external environment, which are beyond the control of the firm. These types of risk are as identified and discussed below.

Financial Risk: It is the type of risk which arises as a result of external obligations. It is associated with the possibility that the business may not have enough funds to meet its financial obligations.
Such obligations include debt repayments, dividend payments, payments of taxes, settlement of financial transactions. The risk also encompasses the possibility that external sources of finance may not be available when needed.

Systematic Risk: This is the type of risk that cannot be abridged or predicted in any approach. Therefore, it becomes almost impracticable to protect the business entity against it. Some examples of these risks are interest rate fluctuation, changes in government legislation, and environmental upheavals.

Speculative risk: This type of risk arises as a result of committing funds in high risk investment such as funds used to speculate on oil business and capital market investment.
In the case of capital market investment, some firms in the country took loans to invest in shares during the initial public offer. This was purely speculative in nature. When the bubble in the Nigerian capital market burst, the investments in shares were lost.
The contagious effect on the banking industry contributed to the collapse of some banks that bore the brunt of the speculative attitude of the investors. The so-called marginal loans that were granted to such capital market speculators turned into toxic assets to the banks.

Exchange Rate Risk: This type of risk arises from the fluctuations in foreign exchange rates. This can affect investment in other countries and transactions on imports and exports. The fluctuations in foreign exchange rate, particularly a constant rise in the value of other currencies compared with the value in currency of the home country cause for home industries. The situation would erode the value of the

purchasing power of the firms when related to the payment to be made for foreign supplies for production.

In terms of oversea investment, in the event of exchange rate risk being high, the value of the home currency may be less than the foreign currency. This may erode a significant amount of earnings of the foreign investment.

Market Risk: This type of risk is associated with the price fluctuations or volatility in the market for a firm's products or services. In the event of persistent fall in the market price for the firm's products, the expected revenue would fall and the firm might not be in a position to meet its obligations in operations.

Political Risk: This type of risk involves the risk associated with investment of funds in another country where the political environment is unstable. The risk can crop up as a result of a major change in the political setup.

It implies that the political risk or country risk as the case may be, could devalue the investment and reduce its overall return. Hence, this type of risk is usually associated with emerging or developing countries that are characterized by unstable political or economic scenarios.

Self-Assessment Exercise 1

Mention and explain the various types of external risk.

4.3.2 Internal Risks of a Business

These risks are associated with the internal intricacies of a firm's operations. These types of risk are as identified and discussed below.

Strategic Risk: This type of risk, according to The Institute of Risk Management, is said to be future oriented and can arise when: a new competitor enters a firm's industry; two businesses in the industry merge to create a power house; the firm faces decisions about creating new products; the firm faces decisions about entering new markets; and the firm is considering the location of a disaster recovery site in relation to the main centre of operations.

It is risky when the recovery site is too close to the main centre of operations due to the possibility of the two structures being consumed in an inferno. It is also problematic when the site is far away from the main centre of operations due to communication and logistic bottlenecks.

Self-Assessment Exercise 2

What are the circumstances that give rise to strategic risk in business?

Unsystematic Risk: This type of risk is inherent in or specific to the nature of the assets. In some cases, such risks can be eliminated or guided against through a process called diversification. Some examples of this type of risk are strikes by workers and changes in management decisions.

Liquidity Risk: This is the type of risk which may arise from the fact that the firm may find it difficult to generate enough quantum of funds with which to meet its short-term financial obligations.
The expected illiquidity position is associated with the use of obsolete items of operational equipment which may break down. Hence, the firm would not be able to compete with other firms in meeting market conditions.

Operational Risk: The operational risk is conceptualized as the risk of loss arising from failed processes, people and systems, as well as external events. In other words, operational risk refers to the possibility that transactions or processes can fail as a result of poor design, inadequately trained personnel and external disruptions.
Operational risk also incorporates the risk of frauds and the possibility that the business can fail to meet the contractual obligations of a transaction arising from operational hiccups.

Compliance Risk: This type of risk arises from the possibility that the firm might not comply with laws and regulations within the jurisdictions where it operates, which could spell some enormous costs and thereby affects its fortunes.

This type of risk can also arise as a result of the possibility that the firm might violate the obligations of a legally binding contract entered into in the course of business transactions. The consequences of such violation are in areas of court cases, costs of legal processes, seizure of operational equipment, etc.

Business Risk: This type of risk is inherent in the uncertainty of income caused by the nature of the firm's business. The uncertainty in income generation can arise from problems associated with company's products, ownership structure, composition of the board, management quality and behaviour, and market position.

4.4 Summary

In this study unit, you have understood that there are both internal and external types of risk that the business entities have to contend with in the process of operations. The internal risks are under the control of the business because they can be effectively managed by the organisation. On the other hand, as you have observed, the external risks are beyond the contemplation of the firms. Nevertheless, the firms will still have to plan for their mitigation.

In this study unit, topics covered include the following:
Types of Risk Confronting Business
External Risks of a Business Internal
Risks of a Business

4.5 References/Further Readings/Web Resources

Bickechaupt, D. (1974). *General Insurance*. (9th ed.). Illinois: Richard D.
Chilellezi, O. (2006). *Risk Management for Insurance Practice*. Lagos: Inter Training and Education Services.

Kaye, D. (2004). *Risk Management*. London: Chartered Insurance Institute.

Oluoma, R. O. (1999). *Elements of Insurance*. Ikeja: Impressed Publishers.

Pritchet, S.T. et al (1996). *Risk Management and Insurance*. (7th ed.). New York: West Publishing Company.

Trieschmann, J.S., Gustavson, S.G. & Hoyt, R.E (2001). *Risk Management and Insurance.* (11th ed.). Illinois: Spout Western College Publishing.

4.6 Possible Answers to Self-Assessment Exercises

SAE 1:
The external risks of business are as follows:

i. Financial Risk: It is the type of risk which arises as a result of external obligations. It is associated with the possibility that the

business may not have enough funds to meet its financial obligations.

ii. Systematic Risk: This is the type of risk that is almost impracticable to protect the business entity against it. Some examples of these risks are interest rate fluctuation, changes in government legislation, and environmental upheavals.

iii. Speculative risk: This type of risk arises as a result of committing funds in high risk investment such as funds used to speculate on oil business and capital market investment.

iv. Exchange Rate Risk: This type of risk arises from the fluctuations in foreign exchange rates. This can affect investment in other countries and transactions on imports and exports.

v. Market Risk: This type of risk is associated with the price fluctuations or volatility in the market for a Firm's products or services, which can affect the expected revenue.

vi. Political Risk: This type of risk involves the risk associated with investment of funds in another country where the political environment is unstable.

SAE 2:

The circumstances that give rise to strategic risk in business are as follows:

a. a new competitor enters a firm's industry;
b. two businesses in the industry merge to create a power house; the firm faces decisions about creating new products;
c. the firm faces decisions about entering new markets; and
d. the firm is considering the location of a disaster recovery site in relation to the main centre of operations.

UNIT 5: RISK AND BUSINESS STAKEHOLDERS

Unit Structure

5.1 Introduction
5.2 Intended Learning Outcomes
5.3 Stakeholders and Business Risks
    5.3.1 Inside Stakeholders and Risk
    5.3.2 Outside Stakeholders and Risk
5.4 Summary
5.5 References/Further Readings/Web Resources
5.6 Possible Answers to Self-Assessment Exercise(s)

5.1 Introduction

Business organisations do not operate in a vacuum. Therefore, they operate in a given environment. In fact, business organisations are creatures of the environment. Such an environment comprises stakeholders who have a vested interest in the operations of various business undertakings. Hence, these stakeholders are interested in the risk affecting businesses and how business entities handle the issue of risk is of paramount consideration in their dealings with them. Therefore, in this study unit, we shall discuss the interests of business stakeholders in relation to the issue of business risk.

5.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain business stakeholders and risks
- mention outside stakeholders' risk
- discuss inside stakeholders and risk.

5.3 Stakeholders and Business Risks

Business stakeholders comprise the interested parties in the operations of any business entity. It is not only the owners or shareholders of a business entity that are interested in the fortunes of such a business.

There are other people or groups who have to have a say in how well the business does.
In the opinion of Kaye (2004), the stakeholders of a business entity comprise the people or organisations that could be affected by a risk incident occurring in the organisation itself. This is in consideration of the fact that risk has great potential to threaten the operations, assets, and other responsibilities of any business entity.

For instance, the tsunami that occurred in Japan recently and the tornado witnessed in the western US in 2011 wreaked havoc on both human beings and business entities to the extent that some business ventures have been completely wiped out of existence. Hence, the implication is that all stakeholders in businesses in both countries have incurred monumental losses.

Stakeholders of a business entity are the management, employees, government, labor unions, suppliers, customers, the media, insurance companies, regulators, investors, banks, capital markets, and other business entities.

Self-Assessment Exercise 1:

Explain the stakeholders of a business organisation.

5.3.1 Inside Stakeholders and Risk

There are some stakeholders who are insiders to the business organisation. Such stakeholders from among those identified above are discussed hereunder.

The Shareholders
The shareholders of a corporate entity have vested interest in the company because of their investment. The board of directors of a company is normally constituted to represent the interest of the shareholders in the business. Therefore, the directors will be interested not only in the level of risk exposures of their company but also the measures put in place by the management to preclude and mitigate the operational risks of the business.
The best practice in corporate governance stipulates that the board of directors of a company should, as a matter of policy, have a risk committee that will be charged with the responsibility of overseeing the management of the risk exposure of their corporate entity.

Therefore, the board of directors as stakeholders in a business has the strategic responsibility in partly managing the risk exposure of the business so as to ensure profitable operations and survival of the entity.

Such onerous role of the board is critical towards avoiding disruptions in the company's business operations which may arise from occurrence of risk.

The foregoing discussion attests to the fact that shareholders are exposed to the risk of losing the funds they invest in a company if anything untoward happens to the business.

Management as a Stakeholder

The major preoccupation of any business entity is to maximize profit from its operations. Nonetheless, management recognizes that the goal of profit maximization can be jeopardized in the event of a risk.

Therefore, management is interested in various risks that are inherent in business operations. The understanding of operational risks will assist the management team in instituting appropriate measures to check and mitigate known business risks such as those discussed in the initial unit of this study material.

The management team of any business organisation cannot afford to neglect the issue of risk in operations. This is because business operations are prone to risks, which have been highlighted and discussed in the earlier study unit. For instance, the occurrence of a risk such as a fire outbreak in a factory can be accompanied by a monumental loss of operational assets and the consequence of stoppage of operations.

The Employees

The employees of a business entity have a vested interest in the operations of the organisation. Such an interest is informed by their stake in the revenue of the organisation because their salaries and allowances come from it.

The other areas of employees' interest in the organisation include their morale and pride, which are often reflected in the degree of their self-motivation, level of performance and productivity, and above all, the quality of their work.

The employees of a corporate entity are also interested in maintaining their jobs in order to sustain their personal and family lives, their self-esteem, and the regular receipt of their salaries and allowances. The occurrence of operational loss arising out of risk can jeopardize the company's operations and, by extension, the payment of employees' salaries and allowances.

Hence, the employees would be interested in appropriate management of business operational risks that can guarantee a safe working

environment, the survival of the organisation, enhanced operational fortunes, and organisational effectiveness.

Labour Union

The labor union, which represents the collective interests of the workers in a business entity, also has a vested interest in the operations of the organisation. The union's interest is informed by their stake in the healthy operations of the organisation. This is because the workers' fate is dependent on the survival of the business.

The labor union in any corporate entity is normally preoccupied first and foremost with the profitable operations of the entity. This operational scenario is needed to guarantee the workers' jobs. The occurrence of a loss arising out of operational risk can jeopardize the company's operations, which will eventually impact negatively on the payment of employees' salaries and allowances.

Therefore, the labor union would be interested in appropriate management of business operational risks that can guarantee ideal working conditions, the survival of the organisation, enhanced corporate performance, and organisational effectiveness.

The Suppliers

The suppliers of productive materials, in the case of a manufacturing outfit, and commercial products, in the case of a merchandising business, have a stake in the business. This is because the operational fortunes of the business have an impact on their patronage and payments for their supplies.

The suppliers will be interested in the nature of risks to which the businesses of their customers are exposed so as to influence their level of business dealings with them. This is because of the fact that any occurrence can impact negatively on the stakes of the suppliers.
The suppliers to any organisation will be concerned and depend on its survival to continue doing business with it in the absence of the occurrence of crippling risks. The survival of the organisation will encourage the suppliers to deliver and receive payment for the goods or services contracted.

Sometimes, the loss of one or more large customers resulting from the occurrence of any of the business risks can destroy the business of a supplier of goods and services to such organisations. Therefore, the suppliers will be interested not only in the level of risk exposure of their customers but also in the measures put in place to preclude and mitigate business risks.

The Distributors

The distributors of products for corporate organisations will be interested in the steady supplies of the products. Since no business is immune to operational risks, the distributors will be worried about the kinds of risks that are built into the way their suppliers do business.

Hence, the distributors will be interested not only in the level of risk exposure of their customers but also in the measures put in place to preclude and mitigate business risks.

This is necessary in order to avoid disruptions in their business operations which may arise from the occurrence of risk to the operations of their suppliers.

Most business customers are free to change their sources of suppliers, but it is easier said than done because of the protocol involved in switching to other organisations that have not been doing business with them before. Such protocols include calling for references from their bankers, signing bonds for performance, and making available qualified guarantors.

Industrial customers

The industrial users of the products of a company are major stakeholders in the business because they depend on the suppliers for their productive operations. Any risk that could stop the suppliers from doing their jobs could hurt the users, who are their customers.

Consequently, the disruption of operations may affect their relationships since it will become difficult to fulfill the contractual obligations for suppliers and, hence, such a failure will make the suppliers lose confidence in them.

Therefore, the industrial customers will be interested not only in the level of risk exposure of their suppliers' operations but also in the measures put in place to preclude and mitigate business risks. This is necessary in order to avoid disruptions to their manufacturing operations which may arise from the occurrence of risk to the operations of their suppliers.

5.3.2 Outside Stakeholders and Risk

There are some stakeholders who are outsiders to the business organisation. Such stakeholders from among those identified above are discussed hereunder.

The Government; The government is interested in the overall economy and, by implication, all the productive units, which include all business organisations, are being monitored by the state apparatus. Therefore, the government has a vested interest in the operations of corporate bodies doing business within its territory.

First and foremost, the government is interested in the growth and development of the economy, which can only be ignited and sustained by business entities. Above all, the industrialization efforts of the government are normally complimented and enhanced by business operations.

Business entities do contribute an enormous quantum of funds to the coffers of the government through profit and income taxes, royalties, rents, commissions, surcharges, fines, and duties. In fact, most countries in the world depend on taxes and the charges paid by business entities for executing projects in developing both economic and social infrastructure, besides using such funds to discharge other numerous state obligations.

Therefore, the government will be interested not only in the level of risk exposure of business entities operating within their economy and even those companies of the country's origin but operating abroad (multinational corporations). In addition, the government is also concerned about the measures put in place to preclude and mitigate the operational risks of business entities.

The concern of the government about business risks and strategic measures to preclude and ameliorate such risk exposures is indispensable. Such a posture of government which finds favour in policies and laws is crucial to forestalling the grave impact of the occurrence of operational risk of business operations on the economy.

For instance, the recent oil leakage (occurrence of operational risk) from the offshore facility of the British Petroleum (BP) company along the East Coast of the US caused monumental damage to the ecological environment, loss of fishing grounds by the natives, and displacement of aquatic life from the area affected by the leakage.

The Regulators

There are business and environmental regulators whose actions are geared towards regulating the operations of businesses to ensure that they conform to laid-down best practices in their dealings and protect the environment.

There are various regulators, such as NAFDAC, SON, CPC, EFCC, Customs, and Immigration, which have operational activities, in many different ways, which require them to take a continuing interest in corporate entities' operations and dealings within the country's economy.
If a business doesn't meet the legal and other requirements of these regulators, the business could be fined, have its operations limited, or even have to shut down.

The Media: The media include both print and electronic outlets, such as local and international newspapers, TV and radio stations, magazines for both the general public and professionals, and the Internet.
These media organisations are always on the lookout to bring to the knowledge of the government and the general public any risk exposures of business entities and, above all, reportage of risk occurrences that may not be in the best interests of companies.

A publication by the print media or coverage of an occurrence of operational risk such as the BP oil leakage in the US normally goes a long way to casting a negative image of the organisation. This is beside the fact that a large quantum of finance will be required to settle and clear such operational fallouts as cleanup, compensation, payment of charges, and sundry expenses for court cases in some instances.

The Investors: The investors are those high-net-worth individuals and companies that have surplus funds to invest with the intent of reaping financial benefits in the future.

Most investors are risk averse because they are not interested in losing their funds. In relation to investment in stocks, investors would commit their funds to the shares of companies whose records of managing operational risks are favorable in terms of the measures that they put in place for preventing and mitigating risks.

Therefore, investors would not only be interested in the track record of operational profits based on the critical fundamentals of business strength of the quoted companies. Investors will also be interested in the level of risk exposure of the operations of such companies before committing their funds to their shares.

Furthermore, in order not to lose their funds, investors do take appropriate steps to assess the measures put in place by quoted companies to preclude and mitigate their operational risks. This is necessary in order to avoid losing their funds as a result of consequential

disruptions to the operations of such companies, which may arise from the occurrence of risks.

