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Strategic, Legal, Financial, and Operational Risks for Businesses During COVID-19 Pandemic

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Abstract

The economic effect of the COVID-19 pandemic is as significant as the threat it poses to public health. Companies are negotiating a new world dealing with new risks. Organizations seek confidence in their risk management and control frameworks and reaction strategies for the short, medium, and long term as COVID-19 grows to threaten commercial life. As a result, it is critical for firms to be proactive in analyzing their risk and susceptibility from many aspects. This exploratory research seeks to discuss some major risks faced by many organizations during the pandemic, namely, the strategic, compliance, regulatory, financial, and operational risks. To thrive in this new business climate, organizations must take immediate action to limit risks and prepare for both fast and gradual recovery. Businesses that properly manage risk not only endure but also strengthen their endurance and equip themselves to capitalize on new possibilities.

Keywords: *Business, COVID-19, Financial risk, Legal risk, Strategic risk*

1. Introduction

Even before the pandemic, organizations faced external and internal challenges from new business environments across the globe. The causes for this include a move to digital platforms and technologies, a growing dependence on third parties as well as the cloud (Alhaddad, 2021), changing laws and regulations, and the challenges that all of this poses to the effectiveness and integrity of risk operations.

COVID-19 has intensified these difficulties. To limit the consequences of the pandemic on their own operations, risk managers must comprehend the pandemic's effect. They have had to keep an eye out for new dangers to the increasingly remote workforce, present and prospective borrowers, and other bank clients, changing regulations, and consumer preferences.

The business environment has grown substantially more perilous in the last year as a result of prolonged uncertainty and misunderstanding in pandemic response tactics, issues with vaccine rollouts, and evolving virus variations - and repercussions into other risks.

Businesses have had to deal with simultaneous economic and health problems, which has resulted in new employee and customer interaction rules, unprecedented remote working, supply chain re-engineering, bankruptcies, consolidations, and inventive collaborations (Liu, Lee and Lee, 2020; Sheth, 2020).

Businesses are questioning how to plan for what may lie ahead in light of these changes and the long-term risk outlook. Their primary concern is survival and the development of resilience. Not just in terms of current pandemic effects and competitive posture, but also in terms of newly released cyber-attacks, catastrophic climatic catastrophes, and social upheaval that need workplace and community reform (Asgary, Ozdemir and Özyürek, 2020).

While many organizations have evolved and adapted to quickly changing conditions, capturing market share along the way, not all have. Not everyone will profit from the anticipated economic upswing. During this turbulent recovery phase, businesses must brace themselves for a chaotic shakeout. In order to be more resilient to future shocks, they will need to reinforce and continually assess their risk mitigation procedures (OECD, 2020) (Aidar Vafin, 2018).

Organizations nowadays work in an extremely complicated environment. New technologies, increased digitalization, and growing consumer expectations present a plethora of hazards that might imperil operations, erode cybersecurity, and negatively impact a company's brand or financial situation (Atieh, 2021a, 2021b). Ineffective risk identification, management, and mitigation may also result in business failure.

2. Strategic Risk during Covid-19

Strategic risk refers to the threats that businesses confront in pursuing their strategic goals. Even if strategy seems to be realistic and on track to achieving, assessing the strategic risks associated with it may assist businesses in identifying hurdles or chances— and addressing them before it is too late (Aumann and Dreze, 2009).

Strategic risks occur when a plan does not provide the desired results, therefore impairing the firm's development and progress (Beasley, Frigo and Litman, 2007; Frigo and Anderson, 2011). Such risks arise as a result of technology changes due to the COVID-19 outbreak, changes in the competitive environment, or shifts in client preferences after COVID-19 lockdowns. To remain competitive, successful firms must do rigorous strategic planning. In terms of execution, this entails streamlining processes and also developing a viable plan. However, many businesses miss out on market possibilities as a result of their failure to manage strategic risks.

During the Covid-19 pandemic, the strategic risk may manifest itself in a variety of ways. One is following the incorrect strategy, such as excessive investment in a new product or acquisition. Even if a plan is a sound, failing to implement it successfully is another problem. Additionally, there is an issue of delay due to the lockdowns or failure to react to significant market movements. External variables like as changing client preferences and developing technology during work from home may make the current approach useless or obsolete.

