THE RULES OF RISK

Taking chances in business is not about making random punts – it requires understanding, practice and discipline. Graeme Yell explains

One only has to open the newspaper to see the most terrifying – and topical – word in business continually played out: risk.

The dramatic ups and downs of the past four years have transformed risk, taking it from being a fairly obscure function and casting it firmly into the glare of corporate, regulatory and public attention. Despite this, it's not at all clear what people mean by 'risk'. In the public understanding, risk is synonymous with investment bankers placing billion-pound deals. In the corporate mind, risk is sliced and diced into operational, credit, reputational, market and so on. For politicians, it's a risk-averse public and business community that is contributing to stalled economic recovery.

'Decision-making with consequences' may be a good definition. If we accept that, we can see that it applies to all fields of endeavour – it is something we all do every day. So it's no surprise that I'm often asked: "How do we get better at risk-taking?" The answer is complicated by the fact that many organisations insert structure and process into what is essentially a human behaviour. As with all behavioural characteristics, you could take the 'best' risk-taker and put them in an environment that hampers their effectiveness.

To put this all into context, Hay Group conducts regular research into employees' appetite for risk-taking compared with the organisational 'reality'. Its latest report, *The Stubborn Gap*, draws on its Organizational Climate Survey of more than 100,000 employees from 1,300 companies over a five-year period. Although companies have taken steps to avoid a repeat of the 2008 downturn, the gap between the level of risk allowed by company procedures and the way in which frustrated employees would like to behave reached or exceeded 20% in nearly half of companies. Above this level, firms are at high risk of employees circumventing organisational controls to 'take matters into their own hands'.

Human appetite may be hard to control. As Princess Leia says to Grand Moff Wilhuff Tarkin in *Star Wars*: "The more you tighten your grip, Tarkin, the more star systems slip through your fingers." She might have said: "The more you try and control risk, the more people will find ways to evade your controls." But the good news is that a lot of the behaviours and skills akin to effective risk-taking can be developed.

What makes an effective risk-taker?

Effective risk-takers tend to demonstrate the following recognisable characteristics:

- **Achievement-driven** – but they are moderated by an appreciation of organisational goals, and willing to seek support when necessary.
- **Broad scanning** – they understand the bigger picture and don't just see decisions in isolation.
- **Conceptual thinking** – they are able to apply experience and recognise patterns – they don't need 100% of the information, but aren't taking random guesses either.
- **Strong 'locus of control'** – they take personal accountability for their actions and their outcomes.

To an extent, the characteristics of ineffective risk-takers are the converse of the above, but there are two main types:

- **The mouse** – is highly indecisive or always needs 100% of the information. The result is that they never take any risks at all.
- **The 'big dog'** – is obsessively driven by a burning desire to break every record or attain hero status. This achieves astonishing results when the formula works, but if things start to go wrong, the 'big dog' will bet the mortgage, the grandmother, the whole firm.

Are risk-takers born or made?

THE PERSONAL EFFECT

All of the effective behaviours discussed above can be developed – although they're mostly deeply ingrained, so it takes serious dedication and practice. To become better risk-takers, employees will firstly need:

- An understanding of the organisation's risk appetite;

TOP TIPS FOR EFFECTIVE RISK-TAKING

- Recognise that risk-taking is a behaviour, not a process, job or department. You can learn to get better at it.
- Make risk planning central to your business model and corporate culture. Siloed compliance, finance and strategy departments can lead to inconsistency in behaviour and risk appetites.
- Identify your best risk-takers and empower them to make decisions, and likewise, appoint mentors to help ineffective risk-takers to improve.
- Define structures, roles, reward and recruitment policies that support your corporate appetite for risk – and do not overwhelmingly employ ambitious high-flyers.
- Ensure risk management cascades down from the CEO. Top leaders need to communicate consistently and ensure all departments understand their responsibilities around risk.

MATTHIAS CLAMER/GETTY

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- A mentor to help them understand the characteristic itself (through formal development and feedback); and
- Practice (safely at first).

Risk-taking isn't necessarily a solo activity – teams can get better by taking the time to understand their existing decision-making skills and considering how to combine strengths and mitigate weaknesses across the group. This goes hand in hand with enhanced cooperation and teamwork.

The final factor is accountability. Good risk-takers take personal accountability for outcomes – feeling the glow when it goes well and the pain of failures is critical – and the knack is working with these emotions, learning and improving from both.

THE ORGANISATIONAL EFFECT

Line managers must strive to ensure that their team develops a risk appetite in line with that of the organisation, but this is challenging (see the Princess Leia point earlier). If the organisation restricts or overstretches employees, they will become frustrated or stressed.

Line managers are also key to assessing where someone feels reluctant to take risks and explore the personal, cultural and organisational issues that inhibit them. You can explore the level of reluctance through the following formula: $R = 1/(A \times I \times S)$; where R = reluctance, A = assessment of own ability (in relation to a task), I = incentive to do it (not just money) and S = self-confidence.

For many years, companies have been hardwiring their organisations to take on more risk by recruiting and developing people with a high achievement motivation. The desire to achieve clearly has beneficial results for businesses. But companies need a range of effective systems to manage that behaviour and prevent it getting out of control.

Successful risk management also relies upon managers being able to extend their influence beyond the confines of the risk function itself. Persuading other business areas to take shared ownership, responsibility and a consistent approach to risk management is a hallmark of success.

Examples of effective risk-takers

There's a much-quoted line that has been attributed to many golfers: "The more I practise, the luckier I get." Risk-taking is not about taking a spin on a roulette wheel or a random punt on a horse, but a matter of understanding, practice and discipline.

While many see Richard Branson as a brazen entrepreneur who thrives on risk, perhaps he should instead be viewed as a successful risk mitigator. Always striving to achieve, spot a gap in the market and 'shake things up', Branson recognises that risk is a balancing act: "If you are a risk-taker, then the art is to protect the downside."

Despite numerous knock-backs, George Lucas saw the potential of *Star Wars* and the value of merchandising and sequel rights. In October, he sold his production company Lucasfilm, together with the *Star Wars* franchise, to entertainment giant Disney, for a whopping $4bn.

...and some less effective ones

The Darwin Awards are testament to the world's less successful risk-takers. One can only hope that many others have learned from their mistakes and are now building effective risk-taking behaviours.

Meanwhile, corporate casualty Lehman Brothers and the government payouts made to shore up high street banks only underline the extent of the fallout from misjudging risk. In Lehman's case, the firm's aggressive growth strategy and its approach to risk led to its ruin. Appetite for risk was reportedly increased and breached, internal warning systems were repeatedly ignored and, despite this, more business was taken on.

Ultimately, while many have tried and failed, neither you nor your business will reach your true potential without a healthy appetite for risk and the desire to pursue new opportunities and innovate. In the words of Goethe: "The dangers of life are infinite, and among them is safety."

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