The Banking Industry: The banking business is dependent on the healthy operations of other businesses, particularly corporate entities. Because of this, banks and other financial institutions will continue to care about the success of the groups to which they have given money.

Once banks perceive a particular industry is prone to greater risk, such as the petroleum industry (both upstream and downstream operations), the cost to be borne by such companies would be very high.

For instance, the BP Company lost a huge quantum of revenue from its operations in the oil spillage in North America, as cited before. In addition, it has to spend a huge amount of funds on the cleanup, compensation, and restoring its damaged drilling facility to normal operation.

The banks that have financial dealings with the company will, one way or the other, be affected as a result of the huge quantum of funds that were lost from the company's revenue, besides funds expended for cleanup, compensation, and restoring its damaged drilling facility.

The Capital Market: The Securities and Exchange Commission and the Stock Exchange are in charge of regulating the operations of the capital market in the country. The quoted companies have their shares listed on the exchange and, therefore, they owe the Commission and the Stock Exchange some obligations in reporting any occurrence of risks to their operations in the course of a financial year.

Such reports can affect the prices of the companies' stocks, and therefore, both capital market authorities would be interested in the measures being put in place to preclude and mitigate their operational risks. This is necessary in order to avoid the loss of investors' funds as a result of consequential disruptions to the operations of such companies, which may arise from the occurrence of risks.

Self-Assessment Exercise 2:

1. Identify the inside stakeholders of a business organisation and

show how they can be affected by risks in operations.
2. Identify the outside stakeholders of a business organisation and show how they can be affected by risks in operations.

5.4 Summary

The analysis in this study unit, as you have understood, indicates that the business stakeholders are also concerned and affected by the risks that the businesses have to contemplate in the process of their operations. For instance, the various stakeholders recognize that they can lose their stakes in the event that their business entities do not have in place mitigating measures with which to manage risks. Hence, they always have to be monitoring the behavior of the management in the handling of risks in order to be rest assured that their stakes are not jeopardized as a result of the occurrence of risks.

In this study unit, topics covered include the following:
Stakeholders and business risks
Risk and Inside Stakeholders
Outside Stakeholders and Risk
In the next study unit, you will be taken through the discussion on people's attitudes to risk.

5.5 References/Further Readings/Web Resources

Bickechaupt, D. (1974). *General Insurance*. (9th ed.). Illinois: Richard D.
Chilellezi, O. (2006). *Risk Management for Insurance Practice*. Lagos: Inter Training and Education Services.

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Pritchet, S.T. et al (1996). *Risk Management and Insurance*. (7th ed.). New York: West Publishing Company.

Trieschmann, J.S., Gustavson, S.G. & Hoyt, R.E (2001). *Risk Management and Insurance.* (11th ed.). Illinois: Spout Western College Publishing.

1.6 Possible Answers to Self-Assessment Exercise(s)

SAEs 1:
The stakeholders of a business comprise the interested parties in the operations of any business entity. These are the people or organisations which could be affected by a risk incident occurring in the organisation itself.

Stakeholders of a business include the management, employees, government, labour union, suppliers, customers, the media, insurance companies, regulators, investors, banks, capital market, and other business entities.

SAEs 2:
The inside stakeholders of business entities are as follows:
The Shareholders: The shareholders of a corporate entity have vested interest in the company because of their investment. The shareholders are exposed to the risk of losing the funds they invest in a company if anything untoward happens to the business.

Management as Stakeholder: The management team recognises the fact that objective of profit maximization can be jeopardized at the instance of occurrence of risk. The occurrence of risk such as fire outbreak in a factory can be accompanied by monumental loss of operational assets and consequence of stoppage of operations.

The Employees: The employees of a business entity have vested interest in the operations of the organisation. Such interest is informed by their stake in the revenue of the organisation because their salaries and allowances come from it.

Labour Union: The labour union which represents the collective interest of the workers in a business entity also have vested interest in the operations of the organisation. This is because the workers' fate is dependent on the survival of the business.

The Suppliers: The suppliers of productive materials, in the case of a manufacturing outfit and commercial products in the case of merchandizing business, have stake in the business. This is because the operational fortunes of the business have impact on their patronage and payments for their supplies.

The Distributors: The distributors of products of corporate organisations will be interested in the steady supplies of the products. The occurrence of risks in operations of a manufacturer could disrupt their business operations regarding the inability of the suppliers to make goods available.

Industrial Customers: The industrial users of the products of a company's are major stakeholders in the business because they depend on the suppliers for their productive operations. The users as customers can be affected by any risk which may disrupt the suppliers' operations.

SAEs 3:
The outside stakeholders of business are as follows:

The Government: Government has vested interest in the operations of corporate bodies doing business within her territory because of the economy. Such posture of government which finds favour in policies and laws is crucial to forestall grave impact of occurrence of operational risk of business operations on the economy.

The Regulators: There are business and environment regulators whose actions are geared towards regulating the operations of the businesses to ensure that they conform with laid down best practices in their dealings and protection of the environment.

The Media: The media organisations are always on the lookout to bring to the knowledge of the government and the general public any risk exposures of business entities and above all, reportage of risk occurrences, which may not be in the best interest of companies.

The Investors: The investors are those high net worth individuals and companies who have surplus funds to invest with the intent of reaping financial benefits in the future. Therefore, they would avoid losing their funds as a result of consequential disruptions to the operations of such companies, which may arise from occurrence of risks.

The Banking Industry: Banking business is dependent on the healthy operations of other business particularly the corporate entities. Therefore, banks and other financial institutions will lose their funds in the event of risk occurring to the corporate entities which are beneficiaries of their loans.

The Capital Market: The Securities and Exchange Commission and the Stock Exchange are in charge of regulating the operations of the capital market in the country. Both capital market authorities would be interested in the measures being put in place to preclude and mitigate

corporate risks so as to avoid the loss of investors' funds as a result of consequential disruptions to the operations of quoted.

MODULE 2

UNIT 1: PEOPLE'S ATTITUDES TO RISK

Unit Structure

1.1 Introduction
1.2 Intended learning outcomes
1.3 Objective and Subjective Elements of Risk
 1.3.1 Objective Element of Risk
 1.3.2 Subjective Element of Risk
1.4 Individual Attitudes to Risk
1.5 Relationship between Risk Aversion & Uncertainty
1.6 Summary
1.7 References/Further Readings
1.8 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

Human beings, particularly investors and managers, have different attitudes towards risk. These diverse postures towards risks by managers and investors alike are precipitated by the nature of risks, which involves their unpredictability generally and the inherent consequences or outcomes therein whenever they occur. The diversity of attitudes of business-minded people gives rise to various classes of people based on their peculiar attitudes to risks. The focus of this study unit, therefore, is on the discussion of such diverse attitudes towards risk.

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explains the objective and subjective elements of risk
- distinguishes between risk and uncertainty
- differentiate between objective and subjective risks
- discuss the different attitudes to risk.

1.3 Objective and Subjective Elements of Risk

Some events and the losses inherent in them can be predicted. This is because such occurrences are common and, therefore, can be predicted with certainty. Nevertheless, some other losses are associated with unexpected events and, therefore, are not predictable.

For instance, the occurrence of fire outbreaks, which can consume all the facilities of a business entity, cannot be predicted accurately even though there are some statistical records on their trends, particularly for the dry season. Nevertheless, the fire outbreaks that occur during the rainy season defy explanation and prediction. Herein is the basis of variations in risk occurrence.

1.3.1 Objective Element of Risk

Risk is embedded in variation in the possible outcomes in a given scenario regarding a risk. Since the timing of the occurrence of risk is uncertain, uncertainty is often used synonymously with risk. Hence, whenever uncertainty is used in place of risk, it usually implies objective uncertainty. This is measurable or quantified because it is used when a measure of variation in occurrences of risk is intended.

A popular measure of variation is the standard deviation. This measure is helpful for use in predicting the expected variation from apparently identical situations which may precipitate different decisions. For example, a manager who is conservative and will always tend to play safe in business decisions that may seem quite risk-free to other decision makers.

A condition of risk implies that the decision maker is confronted with a scenario in which the possible results of his decision are not totally predictable. Nevertheless, such outcomes will most likely fall within a possible range of outcomes. Hence, it implies that there could be more than one possible outcome arising from the choice of an option.

Presumably, the decision maker is understood to know the probability of occurrence of each outcome of his decision. Nonetheless, the decision maker is confronted with the problem of estimating the mathematical probabilities of the occurrence. This problem implies that some errors in estimation or forecast are bound to be involved in the decision maker's prediction.

Basically, there are statistical formulations for determining such errors and measuring them. In fact, the decision maker can make use of his past experience to determine the objective probability and relative frequency of the occurrence of various outcomes. Therefore, measurements could be determined with the support of past experience and available records.
For example, measurements can be determined on such occurrences as seasonal sales figures, cost of production, amount paid as sales commission, quantity of demand in a particular market, population in a segmented market, local authority fees in a geographical area, units of

output in the production of a product, number of customers for a particular product, etc.

Based on personal perspectives, objective risk, which may actually be the same in two scenarios, may be viewed very differently by decision makers who are assessing such a risk.

Therefore, a decision maker's attitude towards risk is equally important besides the knowledge of the degree of objective risk, which altogether influences the person's action.

There are some basic features of risk which influence an individual's reaction to risk situations that are fundamental ingredients in decision-taking toward effective handling of risks.

1.3.2 Subjective Element of Risk

A particular type of event may be of a nature in which it ought to be possible to calculate both the probability and the potential variation in its outcomes. Nevertheless, there are some defects in the quality of data available to risk managers which prevent the calculation of a reliable objective estimate of future loss probabilities.

The common problems or defects inherent in the calculation of future loss possibilities are as follows:

1. Inadequate large samples of data: This refers to the fact that the available details of past experience are based on only a small number of exposure units, and
2. Dynamic nature of risk factors: The dynamic nature of risk factors implies that changes are constantly being observed in risk factors. This has cast doubt on the value of past experience as a guide to the future.

In the above circumstances, decision makers have no alternative other than to draw on their experience and judgment with which to interpret loss trends to arrive at subjective probability estimates.
The implication is that such probability estimates would differ clearly from the fundamental true probabilities. Basically, it is because the estimator's judgment would be affected by his own attitude to uncertainty. So, it means that when risk can't be measured objectively with a reasonable degree of accuracy, it would be necessary to use personal judgment and attitudes.

There appears to be a need for the use of personal judgment and attitudes to estimate the outcomes of risk events; then the subjective element of risk will be manifested. For obvious reasons, subjective risk is seen as the

uncertainty that comes with or is obvious in an event as seen by the person making the decision.

Self-Assessment Exercise 1

Distinguish between objective and subjective elements of risk.

1.4 Individual Attitudes to Risk

Attitudes towards risk differ from one individual to another. The stance on risk is a function of an individual's position in the corporate and investment world. It means that such disparities in attitudes influence investors', financial analysts', and managers' decision-making in terms of investment and commitment of corporate funds to projects. Attitude to risk influences not only the subjective estimates of the probability of the occurrence of loss but also affects such an individual's decisions in handling risk.

Risk Averters

Risk averters are those individuals who have the attitude of taking appropriate measures to avoid incurring risk or the outcomes of risky events. So, to be risk-averse means that a person is not willing to risk more than the expected return in exchange for knowing what will happen.

For example, getting an insurance policy and paying the premium every month means giving up some money in exchange for the insurance company's promise to pay for any expected losses or risks that are covered by the policy.

In insurance parlance, some people refer to this approach as an "exchange of a certain loss of funds," which involves payment of a premium for an uncertain future loss. The critical consideration in the process of the exchange is that the total quantum of premium being paid by the insured is larger than the average or expected loss. This is in view of the fact that insurers' expenses and profit are included in the total premium to be paid by the insured.

Risk Seekers

In the opinion of Pritchett, S., et al. (1996), an investor or manager who accepts risk at less than the expected average loss, perhaps even paying to add risk, such as through gambling, is a risk seeker.

One person may be very cautious and averse to taking chances in investment, whereas another may be highly optimistic regarding future uncertain outcomes regarding risky investment. The former, in terms of attitude to risk, is risk averse, and is likely to arrive at higher loss probability estimates, while the latter, who is less likely to arrive at higher loss probability estimates, is the risk optimist.

Someone who is strongly averse to accepting even the smallest variation in outcomes from the expected may choose to insure. Nevertheless, an individual who is less strongly averse to accepting even the smallest variation in outcomes from the future expectation of loss will be less risk averse and may be prepared to carry the risk himself. This is the stance of a risk-seeker.

Risk Neutrals

Pritchett, S. et al. (1996) posit that a person willing only to pay the average loss as a premium would be considered risk neutral. It means that such individuals are not ready to assume risk and, at the same time, are not prepared to stake more than necessary in either preventing risk or transferring the loss to an insurance company.

The pertinent issue at this juncture is: what makes one person more risk-averse than another? This issue borders on the realms of psychology, sociology, or anthropology. Nevertheless, it can be assumed that factors such as family and societal influences, genetics, and religious and philosophical beliefs all play an important role.

1.5 Relationship between Risk Aversion and Uncertainty

To some extent, there is some ambiguity in the relationship between a person’s risk aversion and his uncertainty. A problem arises as a result of the imprecise way the twin terms aversion and uncertainty are commonly used. Nevertheless, in some respects, uncertainty could be affected by aversion.

For example, a decision maker might be so distrustful of risk in general that he/she would tend to disregard his/her own judgment regarding a particular risk, which might be driven higher by her/his aversion to risk.

In some other scenarios, it is possible to say that uncertainty influences aversion. This is because a person who is consistently exposed to an environment of seemingly random and unpredictable events such as typhoons or tornadoes might eventually develop a high level of aversion to risk (Williams, Smith, and Young, 1995).

Some writers have taken a different perspective in relating risk, risk aversion and uncertainty to one another. In their own view, William and Heins (1989) regard risk as consisting of objective and subjective components. According to them, objective risk refers to the measurable component of risk, while subjective risk reflects an individual's reaction to or attitude towards risk.

On the basis of the above approach, uncertainty becomes an aspect of subjective risk. Basically, there are other views, and perhaps the best that can be discerned is that risk aversion and uncertainty are distinct concepts

that are not fully independent of one another (Williams, Smith, and Young, 1995).

Self-Assessment Exercise 2

1. Differentiate between risk aversion and risk neutral.
2. Briefly explain the relationship between risk aversion and uncertainty.

1.6 Summary

Some risk events and their losses can be predicted because such occurrences are common and, therefore, can be predicted with certainty. However, some losses are associated with unexpected events and, therefore, cannot be predicted. Attitudes towards risk differ from one individual to another. The different postures towards risk by individuals influence decision-making in investment and commitment of corporate funds into projects by investors, financial analysts, and managers. Hence, there are individuals who are risk averters, while others are risk seekers, and yet there are risk neutrals.

In this study unit, topics covered include the following:

- The Objective Element of Risk
- The Subjective Element of Risk
- Individual Attitudes to Risk
- Uncertainty and Risk Aversion

In the next unit, you will be taken through the discussion on costs associated with risk.

1.7 References/Further Readings

Bickechaupt, D. (1974). *General Insurance*. (9th ed.). Illinois: Richard D.
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1.8 Possible Answers to Self-Assessment Exercise(s) within the Content

SAE 1:
An objective element of risk arises when the decision maker makes use of his past experience and available statistical records to determine the objective probability and relative frequency of the occurrence of various outcomes.

On the other hand, the subjective element of risk implies that when risk cannot be measured objectively with some reasonable level of degree of accuracy, personal judgment and attitudes of the decision maker will be used to estimate the outcomes of a risk event.

SAE 2:
Risk aversion implies that those individuals involved have the attitude of taking appropriate measures to avoid incurring risk or the outcomes of risky events. This presupposes that to be risk averse, an individual is not willing to stake in excess of the expected return in exchange for some certainty about the future.

Risk neutrals refer to people who are only willing to pay the average loss as a premium because such individuals are not ready to assume risk and, at the same time, are not prepared to stake more than necessary in preventing risk or transferring the loss to an insurance company.

SAE 3:
The uncertainty element of risk influences aversion because a person who is consistently exposed to an environment characterized by seemingly random and unpredictable events such as typhoons or tornadoes might eventually develop a high level of aversion to risk.

UNIT 2: COSTS ASSOCIATED WITH RISK

Unit Structure

2.1 Introduction
2.2 Intended Learning Outcomes
2.3 Costs Associated with Risk
    2.3.1 Costs in Nature of Risk
    2.3.2 Private & Social Costs Inherent in Risk
    2.3.3 Losses Arising from Risk
2.4 Summary
2.5 References/Further Readings
2.6 Possible Answers to Self-Assessment Exercise(s)
2.7

2.1 Introduction

Every type of risk comes with its own unique set of associated expenses. This is because the occurrence of any risk in the operations of any business entity portends some costs and losses that have to be borne by the organisation. This is the case given the fact that any risk can occur in the operations of any business entity. Some of these costs are ordinarily carried by the organisations that are informed of compensation and damage to the operating facilities of the organisations, while others of these costs are incurred since the nature of the risk itself makes them inevitable.

In addition, the communities in which various companies conduct their business are also responsible for some of the costs that are incurred as a result of the occurrence of risk as a result of the actions of such businesses. Therefore, in this section of the curriculum, the many expenses that are associated with taking risks are enumerated and discussed.