In the near term, an organization may tolerate more strategic risks but will take an effort to mitigate or remove such risks over time. A typical illustration of this kind of risk is changing in the global availability of a critical raw material due to the COVID-19 supply chain disruptions. For example, if the issue is worldwide in scope, the firm may be powerless to prevent it in the near term by switching suppliers (Cai and Luo, 2020). However, over time, by restructuring its manufacturing methods, it may be able to minimize or remove its dependence on the material.

Finally, certain risks should be disregarded and certain business opportunities rejected, either because the potential consequences are too severe or because the chance of success is so low that the rewards are inadequate to justify taking the risk. However, a rival may seize these possibilities, and the earnings generated may help the competitor's firm grow.

There can be other strategic risks during the COVID-19 period. The first is strategic risks that are associated with internal company decisions, such as product development processes, marketing, communication tools, sales methods, and investments in cutting-edge technology. All of these factors have a direct effect on function, productivity, and overall outcomes. Another strategic risk that may arise is external. For example, a rival may introduce a game-changing product or creative solution that poses a considerable risk to the strategy's success (Markides, 2013). Investing in a concept with a low probability of success may result in significant financial hardship, revenue loss, and reputational harm.

Coping with Strategic Risk during COVID-19

Coping with strategic risk focuses on the particular choices and activities necessary to maximize the business's long-term risk-reward profile. Among the critical decision points are the following: • Risk accepting or avoiding (Bryant and Hagg-Rickert, 2001): Through organic growth, core business (latest goods and business growth), mergers, and financial operations, the company may choose to raise or minimize certain risk exposure. • Risk-based valuations: All firms assume risks in order to operate, and there is only one price at which those risks may be rewarded. That is reflected in the price of their goods or service, which should adequately account for the risk associated with them. • Risk minimization: This refers to the process of implementing business and risk management techniques in order to keep strategic risk within predetermined risk tolerance thresholds. • Risk transmission (Barrieu and El Karoui, 2004): If an organization's risk exposures are high or the expense of risk transmission is less than the expense of risk maintenance, it may choose to implement risk transfer measures through insurance coverage or financial markets. • Resource allocation: To optimize firm value, a company may deploy financial and human assets to business operations that provide the best risk-adjusted returns. Strategic risk management seems to be a continuous activity, and it is no different. While monitoring strategic risk involves unique problems, it may provide businesses with vital "heads-up" on impending hurdles. This provides the most potential leeway for changing strategic or tactical actions to reduce negative risk or capitalize on an unanticipated opportunity.

3. Compliance and regulatory risk in the COVID-19 period

The possibility of a change in rules and laws during the COVID-19 pandemic may affect an industry or a corporation. Such regulatory changes may have a considerable impact on an industry's framework, cost structure, and so on. Compliance risk, on the other hand, refers to the possibility that a business may be found in breach of pre-existing rules or regulations (Kurer, 2015). This may be due to a variety of factors, including insufficient controls, neglect, or human mistake. Assuring that a corporation is capable of and adheres to compliance may be a major investment. As with regulatory risk, compliance risk management is a critical component of an organization's overall risk management.

Compliance risk during the COVID-19 pandemic:

Compliance risk is the possibility that a company could face legal consequences, monetary fines, reputational harm, and financial loss as a result of failing to follow government laws, industry standards, or recommended best practices (Ramakrishna, 2015). This risk exists for all types of organizations, including public, corporate, for-profit, nonprofit, state, and federal.

During the COVID-19 pandemic period, to safeguard the health of individuals, countries, and organizations put in place limitations on mobility and methods for health monitoring and reporting. These tools, particularly contact-tracing and selfreporting applications, some collecting and sharing sensitive health information, underline the rising relevance of data security and privacy in this crisis (Bentotahewa, Hewage and Williams, 2021).

Legal risk is the financial loss incurred by a business as a consequence of legal actions, and any penalties incurred by a firm as a consequence of an inability to abide by the law (Sadgrove, 2016). Legal issues, of course, need the aid of qualified attorneys, and the accompanying expenditures. In recent years, one of the most visible instances of legal risk has been the emphasis on data or data leaks. If an organization holds any of customers' data, which is quite probable, it is critical that it adheres to all applicable data protection rules; otherwise, the organization risk jeopardizing company - and its customers. A data breach is not only financially costly but also has a negative impact on one's image.

A more pragmatic worry related to legal risk is the obligation of a company owner to safeguard workers from damage (Calkins, 1989). The development of Coronavirus has brought this necessity into sharp light in recent years, and there are particular standards for risk assessment during the COVID-19 pandemic. Failure to deal with these risks may land a firm in legal trouble.

The risk of the breach of privacy is associated with the changing business environment due to COVID-19 (Bassan, 2020; Faraj, Renno and Bhardwaj, 2021). A frequent danger of non-compliance is a breach of privacy laws. Hacking, viruses, and malware are just a few of the cyber hazards that businesses face. Additionally, if a business handles sensitive data, it is expected to take the necessary precautions to safeguard the data and avoid privacy breaches. Process-related. A process risk occurs when an established technique for accomplishing a job is not followed or when the standard process is deviated from. For instance, a business must have a written method for remotely accessing its network. When an employee violates the required method for remote access, this is referred to as a process risk.

A business may face several compliance risks. Legal compliance guarantees that the business, its agents, and personnel adhere to all applicable industry rules and regulations.

Regulatory risk during the COVID-19 pandemic

Regulatory risk during the COVID-19 pandemic involves the possibility that new laws or legislation during the pandemic may have an adverse effect on security, business, or industry. Businesses must adhere to rules established by industry-specific regulatory organizations. As a result, every change in legislation may have a cascading impact across a sector. Regulations may raise operational expenses, pose legal and administrative obstacles, and in rare cases, prevent a corporation from doing business.

Governments and regulatory agencies often establish new rules or revise existing ones after any major event takes place. The COVID-19 pandemic necessitated the use of updated trade policies by numerous nations. Medical supplies and supplies, as well as agricultural and food items, have been eased into the country, while export restrictions have been placed (Evenett et al., 2020). Import assistance and export restrictions were used to ensure that crucial goods were available to consumers at home (Evenett et al., 2020). Several instances of regulatory reforms that may influence businesses or sectors include the following:

Changes in international trade rules such as tariffs and trade policy may have an effect on businesses that export and import items on a regular basis (Crozet, Milet and Mirza, 2016) (Galeeva, Ivanov and Vafin, 2016). They also have an impact on investors who make foreign direct investments (Vafin, Morozov and G. M. Galeeva, 2012) (Vafin *et al.*, 2012) (Vafin, Morozov and G. M. Galeeva, 2012). Tax changes may have a significant impact on the bottom line of enterprises and private investors alike. Any change in income tax legislation has a direct effect on the revenue generated by parties involved and may introduce new regulatory risks.

Increases in the minimum wage may become a significant cause of regulatory risk since they have a significant effect on firms, particularly those that employ a big number of low-skilled workers. Small enterprises, in particular, incur larger losses as a result of their inability to use economies of scale (Посталюк and Вафин, 2014) (Вафин, 2012, 2013). As with the preceding instances, changes to mandatory holiday or sick leave during the COVID-19 pandemic have an impact on a business's bottom line since they oblige employers to provide workers with more time off (*Regulatory Risk*, 2020).

Managing regulatory risk requires both forward-thinking strategic thinking and a close examination of public sentiment and the regulatory system in a business's industry. Compliance risk requires an understanding of current laws and a more methodical approach to ensuring that the business complies with them all.

4. Financial risks

The recent surge of Covid outbreaks has escalated the financial concerns for individuals and companies. For corporations in financial distress, stimulus measures have provided them breathing room and may even be hiding a more serious level of vulnerability, especially in developing economies and emerging countries. Since the beginning of the COVID-19 lockdowns, the World Bank Group and other sources claim that global financial risks have increased, in part because companies have borrowed to address liquidity gaps while the decreases in corporate profitability have harmed their capacity to repay debt (World Bank Group, 2021). Many businesses may be unable to continue their operations after the pandemic is over, due to changes in customer behavior brought about by the health crisis and following lockdowns.

Many companies will suffer a significant setback. In the future, several industries and market sectors may no longer exist. Some will manifest themselves in various ways. Others will continue, albeit with a significant reduction in staff, business lines, and overall size. As the crisis continues to affect the supply chain, logistics, and other aspects of business, it has become unclear how these enterprises will be able to keep up with demand.