~~1.2~~2.2 Intended ~~learnig~~Learning Outcomes

~~At~~ By the end of this unit, ~~students should~~you will be able to:~~;~~

- ~~-~~mention costs associated with the nature of risk~~,~~
- distinguish between private and social risks
- ~~and~~ identify the various types of losses that are inherent in risk.

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1.2.0 3.3 Costs Associated with Risk

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Costs associated with risk refer to the obvious implications or consequences of the occurrence of risk in organisational operations. The costs, which are inherent in the nature of risk and its sharing among organisational stakeholders, are discussed below.
The various costs of risk are in various categories, which are identified and discussed below.

1.2.1 2.3.1 Costs in the Nature of Risk

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The various costs inherent in the nature of risk consist of three things: risk handling costs, costs of losses that occur, and costs due to the existence of risk.

a. Risk Handling Costs: These risk handling costs are in the areas such as follows:

i. The costs involved in identifying, evaluating, and treating risks
ii. insurance premiums
iii. Charges for loss prevention devices
iv. Fees for consultancy services
v. Opportunity costs in terms of management and staff time spent on dealing with risks, which cannot be devoted to other activities.
vi. The cost of avoiding a risk may be a loss of revenue derived from the particular activity involved.

Costs of Losses Arising from Risk
These costs happen because there is risk in the way the organisation works, and they are as follows:

1. Direct costs to a Firm: These elements of cost in risk from industrial accidents can arise as a result of the following:

Compensation is payable to injured employees Damage to machinery, equipment and work in progress Loss of production Accident investigation expenses.

2. Indirect costs:

These elements of cost in risk can arise as a result of the following:
Other employees may either stop working for a short time or their work rate may slow down from the occurrence of risk.

Decreased morale of workers from the occurrence of risk consequent drop in productivity and an increase in spoilt materials from the occurrence of risk.

Loss of future earnings from the occurrence of risk

3. Costs Attributable to the Existence of Risk: For the following reasons, these elements of cost in risk do arise:

The welfare loss suffered by those exposed to risk, for example, to a risk averter, is referred to as risk exposure.

Externality of risk: this refers to indirect costs which are borne by the rest of society as a result of the occurrence of risk.

In the event that the potential losses from the occurrence of risk are so critical that the firm involved cannot produce its particular product, the consumers will be deprived of the satisfaction they would have derived from its consumption. In addition, other stakeholders would lose their stakes in the company.

Self-Assessment Exercise 1

Identify the forms of cost associated with losses arising from risk.

~~1.2.2~~2.3.2 Private & Social Costs Inherent in Risk

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The costs being shared among some individuals and groups in society are private costs and social costs. Private costs are costs necessarily incurred from the occurrence of risk by the individual or firm which is affected by the outcomes of the risk. The community in which a company operates bears some costs from its operational activities; such a burden constitutes the social costs.

For instance, in the process of production, the company can discharge untreated pollutants such as effluents into the community source of water supply coupled with smoke discharged into the air from the factory. Such pollution constitutes the private cost of the company's operations to the community.

In many countries, the company may be compelled by law to spend some money on the cleanup of the above pollution in the community in addition to the general expense of the pollution. Such costs will appear in the company's accounts as a part of its private costs. So, this means companies have to follow government rules that say they have to pay for all the consequences of their actions.

Both private and social costs may be inherent in many pure risks. A major fire incident may render a factory inoperative and, as a result, necessitate loss of employment by the workers, besides the loss borne by some other stakeholders.

The company involved could be compelled to bear part of these social costs, such as redundancy payments to workers and the payment of compensation to some third parties for personal injury or damage to their property.

Furthermore, an explosion from a factory producing explosives may cause extensive damage to surrounding properties and injuries to members of the public. Another example is the leakage of contaminated sludge from a factory, polluting the surrounding land and river, depriving the community of their source of livelihood and water supply.
In the latter case, the company would be compelled to expend some funds on cleanup of the land and the river of the deadly sludge. In both cases, payment of compensation would also be borne by the companies to the affected members of the public for their injuries and damaged property and on the damaged farmlands, respectively.

The above cases involve both private and social costs borne by the companies and the communities alike. In line with best practices in organisational operations, the companies, in the absence of a legal obligation to compensate the injured third party, may feel morally duty-bound to offer some payment to the communities and individuals affected by the risk.

2.3.3 Losses Arising from Risk

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The undesirable outcome of risk involves an economic loss. This is because there are some benefits which are associated with some forms of risk.

The undesirable end result of risk signifies some loss of benefits which would have accrued from the use of a property. Such an undesirable element of risk involves the decrease or disappearance of value.
The undesirable end of risk is usually in an unexpected or at least relatively unpredictable manner. Since it is associated with risk, the outcome, which is not desirable, would be unpredictable in pecuniary magnitude as well as in the extent of its impact.

There are, however, some other losses that can be expected in nature. This is due to the fact that they are known to always occur. Examples are death, which terminates a bread winner’s life, collateral damage resulting from conflict, depreciation of physical properties, etc.

The above examples of loss are capable of being predicted by decision makers fairly accurately. This is required because, in the case of depreciation, the mere fact that it occurs to a capital asset prepares accountants' minds to set aside some funds for their replacement.
In the case of death, the insurance company encourages people to insure their lives against such an expected loss in order to use the proceeds of such a policy to cater for their dependents after its occurrence.

Nevertheless, as observed by Bickechaupt (1974), many losses cannot be predicted as a result of risk. Examples of such losses include:

a. loss of property due to fire.
b. loss of vehicle because of theft, and
c. Other valuables are lost because of other perils.

Some other losses include:

i. loss of income due to property destruction,
ii. loss of job due to the personal perils of disability and illness,
iii. increased medical costs due to terminal illness, and
iv. loss of assets due to legal liability for losses affecting other people.

Self-Assessment Exercise 2

1. Differentiate between private cost and social cost in relation to risk.
2. Mention losses that are associated with occurrence of risk.

2.4 Summary

You will have appreciated from the discussion in this study unit that risk has some cost implications for the operations of all organisations. Such costs include risk handling costs, losses from risk, and costs attributable to the existence of risk. There are also private and social forms of costs inherent in the occurrence of risk in the operations of corporate entities. As you have understood from the discussion, some causes of risk include perils and hazards, which do aggravate the occurrence of risks to both human beings and corporate entities. Some losses are also inherent in the occurrence of risk, such as loss of property, loss of vehicle, loss of valuables, loss of income, loss of job, increased medical costs due to terminal illness, and loss of assets.

In this study unit, topics covered include the following:

- Costs in the Nature of Risk
- Risk carries both private and social costs.
- Losses Arising from Risk,

2~~1~~.5 References/Further Readings

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~~Trieschmann, J.S., Gustavson, S.G. and Hoyt, R.E (2001). Risk~~

~~Management and Insurance, 11th Ed, Illinois: Spout _ Western College Publishing.~~

~~**Further Reading**~~
~~Kaye, D. (2004). Risk Management, London: Chartered Insurance Institute.~~

2~~1~~.6 Possible Answers to Self-Assessment Exercise(s) ~~within the content~~

SAE 1:

The various costs inherent in the nature of risk consist of the following:

1. Risk handling costs include: costs associated with identifying, evaluating, and treating risks; insurance premiums; charges for loss prevention devices; fees for consultancy services; opportunity costs in terms of management and staff time spent dealing with risks that cannot be devoted to other activities; and costs of avoiding a risk, which may be a loss of revenue derived from the particular activity involved.
2. Costs of Losses arising from Risk: These costs occur from risk in organisational operations, which are:

loss of production; and accident investigation expenses (all of which are considered direct costs); and stoppage of work; decreased morale of workers; consequent drop in productivity; increase in spoilt materials; and loss of future earnings from the occurrence of risk (all as indirect costs). These elements of cost in risk arise from welfare loss suffered by those exposed to risk and the externality of risk as indirect costs borne by the rest of society as a result of the occurrence of risk.

SAE 2:

Private costs are costs incurred from the occurrence of risk by the individual or firm that is affected by the outcomes of the risk. In a case of pollution of the environment, the company would be compelled to expend some funds on cleanup of the land and the river of the deadly sludge in addition to payments to the affected members of the public for damaged property and farmlands.

When the community in which a company operates bears some of the costs of its operational activities, there is a social cost in risk. An example is the leakage of contaminated sludge from a factory, polluting the surrounding land and river, depriving the community of their source of livelihood and water supply.

SAE 3:

Losses that are associated with the occurrence of risk are as follows:

i. loss of property due to fire.
ii. loss of vehicle because of theft, and

Other valuables are lost because of other perils.

i. loss of income due to property destruction,
ii. Job loss as a result of personal perils such as disability and illness; increased medical costs as a result of terminal illness; and
iii. loss of assets due to legal liability for losses affecting other people.

UNIT 3: CAUSES OF RISKS

Unit Structure

3.1 Introduction
3.2 Intended Learning Outcomes
3.3 Some Causes of Risk
- 3.3.1 Perils in Business Operations
- 3.3.2 Hazards in Business Operations
- 3.3.3 Uncertainties in Business Operations

3.4 Summary
3.5 References/Further Readings
3.6 Possible Answers to Self-Assessment Exercise(s) within the Content

~~1.1~~3.1 Introduction

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The operations of any given corporate entity are not the only place where risk of any kind might occur. In most cases, certain circumstances or events serve as the impetus for the occurrence of a risk. To put it simply, risk occurs as a result of certain factors that are associated with the nature of the operations, the behavior of the workers, the types of facilities that are used in the business, the behavior of the parties dealing with the business, and most importantly, the disruptions that occur in the external environment. As a result, this study unit will focus on identifying and discussing a variety of different factors that contribute to risk.

3~~1~~.2 Intended ~~learnig~~Learning Outcomes

~~At~~ By the end of this unit, you ~~should~~ will be able to:

- mention and explain various causes of risk
- identify perils in business operations
- identify hazards in business operations
- mention uncertainties in business.

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~~1.3.1~~ 3.3 Some Causes of Risk

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There are some causes which can precipitate the risk taking place. Such causes are inherent in human nature, environmental conditions, and mechanical operations. Such causes of risk are identified and discussed below.

1. Inadequate Cash Flow

This arises when the management, in the case of large entities, or business owner, in the case of small businesses, does not monitor closely the expenses and accounting records of the operations. The result is that the flow of cash into the business will be jeopardis~~z~~ed.

A cash flow problem can also arise when customers are not purchasing products or patronizing the services of a business. Internal problems such

as lack of planning ahead for contingencies can also precipitate cash flow deficiency. So, it's best for a business owner to have three months' worth of operating costs saved up so that they can keep the business going during hard times.

2. Labour Unrest

Labour problems can precipitate risk in the operations of a business entity. In the event of labour unrest, which can emanate from disagreements between management and labour, operations or production will suffer, and therefore, the business will incur an abnormal loss. Labour unrest can take the form of strikes, stoppages, work to rule, and picketing, among others.

For instance, British Airways has gone through a long period of labour unrest in recent years. The consequences of such labour unrest include loss of revenue, loss of market share, etc. In Nigeria, the Nigeria Labour Congress (NLC) has always led labor unrest on issues such as fuel price increases, national minimum wage, and so on.

The consequences include loss of valuable man hours, a decrease in economic output, disruptions in socio-economic operations, etc.

3. Weak Internal Controls

When corporate entities do not have sound financial and accounting policies, the result is weak internal controls. This is because, in the absence of such policies, there would be no meaningful checks and balances in the operations of the entities, and the result would be loss of revenue, weak cash flow, fraud, embezzlement, and other related problems.

4. Weak Corporate Governance

The absence of good governance in the operations of an entity is indicative of the fact that the best practices for corporate governance issues are not being observed by the management, the board of directors, and the chief executive officer of such organisation.
Therefore, in such a situation, the normal operational protocol will be breached in the management of the funds of the organisation. This results in fraudulent practices, embezzlements, bad debts, illiquidity, and financial distress, etc.

5. Investment in Risky Ventures

Some funds of an organisation may be invested in risky ventures such as speculative businesses to the extent that it becomes difficult to recover such funds in the event that the business goes awry. Examples are the loans advanced by the banks to the capital operators, which invariably become lost to the vagaries of the speculative market. These risky loans

turned into toxic assets on the banks' books, which helped cause their weakness and financial trouble.

6. Operations in a Volatile Environment

Investments and operations in a volatile environment can increase business risk. Investment and operations in a politically unstable environment can lead to the loss of funds and, at times, the whole investment will be wiped off by socio-political uprisings.

7. Poor Planning

Poor planning can lead to what is called "one-dimensional thinking," which can lead to the risk of sinking the operations of the business. For instance, a lack of creative ways of attracting customers by business owners in the face of fierce competition can sink a business.

Self-Assessment Exercise 1

Mention and explain some causes of risk in business operation

3.3.1 Perils in Business Operations

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Peril is regarded as a major cause of risk. Forms of peril in relation to risk include the following: Accidents, thefts, earthquakes, windstorms, floods, and illness, to name a few.

According to the law, perils are regarded as "acts of God" in relation to those perils operating without human agency or intervention and not preventable by human foresight or care.
For example, fire outbreaks precipitated by lightning are often regarded as an act of God because human beings cannot cause lightning to take place. Other examples of acts of God include: storms, floods, typhoons, tornados, tsunamis, and other grave dictates of nature.
The above upheavals of nature indicate that such causes of risk come in various forms and the magnitude of their impact on business operations also varies considerably.

3.3.2 Hazards in Business Operations

Hazards are the various contributing factors to the occurrence of perils. Generally, there are many separate hazards that are associated with any particular object or person. The sum total of hazards normally constitutes perils which can precipitate a particular risk.

In insurance parlance, business hazards are categorised into physical hazards and moral hazards. These classes of hazards are discussed below.

Physical Hazards: Physical hazards are the tangible conditions or characteristics of a risk that influence the frequency and/or severity of loss inherent in the risk. These tangible or physical conditions of risk include considerations such as:

a. location,
b. structure,
c. construction,
d. occupancy,
e. security protection, and
f. exposure, etc.

Particularly, physical hazards include conditions such as:

i. waste paper piled under a staircase gasoline stored on the premises;
ii. weak construction which may fail in a heavy wind;
iii. unsafe brakes on a car;
iv. holes in a sidewalk;
v. inadequate inventory checks in a store;
vi. improper water drainage systems, etc.

Each of the above-mentioned factors can make it more likely that a loss will happen due to a specific danger, such as fire, wind, flood, theft, etc.

Moral Hazards: The term "moral hazard" is used in reference to those factors that have their origins embedded in the mental attitudes of human beings that may influence the outcome of a risk. This concerns hazards precipitated by dishonesty, insanity, carelessness, indifference, etc.

The above list is by no means exhaustive. Hence, there are other similar human attitudes that are psychological in nature.

In drawing a distinction between moral and morale, Pritchett et al. (1996) observe that moral hazards involve dishonesty on the part of the insured. In the context of insurance, moral hazards refer to conditions that encourage the insured to intentionally cause losses. Basically, moral hazard exists when a person can gain from the occurrence of a loss.

For example, an insured person who will be reimbursed for the cost of a new car due to the loss of an old one has the motivation to cause loss to the car. This fraudulent incentive on the part of the insured increases the probability of loss.

Morale hazards, in contrast, do not involve dishonesty on the part of the insured. To a certain extent, morale hazards are attitudes of carelessness and lack of concern that can increase the chance a loss will occur or increase the size of losses that do occur (Pritchett et al., 1996).

For instance, poor housekeeping, such as allowing waste papers to accumulate in the attic or basement of a building, and the occupant's habit of careless cigarette smoking are examples of morale hazards that increase the probability of loss by fire.

Frequently, such a lack of concern on the part of human beings occurs due to the fact that an insurer is available to pay for losses as there will be reimbursement to return the insured to his position.

Nonetheless, Pritchett et al. pointed out that distinguishing between moral and morale hazards is difficult, and their presence can often lead to physical hazards. But they also remarked that hazards are critical characteristics to analyze because people’s ability to reduce their effects will reduce both overall costs and variability. Hence, management of hazards can constitute a highly effective risk management tool.

3.3.3 Uncertainties in Business Operations

There are some uncertainties in the environment of all business entities that make their operations generally risky. Such threats to business operations are identified and discussed below.

i. Political: This involves issues such as guerilla war against the state; revolution; changes in government (through elections or coup d’état); and political turmoil.
ii. Government policy includes things like fiscal and monetary reforms, price controls, trade restrictions, nationalisation, economic regulation, barriers to bringing back earnings, etc.
iii. Macroeconomic: This is in areas such as inflationary trends, changes in relative prices, fluctuations in foreign exchange rates, and depreciation in terms of trade, etc.
iv. Socio-cultural: This is in areas such as changing social concerns, social unrest, riots, demonstrations, terrorist attacks, militant movements, social dissension, etc.
v. Geographical: This is in areas such as rainfall variation, change in climatic conditions, and problems of drought and desertification.
vi. This is in areas such as uncertainty in quality of supplies, shifts in market supply, changes in prices of supplies, inordinate behavior of suppliers, etc.
vii. Product Market: This refers to changes in consumer tastes, the availability of close substitutes, the scarcity of complementary goods, changes in substitute prices, and so on.
viii. Competition: This concerns rivalry among existing competitors, new entrants, and technological uncertainty in relation to product innovations and process innovations.

ix. This concerns input supply uncertainty, raw material shortages, quality changes, spare parts restrictions, machine failures, power failures, production disruptions, etc.

x. Liability: This concerns product liability; liability to the community as a result of pollution; liability to employees resulting from industrial accidents; liability to other people because of damage to their property; etc.