As an external shock, the COVID-19 has harmed businesses throughout the globe. Businesses must cope with debt management, greater borrowing rates as a result of unpredictability, and a rise in the likelihood of bankruptcy (Mulyaningsih et al., 2021) (World Bank, 2020). For example, in the wake of the COVID-19, several businesses were forced to shut down, lay off workers, or even declare bankruptcy, according to the recent research by (Guerrieri et al., 2020) (Vafin, 2017; A. Vafin, 2018).

Disruptions in the supply chain and lower demand from industrialized nations are largely to blame here, as they were in non-industrialized as well. Accordingly, the IMF's economic forecast estimates that the worldwide production loss caused by the epidemic would be in the neighborhood of US$28 trillion over the next five years. As a result of the uncertainty caused by an economic shock, businesses are obliged to reduce their output (Bloom, 2009) (Mulyaningsih et al., 2021).

The most fundamental financial risk is credit risk. Credit risk is a risk associated with borrowing money. Nearly every business will have to do it at some time, whether to finance startup expenditures or to allow the firm to develop and flourish. Businesses must assure that they can afford the repayments since non-compliance with the loan's conditions entails significant consequences. Credit risk, on the other hand, might apply to clients who are unable to make payments for their products or services. At some time, most firms will need to issue a credit to their customers, which carries its own set of risks. Customers who fail on payments will have far-reaching consequences that extend well beyond time and expenses connected with debt collection. Where a firm has shareholders, credit risk may affect them negatively, perhaps costing them significantly in interest or repayments. Costs associated with debt collection just compound this impact.

Another financial risk during the COVID-19 pandemic is the market risk. This is among the most significant categories of financial risks; as a result of demand and supply dynamics, this category of risk has a very broad reach. Market risks arise as a result of changing circumstances in the marketplace in which a firm competes for business. In other words, market risks refer to the possibility of being circumvented by a rival; this form of risk is heavily impacted by economic uncertainty. With the internet's growing dominance during the lockdowns, the way businesses work has changed drastically in a relatively short period of time. As an increasing number of people shop for goods and services online, brick-and-mortar retailers are feeling the squeeze. A company's market is always changing, which might have an effect on its profitability. For instance, organizations that anticipate this digital transformation in advance will have chances to flourish and expand throughout the development.

However, businesses that fail to prepare for these changes in advance will have to battle to remain viable.

5. Operational risks

The operational risk applies to the difficulties encountered when managing a firm on a day-to-day basis (Moosa, 2007). The concept encompasses a wide range of possible risk factors, including card abuse or neglect, human resource challenges, and inadequate management. Even the breakdown of technical equipment may have a financial effect on a business, which is why it is critical to have contingency plans in place for all scenarios (Born, 2014).

This form of risk arises as a result of a business's regular operations. Criminal activity, fraud, and corruption are all examples of operational hazards, as are personnel difficulties (Samad-Khan, 2008) (Alhaddad, 2018b). Operational risks arise as a result of poor management, a lack of or insufficient control within the organization, technology deficiencies, inadequate personnel training, and human mistake.

Criminals and scammers are taking advantage of the turmoil in the Covid-19 environment. Companies and their clients are increasingly exposed to cybercrime, investment scams, money transfer fraud, and business email exposure fraud because of the confluence of employees working from home, rapid adoption of new technology, and possibly weaker controls and monitoring (Deloitte, 2020). According to a poll, 77% reported a rise in fraud in 2020, and 92% predicted that number to climb through 2021 (Kizil et al., 2021). Preventing fraud has become more difficult, according to more than three-quarters of those polled. Though financial fraud and staff embezzlement are likely to grow in the next year, cybercrime was considered the most serious threat.

Cyber-attacks on businesses' IT systems and those of their staff working from home during the initial weeks of the Covid-19 epidemic posed a considerable external operational risk (Alhaddad, 2019). For instance, ransomware attacks have been on the rise in recent months, with the banking industry being one of the most often targeted industries. There are additional vulnerabilities in financial institutions' IT systems because of the widespread use of remote work by many staff. This presents a greater attack surface for cyber thieves.