Self-Assessment Exercise 2

1. What are the forms of peril in relation to risk?
2. What are the forms of hazards in relation to risk?

31.4 Summary

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As a result of the discussion that took place throughout this unit of study, you now understand that there are many different elements that might produce risk. Some of these elements, which might have a detrimental impact on the operations of corporate organisations, are intrinsic to the business' day-to-day activities, while others are connected to the external environment. There are a variety of factors, such as the threats and dangers that their activities are exposed to, that might exacerbate the risks that businesses face.

In this study unit, topics covered include the following: Some Causes of Risk Perils in Business Operations Hazards in Business Operations Uncertainties in Business Operations
In the next unit, you will be taken through the discussion on the scope and benefits of risk management.

31.5 References/Further Readings

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~~Further Reading~~
~~Kaye, D. (2004). Risk Management, London: Chartered Insurance Institute.~~

3~~1~~.6~~5~~ Possible Answers to Self-Assessment Exercise(s) ~~within the Content~~

SAE 1:
Some causes of risk in business operations include the following:

i. Inadequate Cash Flow: This arises when the management (or business owner) does not closely monitor the expenses and accounting records of the operations.
ii. Labor Unrest: Labor issues can exacerbate risk in a business entity's operations. Labour unrest can take the form of strikes, stoppages, work to rule, and picketing, among others.
iii. Weak Internal Controls: When corporate entities do not have sound financial and accounting policies, the result is weak internal control that leads to loss of revenue, weak cash flow, fraud, embezzlement, and other related problems.
iv. Weak Corporate Governance: The absence of good governance in the operations of an entity leads to fraudulent practices, embezzlement, bad debts, illiquidity, and financial distress, etc.
v. Investment in Risky Ventures: Funds invested in risky ventures, such as speculative businesses, are difficult to recover if the business fails.

vi. Operations in a Volatile Environment: Investing and operating in a politically unstable environment can result in a loss of funds, and in some cases, the entire investment can be wiped out by socio-political uprisings.

vii. Poor Planning: Poor planning can lead to what is called "one-dimensional thinking," which can lead to the risk of sinking the operations of the business.

SAE 2:
Forms of peril in relation to risk include the following:
Accidents, thefts, earthquakes, windstorms, floods, and illness, to name a few.

SAE 3:
Hazards in relation to risk include the following:
location,
structure,
construction,
occupancy,
security protection,
exposure,
dishonesty
insanity.
carelessness
indifference.

UNIT 4: GLOBALISATION AND BUSINESS RISKS

CONTENT

~~1.1~~4.1 Introduction
~~1.2~~4.2 Intended ~~learnig~~Learning Outcomes
~~1.3~~4.3 ~~Title of the Main~~
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~~1.3.2~~4.3.1 Global pandemic risk
~~1.3.3~~4.3.2 Infrastructure risk
~~1.3.4~~4.3.3 Supply chain risk
~~1.3.5~~4.3.4 Food security
~~1.3.6~~ 4.3.5 Geo-political risk
~~1.4~~4.4 Summary
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~~1.6~~4.6 Possible Answers to Self-Assessment Exercise(s) within the Content

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4.1~~1.1~~ Introduction

Businesses have always been required to contend with worldwide threats. The idea of a systemic risk, which is defined as a threat that can quickly spread across multiple nations and organisations, has captured the imagination of the general public during the past few years. This research identifies areas that may be susceptible to systemic risks and provides recommendations on how businesses may begin to mitigate those risks. The advent of globalization has presented companies with advantages and prospects that have never been seen before. The hazards that society and businesses confront have been both altered and increased as a result of this. As a direct result of globalis~~z~~ation, the number of risk factors as well as the rate at which they are spread has significantly increased. This presents a number of new risks, including vulnerabilities resulting from the usage of shared infrastructure platforms (such as electricity, the internet, and transportation), as well as larger risks posed by new and mostly unquantifiable shocks to the system.

In a world that is rapidly globalizing, the new risks are the cascading failures caused by the collapse of some critical node in a network; both the physical damage that may be caused as well as the rapid change in perceptions to manage these risks. These new risks include both the physical damage that may be caused as well as the rapid change in perceptions to manage these risks.

The task at hand for businesses is to familiaris~~z~~e themselves with these risks across a diverse range of industries, to heighten their sensitivity to

the activities or developments that constitute them, and to become more alert to the warning signs that suggest a destabilizing event may already be gathering momentum. With this increased comprehension, firms will be better prepared to plan for and react to the risks that they face.

If companies do not strengthen their capacity to weather shocks and do not take steps to prepare for more significant ones, they will not be able to prevent or respond to hazards as effectively as they could. In this unit selected a number of risks which have changed significantly as a result of the past 20 years of rapid globalisation. These are illustrative of the way in which global integration has led to new forms of systemic risk. It is not intended to be an exhaustive list and there are a number of risks, not least those associated with the environment and climate change, which are not covered within this unit.

4.2~~1.2~~ Intended ~~learnig~~Learning Outcomes

At the end of this unit, students are to become familiar with the concepts and motives of economic globalization and understand the different types of firm/organisation risk in the world. It is expected to understand the factors that aid globalis~~z~~ation.

~~1.3 Title of the Main~~

~~1.3.1~~4.3 Economic and Financial Risk

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The success of globalis~~z~~ation in producing global growth and growing wages has led to a hazardous complacency in economic orthodoxy and an inability to recognize the warning indicators. This failure to recognis~~z~~e the warning indications has led to an increase in the risk of economic instability. In the context of a global environment characteris~~z~~ed by rapidly opening markets, increasing connectivity, population expansion, and seemingly limitless computing power, governments and their economic advisors felt confident that the policy recommendations they were making would facilitate further growth.

Risks to business: Credit crunch

As banks and other financial institutions cut back on the amount of credit they can give, there are a number of bad things that happen to businesses: It is difficult for businesses to borrow money from financial institutions and, therefore, expand.

Reduced credit adds to the pressures up and down the distribution chain. Suppliers are paid with increasing delays, and customers are expected to pay more promptly. As these demands cannot be passed on, they in turn reduce the liquidity of suppliers' customers and can lead to a cascading liquidity crisis and bankruptcies.

A welcome boost to certain markets in good times can compound the difficulties when this turns into an investment drought during a global crisis. At the end of 2008, foreign investors owned 41.5% of shares listed on the London Stock Exchange. In 2009, it was reported that the uncertainty created by the economic recession caused investors to pull £1 trillion out of the UK economy. The financial crisis increased the pressure on the City.

Consumption

Consumers lose faith as credit becomes more difficult to obtain and as the government continues to make cuts to the central budget; as a result, consumers begin to reconsider the order in which they spend their money. During the past two to three years, the demand for consumer products and services has remained flat in Europe and North America. However, solid growth in China and other quickly rising emerging countries has helped global corporations to mitigate some of the negative effects of this trend. The economic crisis has had a widely diverse influence on various retail sectors, with some retail sectors being able to better weather the stresses of the slump than others. Despite a general decrease in sales for the year, the restaurant industry in the United States recorded double-digit growth in 2009, making it the fastest growing industry in the country. The market for luxury products has experienced a significant decline. For instance, the global sales of luxury apparel, jewelry, and fashion accessories are estimated to have decreased by about 8% in 2009, according to the consulting firm Bain & Company. This decline was attributed to the declines in the three mature markets of the United States, Japan, and Europe, which still make up approximately 80% of global sales.

~~1.3.2~~4.3.1 Global Pandemic Risk

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At the same time as national borders are opening up to allow for more extensive and lucrative trade, we are also exposing ourselves to a larger variety of infectious diseases and parasites. The fact that we have decreased natural diversity in order to increase our production and transport capacity has made the threat significantly worse. This is due to the fact that both diversity and devastating pandemics existed prior to the development of globalized networks of trade, people, and services. Because of this, the complete effects of a pandemic cannot yet be determined. A highly infectious disease whose initial rate of transmission outpaces our capacity to detect, contain, or immunize against it is an

example of a particular category of health threat known as a pandemic. Pandemics put the entire human population in danger because they outpace our ability to detect, contain, or immunize against them. This danger usually manifests itself in the form of a contagious virus that strikes a particular population of animals; pigs, chickens, and cows are the most prevalent vectors of transmission.

For such a virus to take on pandemic proportions, three conditions must be met. First, the number of host animals must be large enough and close enough together for more and more dangerous strains to develop and change.

Secondly, infected animals must have intensive human contact to afford the virus opportunities to develop efficient bridges across the species barrier. Third, once the virus has accomplished that feat, it requires a rapid and extensive transport mechanism to stay ahead of naturally and artificially occurring immunities in infected populations.

Risks to business

Human resources

The impact of any pandemic on the human resources of a business will entirely depend on the nature of the pandemic and whether or not it targets people of working age. However, a Department of Health publication advised businesses to assume, in the event of an influenza pandemic, that 50% of the workforce would require time off at some point for anything between seven to ten working days. Employers will also need to consider their health and safety obligations during a pandemic, which may require additional costs for preventive measures.

Suppliers and services

There will be knock-on consequences on the provision of services and the delivery of critical supplies as a result of a reduction in the global workforce. These knock-on impacts could affect fundamental services such as the supply of energy, the collection of waste, and food stocks.

Customers and markets

The decisions that customers make may also be influenced by factors such as physiological dread, travel limits, and illness. Businesses who were accustomed to serving consumers from all over the world may discover that their customer base has diminished. As a result, these organisations will need to reorient their business strategy to focus on national or local markets.

4.3.2 Infrastructure Risk

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Because the condition of our essential infrastructure (electricity, gas, oil, telecommunications, water, agriculture, heating, health, transportation, and financial services security) is critical to both our economies and our safety, it requires continual monitoring. The dual trend of increasing population demand for services, along with increasing per capita use of these services as economies advance, puts immense strain on all infrastructures. The engine for this tremendous economic expansion has been the global integration of societies. At the same time, the growth of global networks has made infrastructure efficiency and effectiveness critical to commercial and national competitiveness. How successfully enterprises and communities can benefit from globalization, particularly in terms of global trade, is heavily dependent on the quality of their infrastructure.

Risks to business

Demand pressures

In rapidly developing parts of the world, the supply of critical infrastructure resources is already failing to meet demand or is projected to do so soon. Energy supplies and transport are two networks that are particularly struggling to keep up with population growth, urbanization and growing global trade.

Globalisation has allowed businesses to expand, supplying goods and services on a global scale and benefiting from the ability to outsource key business functions, such as IT customer services, to international locations. However, this global reach makes them more dependent on overseas infrastructure networks and, consequently, more vulnerable to the risks associated with failing infrastructure in both the developed and developing worlds.

Vulnerability of IT infrastructure

The invention of the public internet as a cheap and efficient form of networking revolutionised infrastructure control systems. Prior to its introduction, the majority of critical public works relied on physically and logically separate hardware, operating systems, and software. The internet has allowed businesses to operate across the globe, accessing expanding markets, working out of virtual offices and sending information at the click of a button. As a shared resource, public telecom infrastructure is much cheaper than private lines that are only used by one company.

Cost-cutting has led many public service and private sector infrastructure systems to migrate onto public networks. Globalisation has reduced the variety of infrastructure control systems and increased unified control on a public data network that is open to all and protected by authentication,

encryption, and other virtual security measures. More and more people are worried that criminal and other group is getting ahead of encryption and security, and that this makes it harder to use the internet safely.

~~1.3.4~~4.3.3 Supply Chain Risk

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Over the last 20 years, the acceleration of globalisation has been with significant changes in supply networks. The rapid emergence of new global opportunities for production and sales, reductions in transportation and logistics costs, and new management imperatives arising from quarterly and other reporting requirements have provided a strong impetus to developing supply chains with a broader global reach while also achieving the goals of reducing stocks and tie-up capital. As a result, supply chains have grown in size and complexity.

Risks to business

less control over more complex supply chains in a recent MIT survey of global supply chains, 90% of those surveyed believed that the size and frequency of supply chain shocks were increasing in their company. Globalisation has allowed businesses to expand across many countries and has provided a greater choice of suppliers. However, as supply chains become more complex, additional layers of risk are added. Businesses may not have direct control over every day-to-day operation within every stage of their supply chains.

Vulnerability of just-in-time business models

The risk to complex supply chains is heightened by the small margin of error that businesses build into them. Small changes to delivery schedules can have dramatic knock-on effects on production and sales. The disruption to supplies may arise at the point of production or in transport and delivery. The reasons are extremely wide-ranging and include problems further down the supply chain, such as fires, strikes, energy outages, bankruptcy, accidents, or managerial failures.

Cascade failure

There is strong evidence that as supply chains become more extensive and complex, the risk of a given disruption becoming serious or causing a cascading failure has increased.

A cascading failure is a system-wide shutdown caused by the failure of one or more critical and non-redundant elements. It can be distinguished from routine failure, which is any unplanned disruption that degrades the business model.

Cascading failures, as the name suggests, are a particular threat to lean and long supply chains. Their causes are manifold and include operational and technological risks; social risks; natural hazards; economic variations; and legal and political disruptions. Breaks in supply chains are nothing new, but as these chains get tighter and are connected to more and more global production networks, a small problem in one place can quickly cause a production failure in another.

~~1.3.5~~4.3.4 Food Security

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Globalisation has led to a rapid increase in incomes, which, along with population growth, has fuelled an increase in food demand as well as a transformation in the types of foods in demand, most notably processed foods. Continuing population and consumption growth will mean that the global annual demand for food will increase for at least another 40 years. The global shift towards standardisation is nowhere more stark than in the natural environment and the ecosystems that supply our food. Due to the growth in food demand, our standard practice is to replace natural diversity with artificial monoculture environments that can yield large harvests and herds with minimal labor inputs. Planting monocultures in the fields ensures that the whole regional agricultural support infrastructure, including research, development, suppliers, storage, transport and markets, is also highly specialised and therefore sensitive to fluctuations in crop yields and herd health.

Risks to business
Crop control
The increasing monoculture environments across the globe can be decimated by parasites and pathogens. To counteract that threat, we protect them with pesticides (for crops) and antibiotics (for livestock and herds), which can present a localized risk to populations and businesses.

Food shortages
Poor growing conditions and mass parasitic events—plus the unintended effect of biofuel consumption of maize—aligned to prompt a food crisis in the developing world. Between 2006 and 2008, average world prices for rice rose by 217%, wheat by 136%, corn by 125%, and soybeans by 107%. 98 In response, shortages led to increased hunger and poverty in a number of countries and, in several cases, contributed to outbreaks of violent conflict, mainly in hard-hit parts of Asia and Africa.

~~1.3.6~~4.3.5 Geo-Political Risk

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The definition of geopolitical risk has shifted. Traditional military engagements involving big armies are, in general, unlikely. The shift in power relations at the conclusion of the Cold War from big states to small-

state players represents a fundamental shift in the nature of systemic risk as a result of the recent tidal wave of globalisation. The same infrastructure, networks, technical advancement, and economic investment that have increased the global population can now be used as platforms for coordination and attack by those seeking to overthrow entrenched forces. Systemic vulnerabilities are enticing possibilities for angry non-state actors to unleash catastrophic damage.

Risks to business
Terrorism
The most spectacular evidence of our present geopolitical vulnerability are the New York terrorist attacks of 9/11 in 2001; the March 2004 train bombing in Madrid; and the 7/7 attacks in London. These events demonstrated clearly that a competent, well-financed private organisation—in many of these cases, al Qaeda—can overcome contemporary public security measures in order to prepare, deliver, and detonate effective weapons at strategically and symbolically important locations.

Political instability
As discussed in past units, globalisation facilitated the growth of capital, innovation, and interdependencies, which contributed to the economic crisis. Many governments have had to take drastic action to stabilize their economies. However, this has created emotional and sometimes violent responses amongst national populations.

4.4 Summary

Several developments are undoubtedly slowing, if not reversing, the rapid rate of globalization. As a result of the recent economic crisis, there is evidence of protectionism, nationalist attitudes, and tightened economic laws, as well as other hazards associated with functioning in a globalised environment. Most businesses now operate on a worldwide scale, and most people benefit from the success that globalization may offer.
In many ways, globalisation has built deep and integrated connections between societies and economies that will not be broken easily. In many ways, globalisation has become a defining and permanent feature of the global system.

The topics covered in this unit include the following:

Economic and financial risk,
Global pandemic threat,
Infrastructure risk,

Supply chain uncertainty,
Food security,
Geo-political risk.
We shall proceed to consider various business and government policies in the next unit.

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UNIT 5: BUSINESS POLICY - DEFINITION AND DISCUSSION OF CONCEPT

~~CONTENTS~~ Unit Structure

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5~~1~~.2 Intended ~~learnig~~Learning ~~outcomess~~Outcomes
~~1.3 Main Content~~
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~~1.3.2~~5.3.1 Definition of Business
~~1.3.3~~5.3.2 Nature of Policy
5~~1~~.4 Objectives of Business Policy
5~~1~~.5 Summary
5~~1~~.6 References/Further Readings
5~~1~~.7 Possible Answers to Self-Assessment Exercise(s) ~~within the content~~

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1.1 Introduction

Every organisation has a purpose for which it was established—either for profit-making or non-profit-making—and closely allied to the purpose of an organisation are the principles on which it is to be conducted. These principles, in business parlance, are commonly called policies. According to Kalejaye (1998), a future course of action of intent towards the activities of an organisation. He opined that there is more to the meaning of policy than an expression of intent. To him, there is usually the connotation that policies should express the beliefs of the organisation, the things that are right to do and the courses of action that it ought to take. This explains why policies on the same subject can be so different from one organisation every business requires guidelines which are to be embedded in policy. A policy is a decision rule, not a decision (Ackoff 1993). Principles in business parlance are commonly known as policies.
A policy denotes a future course of action with intent towards the activities of an organisation. In this unit, you will be introduced to the meaning of business policy in order to prepare you for all the associated ideas about the concept in business management. We shall also highlight the reasons why business policy is necessary. Finally, we shall explain business policy implementation in an organisation.

I believe you have read the course guide and have a general understanding of this unit and how it fits into the course as a whole. You will see from the objectives below what you are expected to learn after reading this unit.

5~~1~~.2 Intended ~~learnig~~Learning ~~outcomess~~Outcomes

~~At~~ By the end of this unit, you ~~should~~ will be able to:

- define business policy
- state the need for business policy
- explain business policy implementation in organisation.

5~~1~~.3 Main Content

The introductory unit is intended to familiarize you with business policy. It starts with a description of business policy. It starts with a description of the development process that evolved before learners like you got the opportunity to study this course. Next, we shall introduce you to the nature of business policy and its definition. You should be convinced of the importance of the business policy course to be motivated to learn it better. Hence, we have to be clear about the purpose and objectives of the course that we are learning. The objectives of the course have been described in terms of knowledge, skills, and attitudes. It is essential to know what to expect from this course and which direction the learning objectives are likely to take the students.

5~~1~~.3.1 Definition of Policy

What comes to your mind when the word policy is mentioned? As stated in the introduction earlier, policy is defined as a decision rule, not a decision. For example, accounting policy: hire only professionally qualified accountants for senior accounting positions.

When such a person is hired, it is a decision. A policy is considered the general guideline for decision-making. Kalejaye (1998) defined policy as the objectives, the mode of thought, and the body of principles underlying the activities of an organisation.

According to Fagbemi (2006), a policy refers to what an organisation or a person intends to do or does. Business policy, therefore, is what a

business organisation intends to do. It aims to assist the organisation to deliver services to meet the needs and expectations of its goals of the organisation. Policies are plans in that they are general statements or understandings that guide channel thinking in decision making. In actual business situations, not all policies are (organisation) strictly follow (perhaps for convenience rather than as policy) the practice of promoting from within; the practice may be interpreted as policy and carefully followed by subordinates.

Koontz and Weighrich (2005) to be candid, it is incumbent upon the managers to ensure that subordinates do not interpret as minor managerial decisions that are not intended to serve as patterns.

Business policy is a guide and roadmap to create awareness and direction for the management of any organisation. It publicizes the rights and obligations of different rungs of the ladder, horizontal and vertical, of the different capitals, be it human resource engagement, finance utilization, etc. It ensures that organisations deliver better end products within a framework.

It encourages, promotes, and improves performance attainment in an organisation.

The policy provides the bedrock for the vision and mission statement of the business organisation's corporate objectives and goals. Policy allows the business to be evaluated based on how they carry out their responsibilities and their relationship to the organisation's strategy.

Self-Assessment Exercise 1

What is a business?

5.3.2 Definition of Business

A business (also known as an enterprise or firm) is an organisation engaged in the trade of goods, services, or both to consumers. Businesses are predominant in capitalist economies, where most of them are privately owned and administered to earn a profit to increase the wealth of their owners. Businesses may also be not-for-profit or state-owned. A business owned by multiple individuals may be referred to as a company, although that term also has a more precise meaning.

The term "business" derives from the state of being preoccupied, either as an individual or as a society as a whole, with commercially viable and profitable work. The term "business" has at least three usages depending on the scope: the singular usage to mean a particular organisation; the generalized usage to refer to a particular sector, "the music business" and

compound forms such as agribusiness; and the broadest meaning, which encompasses all activity by the community of suppliers of goods and services. However, the exact definition of business, like much else in the philosophy of business, is a matter of debate and complexity of meanings. Although forms of business ownership vary by jurisdiction, there are several common forms:

Sole proprietorship: A sole proprietorship is a for-profit business owned by one person.

The owner may operate the business alone or may employ others. The owner of the business has unlimited liability for the debts incurred by the business.

A Partnership: A partnership is a business owned by two or more people. In most forms of partnerships, each partner has unlimited liability for the debts incurred by the business.

The three typical classifications of for-profit partnerships are general partnerships, limited partnerships, and limited liability partnerships.

Corporation: A corporation is a limited-liability business that has a separate legal personality from its members. Corporations can be either government-owned or privately-owned, and corporations can be organized either for-profit or not-for-profit. A privately-owned, for-profit corporation is owned by shareholders who elect a board of directors to direct the corporation and hire its managerial staff. A privately-owned, for-profit corporation can be either privately held or publicly held.

Cooperative: Often referred to as a "co-op", a cooperative is a limited liability business that can be organized for-profit or not-for-profit. A cooperative differs from a for-profit corporation in that it has members, as opposed to shareholders, who share decision-making authority. Consumer cooperatives are typically classified as either consumer cooperatives or worker cooperatives. Cooperatives are fundamental to the ideology of economic democracy.

5~~1~~.3.3~~2~~ Definition of Business Policy

Business policy defines the scope or spheres within which decisions can be taken by subordinates in an organisation (Wikipedia, 2012). It permits the lower level management to deal with the problems and issues without consulting top level management every time a decision is made.

Business policies are the guidelines developed by an organisation to govern its actions. They define the limits within which decisions must be

made. Business policy also deals with the acquisition of resources with which organisational goals can be achieved.

Business policy is the study of the roles and responsibilities of top-level management, the significant issues affecting organisational success and the decisions affecting organisations in the long run.

1. Specific policies should be specific and definite. If it is uncertain, then the implementation will become difficult.
2. Clear-policy must be unambiguous. It should avoid the use of jargon and connotations.

There should be no misunderstandings in following the policy.

3. Reliable/Uniform-Policy must be uniform enough so that it can be efficiently followed by the subordinates.
4. Appropriate: Policy should be appropriate to the present organisational goal.
5. Simple: A policy should be simple and easily understood by all in the organisation.
6. Inclusive and comprehensive-In order to have a wide scope, a policy must be
7. Flexible-Policy should be flexible in operation or application. This does not imply that policies should be altered always, but they should be broad in scope so as to ensure that the line managers use them in repetitive/routine scenarios.
8. Stable: Policy should be stable or else it will lead to indecisiveness and uncertainty in the minds of those who look into it for guidance.

Rama Rao (2010) gave some useful definitions of business policy as follows:

1. A business policy is an implied overall guide setting up boundaries that provide a general limit and direction in which managerial action will take place.
2. A business policy is one that focuses attention on the strategic allocation of sca. Conceptually speaking, strategy is the direction of such resource allocation while planning is the limit of allocation.
3. A business policy represents the best thinking of the company's management as to how objectives may be achieved in the prevailing economic and social conditions.
4. A business policy is the study of the nature and process of choice about the future of independent enterprises by those responsible for decisions and their implementation.
5. The purpose of a business policy is to enable the management to relate to propto-thinking.

Difference between Policy and Strategy can be summarised as follows:

1. A policy is a blueprint of the organisational activities that are repetitive/routine in nature. While strategy is concerned with organisational decisions that have not previously been confronted in the same form.
2. Policy formulation is the responsibility of top-level management. While strategy formulation is basically done by middle level management,
3. Policy deals with routine/daily activities essential for the effective and efficient running of an organisation. While strategy deals with strategic decisions
4. Policy is concerned with both thought and actions. While strategy is concerned mostly with action,

A policy is what is, or what is not done. A strategy is the methodology used to achieve a target as prescribed by a policy.

Self-Assessment Exercise 2

State the major differences between a policy and a strategy.

5.4 Objectives of Business Policy

The main objective of business policy is performance-driven, which ensures delivery of service or product depending on the purpose for which the business was set up.

Specific objectives of business policies ensure:

1. Efficiency and effectiveness in the performance of duties
2. Equal provision of services and treatment of customers
3. Better management and the provision of better quality services
4. The utilization and application of resources
5. The formulation of a mission statement
6. The establishment of the vision of the organisation

Policies must always be aligned with the objectives of the enterprise if it is to be effective. All policies follow parallel courses and are directly related to objectives. If they cross or oppose objectives, the collective effect is lost and disorder would prevail. Misunderstanding and confusion are often the causes of problems and poor results rather than faults in the stated policy (Kalejaye, 1998).

The major reasons for having policies are as follows:

Why Create Business Policies?

No matter what the size of the business, business policies can be simple to implement, while adding structure to the great things you are already doing. Specifically, business policies:
Drive strategic planning, and help set expectations and performance objectives.

Lead to more efficient internal operations.

Engage and align the values of stakeholders and build mutual understanding of expectations and challenges. Ensure accountability and transparency. To promote ethical and responsible decision-making. Assess and mitigate risk. Streamline new staff orientation; having established written policies that staff can refer to creates consistency, clarity, and an understanding of the goals and culture of the company. Saving time by thinking ahead of time about how specific situations and issues will be handled eliminates the need to discuss and debate how to handle issues every time they arise.

Meet legal requirements. Some laws say that employers have to make certain rules for their staff and management to follow. Example: Discrimination/Harassment Policy.

5~~1~~.5 Summary

In conclusion, it is deduced that every organisation, including businesses, requires a policy as a decision rule to guide the activities and performance of the business to eventually achieve the goals and objectives of the organisation.

In this unit, we have made an overview of policy. Business and business policy have also been defined. We have also identified the reasons for business policy. Finally, we listed and briefly explained the objectives of a business policy. In the next unit, we will trace the evolution of business policy as a discipline.

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5~~1~~.7 Possible Answers to Self-Assessment Exercise(s) ~~within the content~~

SAE 1

Business policy is a guide and roadmap to create awareness and direction for the management of any organisation. It publicizes the rights and obligations of different rungs of the ladder, horizontal and vertical, of the different capitals, be it human resource engagement, finance utilization, etc. It ensures that organisations deliver better end products within a framework.

SAE 2

1. A policy is a blueprint of the organisational activities that are repetitive/routine in nature. While strategy is concerned with organisational decisions that have not previously been confronted in the same form.
2. Policy formulation is the responsibility of top-level management. While strategy formulation is basically done by middle level management,
3. Policy deals with routine/daily activities essential for the effective and efficient running of an organisation. While strategy deals with strategic decisions

4. Policy is concerned with both thought and actions. While strategy is concerned mostly with action,

MODULE 3

UNIT 1: EVOLUTION OF BUSINESS POLICY AS A DISCIPLINE

Unit Structure

1.1 Introduction
1.2 Learning Outcome
1.3 Evolution of Business Policy as a Discipline
  1.3.1 The Genesis of Business Policy
  1.3.2 Evolution based on Managerial Practices
1.4 Historical Perspectives of the Evolution of Business Policy
1.5 Pointers to the Future
1.6 Summary
1.7 References/Further Readings
1.8 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

Concepts of policy, business and business policy, we also identified the reasons for business policy. Finally, we listed and briefly explained. In this unit, we shall trace the evolution of business policy as a discipline.

1.2 Learning Outcome

By the end of this unit, you should be able to:

- trace the evolution of business policy as a discipline
- discuss the genesis of business policy; trace the evolution of business policy based on managerial practices
- discuss the historical perspective of the evolution of business policy predict the future business policy with regard to managerial practices.

1.3 Evolution of Business Policy as a Discipline

Kazmi (2006) states that business policy is a mandatory course which is usually included in a typical management study curriculum. According to him, almost all management education programs offered by Nigerian universities and management institutes include business policy courses

(by whatever nomenclature they are referred to) in the latter part of a degree or diploma programme.

1.3.1 The Genesis of Business Policy

Tracing the history of business policy, Kazmi (2006) stated that it can be traced back to 1911, when the Harvard Business School introduced an integrative course in management aimed at providing general management capability. This course was based on case studies that had been in use at the school for instructional purposes since 1908 (Christensen, et al., 1982, cited in Kazmi, 2006). However, the real impetus for introducing business policies into the curriculum of business schools (as management institutes or departments are known in the United States) came with the publication of two reports in 1959. The Gord Howell report, which was paid for by the Ford Foundation and came out at the same time, had suggested a capstone course in business policy that would bring together what students had learned in their different business fields.

The American Assembly of Collegiate Schools of Business (the American Assembly of Collegiate Schools of Business is a regulatory body for business schools) made business policy a mandatory requirement for recognition in 1969. In the last two decades, business policy has become an integral part of the management education curriculum. The practice of including business policy in the management curriculum has spread from the United States to other parts of the world. The content of the course, teaching methodology, and so on vary from institution to institution.

But basically, business policy is considered a capstone integrative course offered to students who have already been through a set of core functional area courses. Traditionally, though, new titles such as strategic management, corporate strategy and policy, and so on are now extensively used for the course. The discussion has so far been related to the academic status of the business policy course. In practice, however, the development has been along different lines.

1.3.2 Evolution based on Managerial Practices

Kazmi (2006) viewed the development in business policy as arising from the use of planning techniques by managers. Starting from day-to-day planning in earlier times, managers, till recently, tried to anticipate the future through the preparation of budgets by using control systems like capital budgeting and management by objectives.

However, as these techniques were unable to emphasise the role of the future adequately, long-range planning came into use. However, long-

term planning was quickly replaced by strategic planning and then by strategic planning of strategy. Strategic management forms the theoretical framework for business policy courses today.

1.4 Historical Perspective of the Evolution of Business Policy

Hofer et al. (1984) have viewed the evolution of business policy in terms of four paradigm shifts. For simplicity's sake, these changes can be thought of as four phases that overlap in the development of the subject, business policy. It is interesting to note that the development of business policy as a field of study has closely followed the demands of real-life business. He further argues that the first phase, which can be traced to the mid-1930s, rested on the paradigm of ad-hoc policy-making. The need for policy-making arose due to the nature of American business firms of that period. The first business grew in one or more of these three ways. It had started out with a single product line that was sold to a specific group of customers in a small area.

Informal control and coordination became partially irrelevant as expansion took place and the need to integrate functional areas arose. This integration was brought about by framing policies to guide managerial action. Policy-making became the prime responsibility of erstwhile entrepreneurs who later assumed the role of senior management. Due to the increasing environmental changes in the 1930s and 40s in the United States, planned policy formulation replaced ad-hoc policy-making. Based on this second paradigm, the focus shifted to integrating functional areas in an environment that was changing quickly.

Increasing complexity and accelerating changes in the environment made the planned policy paradigm irrelevant since the needs of a business could no longer be served by policy-making and functional area integration alone. By the 1960s, there was a demand for a critical look at the basic concept of business and its relationship to the environment. This need was met by the idea of strategy, and the early 1960s saw the start of the third phase, which was based on a strategy paradigm.

The current thinking, which emerged in the eighties, is based on the fourth paradigm of strategic management. The initial focus of strategic management was on the intersection of two broad fields of inquiry: the strategic process of business firms and the responsibilities of general management.

The story is far from over. As Thompson and Strickland (1984) say, the approach to managing an enterprise.

1.5 Pointers to the Future

The resolution of strategic issues that affect the future of a business firm has been a continuous endeavour in the subject of business policy. The endeavour is based on the fact that they apply obvious ways of thinking to the focus of the efforts of researchers and academicians in the field of business policy.

What, then, are these general principles? As a first step, the model of strategic management that has developed so far and is under constant review incorporates these general principles.

The direction in which strategic management is moving can be anticipated from how discontinuous change, which takes account of psychological, sociological, political, and organizational changes, and which, in the words of Toffler, are no longer responsible simply for making a profit or producing goods but for simultaneously contributing to the solution of extremely complex ecological and moral policies, is expected to rise tremendously. The general managers of tomorrow may be called upon to shoulder a set of entirely new responsibilities, necessitating a drastic review of the emerging concepts and techniques in business policy. Responding to the need for evolving new approaches to the teaching of business policy, the AACSB no longer insists on the provision of just one course in this area. Now there is an emerging trend to have several courses, such as the theory of strategic competitive strategy, industry dynamics, hyper-competition, and global strategy, in the curriculum (Kazmi, 2006).

While reviewing the development of strategy and theory, Rumelt, Schendel, and Teece (1994) posed four fundamental questions which, in their view, characterize the major concerns of strategic management. These four fundamental questions are:

1. How do firms behave? Or, do firms really behave like rational actors, and, if not, which models of their behavior should be used by researchers and policy-makers?
2. Why are firms different? Or, what keeps close competitors from having the same resources and performance, even though they compete and try to copy each other?
3. What is the function of or the value added by the headquarters unit in a diversified firm? Or, what limits the scope of a firm?
4. What determines success or failure in international competition? Or, what are the origins of success and what are its particular manifestations in international settings or global competition? In dealing with most of the issues raised by these fundamental

questions, we would need to look at what has been happening in the Nigerian business scene.

Self-Assessment Exercise

1. Business policy is a capstone, integrative course. Explain.
2. In what direction is strategic management likely to move in the future?

1.6 Summary

In this unit, we have traced the evolution of business policy as a discipline; discussed the genesis of business policy; traced the evolution of business policy based on managerial practices; discussed the historical perspective of the evolution of business policy; and predicted the future of business policy with regard to managerial practices. In the next unit, we will examine the nature, objective, and purpose of business policy.

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1.8 Possible Answers to Self-Assessment Exercise(s)

SAEs 1

Tracing the history of business policy, Kazmi (2006) stated that it can be traced back to 1911, when the Harvard Business School introduced an integrative course in management aimed at providing general management capability. This course was based on case studies that had been in use at the school for instructional purposes since 1908 (Christensen, et al., 1982, cited in Kazmi, 2006). However, the real impetus for introducing business policies into the curriculum of business schools (as management institutes or departments are known in the United States) came with the publication of two reports in 1959. The GordHowell report, which was paid for by the Ford Foundation and came out at the same time, had suggested a capstone course in business policy that would bring together what students had learned in their different business fields.

SAEs 2

The direction in which strategic management is moving can be anticipated from how discontinuous change, which takes account of psychological, sociological, political, and organizational changes, and which, in the words of Toffler, are no longer responsible simply for making a profit or producing goods but for simultaneously contributing to the solution of extremely complex ecological and moral policies, is expected to rise tremendously. The general managers of tomorrow may be called upon to shoulder a set of entirely new responsibilities, necessitating a drastic review of the emerging concepts and techniques in business policy.

UNIT 2: NATURE, OBJECTIVE AND PURPOSE OF BUSINESS POLICY

Unit structure

2.1 Introduction
2.2 Learning Outcome
2.3 Nature of Business Policy
 2.3.1 Importance of Business Policy
 2.3.2 Purposes of Business Policy
2.4 Objectives of Business Policy
2.5 An Alternative Viewpoint on the Objectives of Business Policy Course
2.6 Summary
2.7 References/Further Readings
2.8 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

Concepts of policy, business and business policy, we also identified the reasons for business policy. Finally, we listed and briefly explained. In this unit, we shall trace the evolution of business policy as a discipline.

2.2 Learning Outcome

At the end of this unit, you should be able to: state the nature of business policy; highlight the importance of business policy; and enumerate the purposes of business policy. List the objectives of business policy.

2.3 Nature, Objective and Purpose of Business Policy

2.3.1 Nature of Business Policy

Before we proceed to understand the nature of business policy, let us witness these situations, as reported in an issue of a reputed business magazine in India: (Karmi, 2006). Exide reaps the benefits of its strategies, which include modernization, expansion, and acquisitions, to become the integrated leader in the battery sector. Costly expansion and poor demand have forced JKCorp to rework its strategies. It is now banking its future on its core paper business. This will come through the divestment of its cement division, Laxmi Cements, and the acquisition of the Central Pulp Mills. Tisco is using divestments and mergers to restructure its core businesses of steel, allied industries, refractory, and engineering. The Exim Bank (the Export and Import Bank of India), established in the early eighties with the objective of extending support to

Indian exporters and importers, still remains small, given the Indian banks. It needs a strategic vision to cope with the increasing competition in the new millennium. From the above reports, we can see that when companies either promotes a joint venture, divests a part of its business, embarks upon an expansion programme, undertakes mergers and acquisitions or takes other similar actions that have a long-term impact on its future operations and status, those are a result of senior management decision-making. Senior management in any organization is primarily responsible for guiding the future course of action and providing a sense of direction. To these ends, business policy attempts to instill in one the capability for senior management. The problems of policy in business, like those of policy in public affairs, have to do with the choice of purposes, the molding of organizational identity and character, the continuous definition of what needs to be done, and the mobilization of resources to achieve goals in the face of challenges. This comprehensive definition covers many aspects of business policy. Firstly, it is considered as the study of the functions and responsibilities of the senior management related to those organizational problems which affect the success of the total enterprise.

Secondly, it deals with the determination of the future course of action that an organization has to adopt. Thirdly, it involves choosing the purpose and defining what needs to be done in order to mould the character and identity of an organization. Lastly, it is also concerned with the mobilisation of resources, which will help the organization to achieve its goals.

Senior management is made up of managers with titles like Chief Executive Officer, President, General Manager, or Executive Director, who are mostly in charge of making long-term decisions. These are people who are not concerned with day-to-day problems but are expected to devote their time and energy to thinking and deciding about the future course of action. With its concern for the determination of the future course of action, business policy lays down a long-term plan, which the organization then follows. While deciding about a future course of action, the senior management is confronted with a wide array of decisions and actions that could possibly be taken. The senior management exercises a choice, on the basis of given circumstances, which, in their opinion, would lead the organization in a specific direction. By moving in a predetermined direction, an organization can attain its identity and character.

2.3.1 Importance of Business Policy

Kazmi (2006) opined that business policy is important as a course in the management curriculum and as a component of executive development

programs for middle-level managers who are preparing to move up to the senior management level. A study of business policy fulfills the needs of management students as well as those of middle-level managers. To show how important business policy is, we will look at four ways that this course is helpful.

2.3.2 Purposes of Business Policy

The management course, which is generally studied in the latter part of the degree or diploma, is preceded by the study of functional area courses in finance, marketing, operations, and personnel (Kazmi, 2006). The business policy course seeks to integrate the knowledge gained in various functional areas so as to develop a generalist approach in management students. Such an approach is helpful in viewing organizational problems in their totality. It can also create awareness of the repercussions that an action taken in one area of management can have on other areas, both individually and as a whole. The viewpoint adopted in business policy is different from that adopted in the functional area courses. For instance, a marketing problem is not viewed purely as a problem of understanding a business as a system consisting of a number of sub-systems. Any action taken in one sub-system has an impact on other sub-systems and on the system as a whole.

It is of vital importance for the top management in any organization to adopt such a systems approach to decision-making. Business policy helps a manager to become a generalist by avoiding the narrow perspective generally adopted by specialists and dealing with business problems from the viewpoint of senior management.

The problem of declining sales volume is apparently a marketing problem. However, an analysis of the problem will show that its roots may lie anywhere in the organization. Declining sales volume may be due to a rising level of competition, inefficient distribution, faulty sales promotion, inappropriate recruitment policies, misdirected training, inadequate sales promotion, limited commission to sales personnel, falling quality standards, a decrease in the variety of products offered, outdated design, underutilization of capacity, demotivating credit policies, and so on. A problem, which apparently seems to be a marketing problem, may be due to factors not necessarily within the control of the marketing department. A solution to the problem would necessitate transgressing the artificial boundaries between the functional areas, each of which is looked after by a team of specialists. Because of their background, training, and maybe even loyalty to their fields, these specialists don't know how to solve all the problems as a whole and aren't equipped to do so.

They may come up with short-term solutions, but these are only like first-aid when a thorough diagnosis and treatment are required to mitigate the misery. A generalist, on the other hand, is better qualified to deal with organizational problems and can come up with solutions that will have a lasting effect. On the basis of the above discussion, we can say that the purpose of business policy is three-fold:

1. To integrate management knowledge gained across multiple functional areas;
2. I adopt a generalist approach to problem-solving and
3. It is to understand the complex interlinkages operating within an organization through the use of a systems approach to decision-making and relate these to the changes taking place in the external environment.

In order to make the study of business policy purposeful, specific objectives need to be defined, which we shall do in the next section.

2.4 Objectives of Business Policy

It is essential that we first state the objectives of business policy and only then proceed. The objectives of business policy have been stated in terms of knowledge, skills, and attitudes that could be derived from the purpose of business policy.

Knowledge

i. The learners of business policies have to understand the various concepts involved. Many of these concepts, like strategy, policies, plans, and programs, are encountered in functional area courses too. It is imperative to understand these concepts, specifically in the context of business policy.
ii. Knowledge of the external and internal environment and how it affects the functioning of an organization is vital to an understanding of business policy. Through the tools of analysis and diagnosis, a learner can understand the environment in which a firm operates.
iii. Information about the environment helps in the determination of the mission, objectives, and strategies of a firm. The learner appreciates the manner in which strategy is formulated.
iv. The implementation of a strategy is a complex issue and is invariably the most difficult part of strategic management. Through the knowledge gained from business policy, the learner will be able to visualize how the implementation of strategic management can take place.

v. Learning that the problems in real-life business are unique and so are the solutions is an enlightening experience for the learners. The knowledge component of such an experience stresses the general approach to be adopted in problem-solving and decision-making. With a generalized approach, it is possible to deal with a wide variety of situations. The development of this approach is an important objective to be achieved in terms of knowledge.
vi. Surveying the literature and learning about the research taking place in the field of business policy is also an important knowledge objective.

Skills

1. The attainment of knowledge should lead to the development of skills so as to be able to apply that which has been learnt. Such an application can take place through an analysis of case studies and their interpretation, as well as through an analysis of the business events taking place around us.
2. The study of business policy should enable a student to develop analytical ability and use it to understand the situation in a given case or incident.
3. Further, the study of business policy should lead to the skill of identifying the relevant factors in decision-making. The core content of general management decision-making is an analysis of an organization's strengths and weaknesses, threats and opportunities in the environment, and the recommendation of appropriate strategies and policies.
4. The above objectives, in terms of skills, increase the mental ability of the learners, enabling them to link theory with practice. Such ability is important in managerial decision making where a large number of factors have to be considered at once to suggest appropriate action.
5. As a part of business policy study, case analysis leads to the development of oral as well as written communication skills.

Attitude

1. The attainment of the knowledge and skill objectives should lead to the inculcation of an appropriate attitude among the learners. The most important attitude developed throughout this course is that of a generalist. The generalist attitude enables the learners to approach and assess a situation from all possible angles.
2. By acting in a comprehensive manner, a generalist is able to function under conditions of partial ignorance by using his or her judgment and intuition. Typically, case studies provide only a glimpse of the overall situation, and a case analyst frequently faces

the frustrating situation of working with less than the required information. Experience has shown that managers, especially in the area of long-range planning, have to work with incomplete information. A specialist would tend to postpone or avoid a decision under such conditions, but a generalist would go ahead with whatever information was available. In this way, he or she acts more like a practitioner than a perfectionist.

3. For a general manager, information and suggestions are important to possess a liberal attitude and be receptive to new ideas. Dogmatism with regard to techniques should be replaced with a practical approach to decision-making for problem-solving. In this way, the general manager can act like a professional manager. Problematic situation. Developing a creative and innovative attitude is the hallmark of a general manager who refuses to be bound by precedents and stereotyped decisions.

2.5 An Alternative Viewpoint on the Objectives of Business Policy Course

Anisya S. Thomas of Florida International University says that the main goals of the capstone business policy course have stayed mostly the same for a long time.

There is broad agreement among textbook writers and instructors that these objectives encompass content as well as process dimensions; that is, they deal with the core concepts and theories and also seek to teach an analytical process that incorporates multiple perspectives.

More specifically, these objectives are as below:

1. integration of functionally specific knowledge. Business policy acts as an integrative, capstone course, demonstrating the interdependence between separate functional areas, such as marketing, finance, and so on.
2. Understanding by managing the interdependence among the functional areas is a critical objective of business policy. A general management perspective aids in exposing the student to the tradeoffs involved in achieving superior performance by balancing the internal competencies with the external requirements.
3. Working as part of, managing, and leading a team. Working with and managing a diverse and flexible team is a critical priority for corporate recruiters. (Interestingly, a similar view is expressed on the basis of surveys conducted by the Indian business magazines too.) Business policy tries to build up teamwork spirit by illustrating the finer aspects of group dynamics and by bringing together students from different specialization areas.

4. Enhancement of comprehension and communication skills. Business policy lays great emphasis on allowing students to be active participants in the learning process. In contrast to the functional courses, there is a stress on using methodologies, such as case discussions, oral and written presentations, and reports.
5. Ability to assess the applicability and relevance of strategic management research (theory to practice). Theoretical advances in the field of business policy are taking place rapidly. It is necessary for the students to evaluate the relative merit and applicability of theoretical advances to deal with the rapid environmental and strategic changes that characterize the business arena. So it is imperative that students not just learn, but also learn how to learn (Kazmi, 2006).

Having looked at the alternative view of the objectives of the business policy course, you will be in a position to gain further insight into the issue. The objective business policy in terms of knowledge, skills, and attitude could be further extended to the areas of behavior and performance. After having attained knowledge of the objectives in the classroom, or in an executive development program, the learner is expected to exhibit appropriate behavior and good performance on the job. The structure of business policy is built through the accumulation of experience as one moves up the managerial ladder. The richness and variety of experience gained as one moves up the managerial ladder in business offers opportunities for testing, validating, and replicating the mental images and models learnt in the business policy course.
Such an approach imparts an added impetus to the development of general management capability, which is the sine qua non for a manager who wishes to succeed in his or her job and make a meaningful contribution to the organization he or she works for.

Self-Assessment Exercise

1. What are the different aspects of the nature of business policy? Discuss each one of them with the help of suitable examples. 2. What are the objectives set for a business policy course in terms of knowledge, skills and attitudes?

2.6 Summary

In this unit, we have stated the nature of business policy; highlighted the importance of business policy; enumerated the purposes of business policy; and listed the objectives of business policy. In the next unit, we will examine the characteristics of business policy.

2.7 References/Further Readings

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2.8 Possible Answers to Self-Assessment Exercise(s) within the content

SAE 1

Exide reaps the benefits of its strategies, which include modernization, expansion, and acquisitions, to become the integrated leader in the battery sector. Costly expansion and poor demand have forced JK Corp to rework its strategies. It is now banking its future on its core paper business. This will come through the divestment of its cement division, Laxmi Cements, and the acquisition of the Central Pulp Mills. Tisco is using divestments and mergers to restructure its core businesses of steel, allied industries, refractory, and engineering. The Exim Bank (the Export and Import Bank of India), established in the early eighties with the objective of extending support to Indian exporters and importers, still remains small, given the Indian banks. It needs a strategic vision to cope with the increasing competition in the new millennium. From the above reports, we can see that when companies either promotes a joint venture, divests a part of its business, embarks upon an expansion programme, undertakes mergers and acquisitions or takes other similar actions that have a long-term impact on its future operations and status, those are a result of senior management decision-making. Senior management in any organization is primarily responsible for guiding the future course of action and providing a sense of direction. To these ends, business policy attempts to instill in one the capability for senior management. The problems of policy in business, like those of policy in public affairs, have to do with the choice of purposes, the molding of organizational identity and character, the continuous definition of what needs to be done, and the mobilization of resources to achieve goals in the face of challenges.

UNIT 3: CHARACTERISTIC OF BUSINESS POLICY

Unit Structure

3.1 Introduction
3.2 Learning Outcome
3.3 Characteristics of Policy
3.3.1 Sources of Policy
3.4 what makes a Good Policy
3.5 Summary
3.6 References/Further Readings
3.7 Possible Answers to Self-Assessment Exercise(s)

3.1 Introduction

We shall continue with the discussion on an overview of business policy in this unit. This discussion will centre on the nature and characteristics of policy, reasons for formulating policies, and formulation of policies. The policy thrust of an organization solely depends on the type of business offered—whether it is for production or services; the intensity of needs of operation; and the quality of human resources to be employed. It provides guidance to achieve the objectives and goals of organizations.

3.2 Intended Learning Outcomes

By the end of this unit, you should be able to:

- explain the characteristics of policy
- discuss the sources of a new policy; State the features that make a good policy.

3.3 Characteristic of Business Policy

Most organisations produce statements and explanations of what they are trying to achieve in particular areas. Policies are divided into and stated in terms of procedures, which are a series of related steps or tasks expressed in a chronological order, and rules, which are a prescribed course of action that explicitly state what is to be done under a given set of circumstances. Many organizations provide parameters within which decisions must be made. Some of these will be written by specialists in different operational areas, like employment matters, which may focus on hiring and firing; sales and marketing departments may provide guidelines on pricing and credit facilities; purchasing department policies

may prohibit gifts from suppliers. Some policies focus on materials and stock, others on capital and equipment. Some describe objectives and others mean

In general, policies may be classified in relation to personnel, capital, objectives, means and specific organizational areas. This is an arbitrary but convenient way to classify policies. It should be noted that these categories are not mutually exclusive but frequently overlap.

3.3.1 Characteristics of Policy

Sound policies usually contain a combination of the following characteristics:

i. Destiny
ii. Top Management Approval and Commitment
iii. Intellectual Contribution
iv. Acceptability
v. Communicated to Staff
vi. Genuine Intention and Application
vii. Balanced Interpretation
viii. Alignment with Objective

Destiny: A common characteristic of policy is that it denotes future action and intent. It usually describes a goal or destiny that is waiting to be achieved. In addition, it implies people in the organization.
The manner in which a policy is expressed and the detailed procedures which stem from it all point in the same direction and do not allow individual actions to follow a different direction. If the actual procedures and wording do not imply belief in a course of action, then it is probably a wrongly formulated policy.

Top Management Approval and Commitment In practice, it may be the job of lower-level managers in an organization to make policy contributions and recommendations, but a policy's defining characteristic is that it is approved and supported by top management.
This may be the Board of Directors and Managing Director, or the responsibility may be delegated to a top executive committee. Directors and top managers are primarily responsible for policy making and setting long-term objectives. Once the series of policies are approved at the top, there is every possibility that all segments of the organization will move in the same direction toward the set objectives.

Intellectual Input: Policy requires a high level of intellectual and intelligent input because policies are concerned about the future activities deemed to be just and right for the organization. Policies must be able to withstand pressures, opposition, and challenges from all parts of the

organization and its environment, which may see and treat the policies differently.

A policy may be less effective and may even fail to provide the framework for long-term decision making if it lacks a high level of thorough analysis and deep thought during information gathering.
Most of the time, policymakers have thought about all aspects of a policy. This makes the policy consistent and long-lasting, which makes it hard to change it often. Constant changes in the course of action and direction of an organization will surely bring about confusion, resentment, and even a general derailing of all things that sound policies are trying to achieve. For practical purposes, almost all policies are long-term in nature, although for practical purposes; long-term policies are sub-divided into short-term.

It is important to note that there may be times when they need to be tweaked or changed. In the end, they are meant to create a continuum that can be used to set daily standards and make decisions.

Acceptability: The degree of acceptance of organization policy by everyone is marked by the persistence and understanding of employees who want to know why the policy is made or changed. Genuine reasons must be forthcoming, and management needs to provide supervisors with sufficient information to satisfy queries regarding a policy. There is a danger in withholding information, which often leads to gossip and speculation in an organization, as this can be disorganizing, cause increased friction between management and employees, upset and strain relationships through general suspicion and mistrust**.**

Communicated to staff: As soon as policies are formulated and ratified, they should be communicated to members of the organization. Everybody must be aware of the mission and objectives of the organization; hence, there should be no exception in communicating policies to the members of the organization. Appropriate channels must be used in channeling policies throughout the organisation, so that nobody is left out. This, of course, will cement relationships in the organization and motivate the staff to reach higher heights.

Intent and Use: It's not unusual for management to announce a policy for prestige reasons, like publicity, but then not follow through on it**.** Some managers use policies in wrong and bad ways, hiding behind one excuse or another when they don't follow a certain course of action. These policies are rarely put in writing, and when they are, they are usually wrongly worded in such vague ways that they will be distorted to fit in with any genuine course of action down the line. These kinds of policies

should be avoided. Every management policy should be taken as seriously as it should be and applied in the way it was meant to be used.

While correctly interpreting policies, managers do rigidly conform to principles and procedures without due regard to the human elements of organizational and emerging pressing issues. Inhuman society and an ever changing, complex environment require something more than correctness; all these factors, when weighed carefully, might well provide a more balanced interpretation which would relegate to the background the narrowly correct ones. The real skill of managing and supervising is having a little bit of flexibility to deal with new things and a balanced view of the rules, which can't be blamed on policy abuse.

All policies must take parallel actions that are directly related to the objectives. When they cross or oppose objectives, the collective effect is lost, and disorder reigns. Misunderstanding and confusion are often the causes of problems and poor results rather than faults in the stated policy. These known risks show how important it is to check policies for ambiguity, especially at the lower levels of management, so that people don't get confused.

Self-Assessment Exercise 1

1. What are the characteristics of a policy? List some of them and explain them briefly.

3.3.2 Sources of Policy

Kalejaye (1998) examined the major sources of policies and classified them as originated, appealing, implied, and externally-imposed. These are explained as follows:

i. Originated Source: The most acclaimed source of policies is the one from Top operations. Originated policies flow basically from the objectives of the enterprise, as they are defined by top executive authority. These types of policies may be broad in scope, allowing key subordinates to give them clearer definitions, or they might be promulgated so completely and comprehensively as to leave little room for definition or interpretation.
ii. Appealed Source: In practice, in most cases, policies stem from appeals through the hierarchical level of management authority. If an occasion for decision arises for executives who do not know whether they have sufficient authority or how such matters should be handled, they appeal to their supervisors for the necessary support and action. As appeals are heard and decisions are rendered, a set of rules and procedures emerge. Precedent,

therefore, develops and becomes a guide for future managerial action and serves as a reference point.

iii. Useful policies are developed from the actions that employees see about them and believe to constitute them. Real employees will readily understand what real policy is if they work for a company that operates policies that produce high quality goals. Take labour policy, for instance, though the real policy is implied.

iv. Externally-imposed: to a large extent, policies are externally imposed by such agencies as the government, trade unions, professional associations, and others like trade associations. This might come in the form of direct regulation or one of the many conditions of accepting government aid or contract; it could also be to maintain industrial peace. Besides, local and state governments, professional associations, and social and charitable organizations do influence the policies of organizations.

3.4 What makes a Good Policy?

Wikipedia (2012) states that company policies are most effective as official written documents. While policies often differ in form depending on company size, industry, and length of time in business, policy documents generally contain certain standard components, including: purpose statement, outlining why the organization is issuing the policy and what the desired effect or outcome of the policy is. Specifications, including statements indicating the specific regulations, requirements, and organizational behavior that the policy is creating, Individual policy statements and how policy adherence will be ensured by indicating which parties are responsible for carrying them out.

An Effective Date, which indicates when the policy is considered in force (an executive signature or endorsement can be useful to legitimize the policy). The policy's applicability and scope statement, describing whom the policy affects and what actions are impacted by the policy.
Background, indicating any reasons, history, and intent that led to the creation of the policy, which may be listed as motivating factors. Definitions, providing clear definitions for terms and concepts found in the policy document.

Self-Assessment Exercise

Briefly explain the four major sources of policies that you know of.

3.5 Summary

In this unit, we describe the nature and characteristics of a policy and the sources of policy. We also listed the attributes of a good policy. The third part of the overview on business policy will be discussed in the following unit, which will extensively dwell on the types of policies, uses of policies for management effective integration, and relationship of policies to objectives, reasons for formulating policies, and the role of workers in policy formulation.

3.6 References/Further Readings

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Rama Rao, V. S. (2010). Business Policy. downloaded on November 3, 2010 from
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3.7 Possible Answers to Self-Assessment Exercise(s)

SAEs 1

i. Destiny
ii. Top Management Approval and Commitment
iii. Intellectual Contribution
iv. Acceptability
v. Communicated to Staff
vi. Genuine Intention and Application
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This may be the Board of Directors and Managing Director, or the responsibility may be delegated to a top executive committee. Directors and top managers are primarily responsible for policy making and setting long-term objectives. Once the series of policies are approved at the top, there is every possibility that all segments of the organization will move in the same direction toward the set objectives.

Intellectual Input: Policy requires a high level of intellectual and intelligent input because policies are concerned about the future activities deemed to be just and right for the organization. Policies must be able to withstand pressures, opposition, and challenges from all parts of the organization and its environment, which may see and treat the policies differently.

A policy may be less effective and may even fail to provide the framework for long-term decision making if it lacks a high level of thorough analysis and deep thought during information gathering.
Most of the time, policymakers have thought about all aspects of a policy. This makes the policy consistent and long-lasting, which makes it hard to change it often. Constant changes in the course of action and direction of an organization will surely bring about confusion, resentment, and even a general derailing of all things that sound policies are trying to achieve. For practical purposes, almost all policies are long-term in nature, although for practical purposes; long-term policies are sub-divided into short-term.

It is important to note that there may be times when they need to be tweaked or changed. In the end, they are meant to create a continuum that can be used to set daily standards and make decisions.

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SAEs 2

i. Originated Source: The most acclaimed source of policies is the one from Top operations. Originated policies flow basically from the objectives of the enterprise, as they are defined by top

executive authority. These types of policies may be broad in scope, allowing key subordinates to give them clearer definitions, or they might be promulgated so completely and comprehensively as to leave little room for definition or interpretation.

ii. Appealed Source: In practice, in most cases, policies stem from appeals through the hierarchical level of management authority. If an occasion for decision arises for executives who do not know whether they have sufficient authority or how such matters should be handled, they appeal to their supervisors for the necessary support and action. As appeals are heard and decisions are rendered, a set of rules and procedures emerge. Precedent, therefore, develops and becomes a guide for future managerial action and serves as a reference point.

iii. Useful policies are developed from the actions that employees see about them and believe to constitute them. Real employees will readily understand what real policy is if they work for a company that operates policies that produce high quality goals. Take labour policy, for instance, though the real policy is implied.

iv. Externally-imposed: to a large extent, policies are externally imposed by such agencies as the government, trade unions, professional associations, and others like trade associations. This might come in the form of direct regulation or one of the many conditions of accepting government aid or contract; it could also be to maintain industrial peace. Besides, local and state governments, professional associations, and social and charitable organizations do influence the policies of organizations.

UNIT 4 TYPES/KINDS OF POLICIES

Unit Structure

4.1 Introduction
4.2 Learning Outcome
4.3 Formulation of Policy
  4.3.1 Types of Policy
  4.3.2 Reasons for Formulating Policies
4.4 The Uses of Polices for Management Effectiveness
  4.4.1 Integration and Relationship of Policies to Objectives
  4.4.2 Management Policy Areas
4.5 The Role of Workers in Policy Formulation
4.6 Summary
4.7 References/Further Readings
4.8 Possible Answers to Self-Assessment Exercise(s)

4.1 Introduction

In the last unit, we describe the characteristics of a policy and the sources of a policy. We also listed the attributes of a good policy. In this unit, we will go over the third and final section of the business overview, which will go over the various types of policies, their applications for management effectiveness, the integration and relationship of policies to objectives, the reasons for developing policies, and the role of workers in policy development.

4.2 Intended Learning Outcomes

By the end of this unit, you should be able to:

- describe how policies are formulated
- list the types of policies and enumerate the reasons for formulating policies
- explain the use of policies to improve management effectiveness
- explain how policies are integrated in relation to objectives
- make a list of the management policy areas
- state the role of workers in policy formulation.

4.3 Title of the Main Content

Business policy basically deals with decisions regarding the future of an ongoing enterprise. Such policy decisions are taken at the top level after

carefully evaluating the organization's strengths and weaknesses in terms of product price, quality, leadership position, resources, etc., in relation to its environment. Once established, the policy decisions shape the future of a company, channeling the available resources along desired lines and directing the energy of people working at various levels toward predetermined goals.

In a way, business policy implies the choice of purposes, the shaping of organizational identity and character, the continuous definition of what is to be achieved, and the deployment of resources to achieve corporate goals.

Business policies generally have a long life. They are established after a careful evaluation, and when circumstances change in a major way, the firm is naturally forced to shift gears, rethink, and reorient its policies. The World Oil Crisis of the 1970s compelled many manufacturers all over the world to abandon their previous practices and pursue a policy of producing fuel-efficient vehicles. Therefore, policies should be changed in response to changing environmental and internal system conditions.

4.3.1 Formulation of Policy

The studies or theories in which purposeful organizations formulate policies represent a scholarly pursuit which has been carried on for years by management theorists. Scholars have observed and analysed the decision-making actions of managers of businesses and other organisations as they determined the direction and course of their respective organisations.

One of the most important things an executive does is try to change the way an organization thinks about policy. The more successful an executive is, the more respect he gets from other executives. This, in part, is what contributes to the executive's His thinking is centered on policy issues, and as you will note, all policies are crucial to the survival, health, and success of an enterprise.

Policy decisions rest fundamentally on human judgement and intuition. Some policies evolve informally over a long period of time without conscious or selective formulation.

They have their origin in slowly developing customs, traditions, and attitudes. Others are formulated quickly because the situation requires rapid implementation. Both types can start at the top of an organization and work their way down; they can also start in a specific area and stay there; or they can start at lower levels and spread upward. In general, policies should be formulated by those in an organization who have the

responsibility for accomplishing the particular objectives to which they relate.

Policies from Top to Bottom

Some policies cut across all functional areas of the organization. Many are so interrelated with all areas of operations that their significance can best be understood by the top level management.

Policies that originate from the top arise out of broad, basic needs perceived and defined by the top managers. In large corporations today, for instance, the Chief Accountant is an important contributor to advanced planning and policy formulation. Complex taxes, new accounting procedures, mergers, computerization, insurance, pensions, investment options, appraisal, profit sharing, and depreciation of assets, among many other cost-implication corporate issues, cause the Chief Accountant to become involved in areas that are other than strictly finance.

General policies or corporate policies affecting all areas of operation usually originate from the top management. Descending levels in the organizational structure will be guided by these policies when formulating more limited policies at their own levels.

Policies within Functional Areas of Departments

Those in charge of functional areas and/or departments are generally involved in establishing policies for those areas. Marketing executives formulate marketing policies; purchasing executives formulate purchasing policies; personnel managers formulate personnel policies, etc.

These are operational policies proposed and formulated at functional areas and departmental levels. Managers must be consistent and operate within corporate policy guidelines while formulating policies at these levels. Policies established within functional areas may influence the formulation of policies in other functional areas as well as the strategies developed to pursue those policies.

Policies from Bottom to the Top

There are lots of advantages and wisdom in inviting supervisors and other personnel to participate in developing and implementing policies. Whenever possible, non-management employees should have a voice in policy matters that will directly affect their work.

This gives the managers a chance to hear from the workers' reactions to subject policies and to accommodate them, but also gives the workers the opportunity to gratify their deep needs for recognition and influence on policy making. A worker develops a managerial perspective and a

tendency to consider the enterprise as a whole, thereby contributing to its success.

One important thing to note in the above arrangement is that policies and suggestions, which may originate at or near the bottom of an organisation and which may be useful, never get to the top except through strong influential pressures. If upper management is open to the ideas, feelings, and attitudes of those below, they will gain valuable policy input from them. The openness of upward communication and the use of participatory management methods can do much to generate upward policy formulation process.

In general, it is advisable that managers review all policies periodically, as some might have outgrown their original purpose or usefulness. They should not be glorified and perpetuated merely because they are policies; rather, they should be modified or replaced when circumstances call for such a change. Once a policy has been adopted or modified, it should be communicated to all affected by it. It is advisable to communicate policy statements at all levels in writing and to maintain a policy file that is accessible to everyone. People expected to conform to a policy have a right to know that such a policy exists, the purpose of that policy, and why it was formulated. Since policy formulation is not a guessing game, certain definite steps are stipulated to be followed by decision makers when formulating new policies or modifying existing ones.

These are (Kalejaye, 1998):

1. Identify the need for a policy in a given area.
2. Source and collect all relevant and possible information for policy formulation.
3. Consideration must be given to all alternatives, especially as they relate to the policy.
4. Analyse all possible available outcomes.
5. Select the best policy statement so far, taking into consideration its possible
6. Review the policy statement with the employees and others who will be affected by it.
7. Ensure the policy is in line with the other existing policies of the organisation.
8. Draw out the final policy statement, including the effective dates of such a policy.

Self-Assessment Exercise 1

List the steps required for formulating a new policy or review an existing policy.

4.3.2 Types of Policies

The type of organization influences the type of policies muted for compliance. The regulations which guide decisions and actions vary considerably and cut across the hierarchical structure of the organization depending on the nature and magnitude of the objectives. There are many types of policies marketing policies, financial policies, production policies, personnel policies, to name a few in every organization. Within each of these areas, more specific policies are developed. For example, personnel policies may cover recruitment, training, promotion, and retirement policies. Viewed from a systems angle, policies form a hierarchy of guides to managerial thinking. At the top level, policy statements are broad. Management is responsible for developing and approving major company policies. Middle managers usually establish less critical policies relating to the operation of their sub units. Policies tend to be in line with these policies. Each policy must help the firms reach their goals, and there shouldn't be any conflicts between policies in different sub-systems.

Although it is customary to think of policies as written statements, it is not necessarily the case.

For example, a firm may simply decline to consider handicapped employees in the selection of new personnel. In practice, this becomes the company's policy, even though it has never been said out loud.

There are many types of policies. Examples include: hiring university-trained engineers; encouraging employees' suggestions for improved cooperation; promoting from within; conforming strictly to a high standard of business ethics; setting competitive prices; and insisting on fixed, rather than cost-plus, pricing. Hicks and Gullett (1985) expressed the opinion that every operating area, ranging from sales, procurement, manufacturing, personnel (human resources), and finance, needs a hierarchy of supporting policies to drive the business. This action makes policies better by defining the limits of the organization and making sure that decisions are made with the organization's goals in mind. As you move from goals to policies to procedures to rules, the limits get smaller and smaller.

Steiner (1969) stated that the regulations which guide decisions and actions very considerably and cut across the hierarchical structure of the organization depend on the nature and magnitude of the mission to be accomplished. So, he made a pyramid to show how different business policies fit together. This pyramid will be used as a model, as we'll talk about below.

Source: Steiner, G. (1969), quoted in Kalejaye, A. (1998). Top Management

Major Policies: Main purpose they provide guidelines pertaining to such things as the line of business and ethical conduct of organizations.

Secondary Policies or Corporate Policies: These policies are broad and general policies formulated at the upper levels of management of the organization. These policies apply to the entire organization and deal with business facets such as the selection of major products and services and the selection of marketing areas. A lot of the information that comes out of making sure that major policies are right can be used to make secondary policies, which are more specific than major policies.

Policy Functions: this deal with specific functional areas of the organization. They involve policies that specifically relate to marketing, production, finance, and other functional areas. As an example of a functional marketing policy, the ABC Transport Company will let customers exchange or return items they have bought within one month.

Minor Regulations: They come after functional policies and explain in detail things like equipment maintenance, schedules, plant layout, absenteeism, and so on.

Procedure: This is a series of related steps or related tasks expressed in chronological order to achieve a specified purpose. The procedure defines, in step-by-step fashion, the method by which policies are achieved. They outline precisely the manner in which an activity must be accomplished. The procedure generally permits little flexibility and deviation.

Rules: This is a statement of what may, must, or must not be done in a particular situation or when playing a game. It explains in a lucid manner what an employee should do or is advised to do in a particular situation. You can also describe rules as habits, the normal state of things, or what is true in most cases. Finally, a rule is a statement of what is possible according to a particular system. Rules permit the use of discretion in performing a particular task.

Self-Assessment Exercise

What is the main characteristic of functional policy?

Business policies

Business policies are sets of rules followed by a store or group of stores that define business processes, industry practices, and the scope and characteristics of a store's or group of stores' offerings. They are the main

source and template for all practices that are allowed and supported in a store or group of stores.

In WebSphere Commerce, business policies are enforced with a combination of one or more business policy commands that implement the rules of the business policy. Each business policy command is a Java class. A business policy command can be shared by multiple business policies. The parameters passed to the business policy command determine what the command does.

Parameters affecting the function of a business policy command can be introduced in three places: The contract terms and conditions reference the business policy, the business policy definition and the business policy demands.

The business policy definition may specify a set of parameters that are automatically fed into each invocation of any of the commands associated with the policy. A business policy may specify additional parameters when it is invoked. Lastly, a contract's terms and conditions may add extra parameters to a business command that aren't found anywhere else.
Business policy commands for the same type of business policy must have the same interface. The following categories of business policies are provided in Web Sphere Commerce:

List of business policies
Catalog business policies outline the scope and features of a store's catalog of products for sale, such as prices and how the products are grouped.

Payment policies for businesses
Invoicing, payment, and refund business policies define how a store accepts payments, pays refunds, and the format of a store's invoices.

Returns to business policies
Return business policies specify whether or not refunds are accepted, how long they are accepted for, and whether or not re-stocking fees apply to returns.

Shipping company policies
The shipping business policies define the shipping providers a store can use and the associated charges with each type.

Business policies for referral interfaces
Referral interface business policies say how a proxy store and a remote store should work together. Many contract terms and conditions reference business policies. This provides a measure of control over the nature of

contracts a store enters into, providing flexibility in creating the contract terms and conditions. There are several types of business policies being followed in the business environment. Business policies may be of the following types:

1. **External Policies**: Policies framed to give effect to the decisions of the government, judiciary, trade associations, and such other external forces are what are called "external policies. For example, under the Income-Tax Act, every employer is bound to deduct tax from the salary payable to employees every month. Similarly, the government requires a certain number of jobs to be reserved for the backward sections of society. To give effect to such orders, policies may be formulated at the enterprise level.
2. **Internal Policies**: These are formulated to give effect to certain decisions taken by the owners of a business establishment; they are what are called "internal policies. For example, it may be the policy of a certain private-sector organization to appoint certain categories of workers on a purely on-contract basis. Similarly, a business organization may adopt a policy of producing only for the foreign market.
3. **Appealed Policies**: Such policies are formulated to give effect to the suggestions of the staff of an organization. For example, the employees may make an appeal to the top management to retire. If the management agrees with such a proposal, it could be made into a policy.
4. **Explicit Policies**: Those policies of an organization that are stated outwardly are called explicit policies. Such policies form part of the organization's manual. Most of the policies of an organization are explicit in nature. The sales policy, credit policy, etc., may be cited as examples. Unspoken Policies:

These policies are not stated outwardly. For example, every organization follows a certain policy for the recruitment of employees. Such a policy is not usually stated explicitly.

Even the existing employees may not be aware of it.

4.3.3 Reasons for Formulating Policies

Many professionally managed businesses acknowledge that it is necessary to have policies in all the major functional areas of management. The focus areas will thus include production policies, purchasing policies, marketing policies, selling and promotional policies, etc. All these policies are expected to give support to the overall objectives of the organization as defined by the top management, and they complement each other. The major reasons for having policy areas are as follows:

1. It is impossible and wrong to rely on expediency or precedents to solve problems that arise intermittently or regularly. To that extent, decision-making is more consistent and detailed when policy is defined and known.
2. Policy provides continuity for the organization. They are more permanent than individuals who are employed and later leave for greener pastures or are sacked, thus providing an enduring foundation for continuity.
3. They help to facilitate the expansion and integration of new businesses into the company, so that when growth occurs, there is already a firm foundation policy to apply in the new situation.
4. They provide a yardstick with which to measure progress in the organization. For example, the policy on the issue of stock items _ stipulating that no condition on which stock should be issued on verbal instruction. This may not be achievable instantly, but it sets a standard against which progress can be measured as the policy is implemented.
5. They stimulate action because managers and supervisors have the knowledge and confidence to make decisions and take actions knowing fully well that they are following laid-down policies.
6. Policies also save management time because the information is available and the procedures for carrying them out are known. This, of course, assumes that the policies are made freely available to those who require them.
7. They promote fairness in treating employee matters, provided the policies take account of the needs of the entire organization and are interpreted consistently.
8. Policies serve as the basis for the defence of the various organisational actions and activities in the event of challenges and litigation in the court of law.

4.4 The Uses of Polices for Management Effectiveness

Policies are of great importance to every organization as they are used to establish stable acceptability by the public. Kalejaye (1998) itemised the various uses of policies as follows:

1. Policies are used to prevent deviation from a planned course of action by providing a clear guide to follow. They provide the communication channels between organizational units, thus facilitating the delegation process.
2. Policies provide a conceptual framework within which other plans can be established to form a balanced and coordinated structure of plans. Since they serve as a guide to further action, the existing policies relieve managers of the necessity to ask superiors for permission to do or not to do certain things. As long as managers

are conforming, they can safely proceed and use their own initiatives.

3. Through policies, closer coordination and cooperation can be promoted among the organization's elements. Closer coordination and easier delegation will permit a greater degree of decentralization within the organization.
4. Employees are more likely to take action and voluntarily assume greater responsibility when they are aware of organizational policies. Personnel are more likely to act if they are confident that their actions are consistent with organizational policies.
5. Definiteness and flexibility are both desirable for goal attainment, but calculating the tradeoff is the problem. In certain cases, decisions are too trivial to require policy and, at the other extreme, decisions may be too important to rule; hence, in between these extremes, there is a need for policies to save time and increase the speed of decision making.
6. To the subordinates, policies will not only serve as a means of exercising authority; they will also lay down the guidelines that define and limit the exercise of the subordinates' authorities and responsibilities.
7. Policies underlie the planning of a future course of action. They show the way future plans and activities of an organization are formulated and implemented.
8. Policies define and clarify the objectives and goals of an organization. They give a further definition of how the objectives of the organization can be accomplished.
9. Policies are especially important at lower levels, where the relationships between actions and objectives are frequently ambiguous. Policies are used to bridge the gap, ensuring that staff actions are consistent with the broad policies and actions of the organisation. If this were not done by policies, every action would have to be approved, putting an impossible communication burden on coordinating supervisors.
10. Policies are used to mould and project the image of the organization before various interest groups, such as shareholders, suppliers, customers, employees, and the public in general.
11. The reputation that a company enjoys, whether favourable or otherwise, is frequently linked to the way an outsider perceives the company through its policy structure. It is common to hear credit policy or the'

4.4.1 Integration and Relationship of Policies to Objectives

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olicies are general statements specifying how objectives are to be accomplished; they are Organizational objectives and policies are not mutually exclusive components of the management process. Rather, the

relationship between policy and goal is highly interdependent and inseparable. The two are interlocked and interrelated; while the objective defines the standard of what the organization should accomplish, the policy directs action towards the attainment of the standard set by the objective.

It is not possible to attain objectives without knowing the policy guidelines that must be followed. Similarly, strategies cannot be determined without first knowing the objectives to be pursued and the policies to be followed. Rogers (1973) provided the basis for the above analogy, which demonstrates the interdependence among objectives, policies and strategies.

Relationships between Objectives, Policies, and Strategies Source: Rogers, D.C.D. (1973). Corporate Strategy and Long Range Planning, Ann Arbor, Mich., The Landis Press, p. 18.

This indicates a situation where the boat is going up a river. The surrounding terrains represent the organizational purpose, and the surrounding terrains influence the general flow and direction of the river.

The primary objective is the harbour or stopping point, some distance up the river, to be reached by a certain time. Organizational objectives and other subordinate goals and plans can be represented by other milestones and the harbour. Policies are the river banks that direct and guide the boat towards the harbour. Like the river bank, policies remain in effect after the primary objectives have been reached. They are independent of time and must be reviewed as to acceptability and consistency whenever objectives are set. By all indications, it has been established that policies and objectives are related and that one leads to another. Policies serve as guidelines that provide managers with direction and vision when making decisions. With articulated and purposive policies, managers can make decisions core objectives realizable within the stipulated time.

4.4.2 Management Policy Areas

Management policy areas are very extensive; some of the specified principal areas are as discussed below.

Organization: The organization has to develop policies for itself. Such policies have to do with defining the appropriate departments, jobs, and ranks within the organization and their interrelationships in line with the corporate objectives of the organization.

Administrative Policies: Administrative policies of the organization are formulated with a view to ensuring that there is effective leadership, direction, and supervision at all levels and divisions of the organization.

Unions: The policy statements are set out to maintain appropriate relationships with management. Between the organisation and the unions/labour movement, they also space out the procedure for negotiating conditions of service and settling industrial disputes.

Control: Policies on control are essential in organizations because they facilitate and pave the way for the attainment of organizational goals by maintaining appropriate standards of tasks, personal and group performance.

Training and Development: This category of policies are formulated to guide the top management in providing programmes designed to meet the organization's needs, individual needs, and career requirements of managers and employees.

Incentive: This involves developing appropriate incentives to motivate employees and managers alike in order to ensure efficient performance.

Public Relations: This policy directs how much attention is paid to public attitudes and reactions to the organization's policies and practices**.**

Political Action: This policy expresses the position or attitude of the organization on political issues and events. The policy statement in this regard may restrain employees from talking to the press on political issues or even discussing political matters within the organization.

4.5 The Role of Workers in Policy Formulation

The concept of workers' participation in management policy formulation has always been controversial. The principal perspectives in which workers' participation in management policy may be seen as:

i. Workers' participation is viewed as a means of advancing the interests of workers;
ii. Workers' participation is a way of distributing power within the enterprise more equally and in handling conflicts of interest by democratic procedure, otherwise known as industrial democracy.
iii. By involving workers in policy formulation, this will bring about the effective utilization of the human resources of the enterprise.
iv. Workers' participation in management policy is in effect seen as the antidote to uncooperative attitudes and an increase in industrial conflicts.

Self-Assessment Exercise

1. Itemize the reasons why policies are formulated. 2. What is the relationship between objectives, policies and strategies?

4.6 Summary

In this unit, we have: described how policies are formulated; listed the types of policies; enumerated the reasons for formulating policies; highlighted the uses of policies for management effectiveness; explained how policies are integrated in relation to objectives; itemized management policy areas; and stated the role of workers in policy formulation. In the next unit, you will learn about organization policies, which is another topic.

4.7 References/Further Reading

Gomez-Mejia, L. R., Balkin, D.B. & Cardy, R. L (2005) Management _ People, Performance, Change New York McGraw-Hill Companies

Hicks, H. G and Gullett, C. R (1985) Management Singapore McGraw-Hill, Inc

Kalejaye, A. (1998) Basic Management Practice Lagos Mak-Jay Enterprise

4.8 Possible Answers to Self-Assessment Exercise (s)

SAEs 1

The major reasons for having policy areas are as follows:

i. It is impossible and wrong to rely on expediency or precedents to solve problems that arise intermittently or regularly. To that extent, decision-making is more consistent and detailed when policy is defined and known.
ii. Policy provides continuity for the organization. They are more permanent than individuals who are employed and later leave for greener pastures or are sacked, thus providing an enduring foundation for continuity.
iii. They help to facilitate the expansion and integration of new businesses into the company, so that when growth occurs, there is already a firm foundation policy to apply in the new situation.
iv. They provide a yardstick with which to measure progress in the organization. For example, the policy on the issue of stock items _

stipulating that no condition on which stock should be issued on verbal instruction. This may not be achievable instantly, but it sets a standard against which progress can be measured as the policy is implemented.

v. They stimulate action because managers and supervisors have the knowledge and confidence to make decisions and take actions knowing fully well that they are following laid-down policies.

SAEs 2

Relationships between Objectives, Policies, and Strategies Source: Rogers, D.C.D. (1973). Corporate Strategy and Long Range Planning, Ann Arbor, Mich., The Landis Press. This indicates a situation where the boat is going up a river. The surrounding terrains represent the organizational purpose, and the surrounding terrains influence the general flow and direction of the river.

UNIT 5: THE CONCEPT AND FIELD OF PUBLICPOLICY ANALYSIS

Unit Structure

5.1 Introduction
5.2 Learning Outcome
5.3 Definition of Public Policy
5.3.1 the Features of Public Policy
5.4 the Meaning of Policy Analysis
5.5 Summary
5.6 References/Further Reading
5.7 Possible Answers to Self-Assessment Exercise (s)

5.1 Introduction

According to Olaniyi (1998), public policy analysis is a field of study that has its meaning enriched by two separate terminologies—namely, "public policy" and "analysis." Thus, any attempt at understanding the field must first explain the two concepts separately before their integration.

5.2 Intended Learning Outcome

At the end of this unit, you should be able to:

- discuss the definition of public policy
- explain the features of public policy
- examine the meaning of policy analysis.

5.3 Title of the Main Content

A policy can refer to a proposal, a major decision, or the refusal to make a certain decision. (Sharkanskv: 1978).

In other words, policy is simply actions taken or to be taken by a government or private organization. (Ikelegbe, 1996) A policy option made by an individual is known as a "private policy" because it affects only that person and not any other person. (Olaniyi: 1998). It can be used and aimed at a wide range of people and groups that are or aren't part of the state's system and are, to varying degrees, free from state

control or influence. (Barrett and Fudge:1981) Chandlier and Plano (1988) defined public policy as "the strategic use of resources to alleviate immediate problems or government concerns". Dimock et al. (1983) said that public policy is deciding at any time or place what goals and substantive measures should be chosen to deal with a specific problem or new idea.

It also includes the reasons they should be chosen.

Self-Assessment Exercise 1

Define Public Policy?

5.3.1 The Features of Public Policy

The main features of a policy are that, first, it involves a choice. It is an important choice or a critical or important decision taken by individuals, groups, or organisations. Therefore, there have to be several policy alternatives, and policy formation involves the development of several policy alternatives and the choice of an alternative.

Second, policies are proposed courses of action or projected sets of decisions. Policies are prospective or are statements of future actions. Policies state what is going to be done or would be done. It outlines a course of contemplated or desired action in relation to certain desired objects or events in the real world.

Third, a policy is goal-oriented. It is directed at the attainment of certain end states or objectives. A policy has a certain purpose or intention. Fourth, policies have to do with particular problems or problem areas.

They are not abstract, but rather relate to and are actually responses to the challenges and pressures arising from an environment. Furthermore, policies are designed and targeted at solving existing or future problems or satisfying certain needs.

Finally, a policy is a course-setting action. It provides the direction, the guide, and the way to the achievement of certain goals. It provides the framework within which present and future actions are undertaken. It is a major guideline for action (Ikelegbe 1996).

5.4 The Meaning of Policy Analysis

Policy analysis is defined as a set of techniques that seek to answer the question of what the probable effect of a policy will be before it actually occurs (Shafritz 1986:409). This refers to a "before the fact" analysis of

public policies. However, the term is also frequently used to refer to analyses of public policies conducted both before and after the fact. But analysis undertaken on a programme that is already in effect is more properly called all policy analysis. It uses systematic research methods, most of which come from other fields.

Similarly, Chanlder and Plano explained policy analysis as an attempt to measure organizational effectiveness through an examination and evaluation of the qualitative impact of an agency program. Policy analysis is a systematic and data-based alternative to intuitive judgments about the effects of policies or policy options. It is used

1. for problems' assessment and monitoring.
2. as a "before the fact" decision tool, and
3. For evaluation (Olaniyi, 1998:17).

Furthermore, Roberts and Edwards (1991:98) argued that policy analysis is the study of the formation, implementation, and evaluation of public policy; the values of policymakers; the environment of the policymaking system; and the cost of policy alternatives.

Lastly, policy analysis can also be used in a different way to mean a detailed look at a policymaking system at any or all stages of the policymaking process.

Self-Assessment Exercise 2

What is policy analysis?

5.5 Summary

The unit discussed the conceptualization of public policy and its characteristics. In addition, the meaning of policy analysis was also analyzed to enhance your understanding of public policy analysis.

5.6 References/Further Reading

Barrett, S. and Fudge C. (eds). Policy and Action Essays on the Implementation of Public Policy. London and New York: Methuen.

Chandler, R.C. and Plano, J.C. (1988). The Public Administration Dictionary. England: ABC-CL 10.

Dimock, M.E., et al (1983). Public Administration. New York: Saunders

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Roberts, G. and Edwards, A. (1991). A Dictionary of Political Analysis.London: Edward Arnold.

Shafritz, J.M. (1986). The Dictionary of American Government and Politics. New York.

Sharkanskv, I (1978). Public Administration Policymaking in Government Agencies. Chicago: Rand McNally College Publishing Company.

Olaniyi, J.O. (1998). Foundations of Public Policy Analysis. Ibadan: SUNAD Publishers Limited.

Ikelegbe, A.O. (1996). Public Policy Making and Analysis. Benin City:URI Publishing Ltd.

5.7 Possible Answers to Self-Assessment Exercise (s)

Answer to Self-Assessment Exercise 1
Public policy can be defined as actions taken or to be taken and actions not taken or not to be taken by government.

Answer to Self-Assessment Exercise 2
Policy Analysis is a set of techniques that seeks to answer the question of what to probable effect of a policy will be before they actually occur.