Cyber hackers often target financial companies because of their IT infrastructure. As a result, risk management will continue to emphasize the need of investing in a robust IT infrastructure and improving cyber security at institutions (Mosteanu, 2020; Moşteanu, 2020) (Alhaddad, 2018a). In the future, educating workers on the dangers of working from home will be another method of reducing these hazards.

Operational risks are classified into two types: model risk, which pertains to the company's growth and development plan; and marketing risk (Mun, 2010). If the company's strategy is not thoroughly scrutinized, it may result in a financial disaster. Operationalized risk also includes fraudulent activity risk, which refers to economically incompetent or fraudulent action inside a business. Fraud risks jeopardize a firm's integrity; one effective technique to mitigate fraud risk is to use a voided check; it is critical to protect the privacy of a privately owned business or company's information.

Operational risks are difficult to accurately quantify, and they invariably lead to financial loss. To evaluate operational risk effectively, the organization must first build a historical record of failures associated with operational risks and afterward determine the probable relationship between these failures.

Operational risk comes from both internal and external sources and is often produced by people, procedures, and technology (Kuritzkes, 2002). Identification is a critical aspect of risk management. Failure to recognize risk will most likely result in no action being done to mitigate it. There are numerous techniques for determining risk. A frequently utilized technique in risk detection is the utilization of 'brainstorming' workshops. This may be utilized at many levels within an organization and is capable of identifying a significant number of hazards in a short period of time. To maintain ideas to improve, it is critical to keep risk identification discussions focused on risk identification and not on risk evaluation. Because operational risks are mostly determined by procedures and processes, they lend themselves to risk detection through an audit. Risk-based auditing may be used to both identify and report on the efficacy of an organization's risk management system to the board of directors.

Risk management in operations Risk assessment is used to determine its importance to the organization and whether or not to accept or address each individual risk. Once the risk's severity has been determined, any of the following risk-control approaches may be used: • risk acceptance • risk sharing or risk transfer • risk minimization • risk avoidance. Insurance is a time-honored technique of risk transmission. This is true for a variety of operational risks, such as building damage. However, there is a surge in the usage of insurance in conjunction with other strategies in recent years. One difficulty with quantifying and controlling operational risks is that, unless the risk happens, it is impossible to know the risk's effect. The risk's severity may be underestimated. One of the challenges associated with operational risk management is the ever-changing corporate environment. A strong internal control system is contingent upon a comprehensive and ongoing assessment of the risks to which it is subject.

Because operational risk is a reflection of human-created procedures and thought processes, operational risk can be thought of as a human risk. In other words, it is the risk of corporate operations failing as a result of a human mistake (Waring, 2015). It varies by sector and is critical to consider when evaluating future investment choices. Industries with a lower level of human involvement are expected to have a reduced chance of operational failure. The trend of transformation to automate business during the COVID-19 pandemic has accelerated, as a result, companies with automated activities seem to be ahead of the operational risk in some ways.

conclusion

The coronavirus disease 2019 (COVID-19) has had a huge economic effect in addition to its influence on public health. COVID-19 has a direct impact on business continuity by interrupting supply chains, business travels, manufacturing, and consumption, as well as jeopardizing financial markets. These risks may swiftly lead to liquidity issues, covenant pressure, re-financing needs, and increased third-party risk.

Risk managers should boost communication across risk departments and embrace new technology and tools to support an agile response to COVID-19 — as well as the new social norms that will develop. These solutions may assist the organization in quickly giving risk insights to support informed choices by boosting the precision and agility of data gathering and analysis.

COVID-19 has informed the businesses that pandemic vulnerability is real and has the potential to drastically alter a company's risk profile. This has made it clear that businesses must have a strategy in place to monitor and manage any major risks, and be ready for those potential consequences to rise in the future – no matter how implausible they may appear at the moment.

Risk executives must assist manage the COVID-19 danger while also collaborating with other senior managers. They should also ask the proper questions now in order to promote a later recovery... and to plan for the next large risk event.

It is critical to have an emergency scenario in place to maintain company continuity. In the present circumstances, it is critical to respond as quickly as can be in order to limit damages and other risks, as well as to prepare the organization for the further evolution of the COVID-19 outbreak and its conceivable scenarios. Business continuity management addresses infrastructure, cyber, personnel, business, operational, and connectivity risks, with the goal of managing an organization that must meet new challenges and risks while ensuring operational and production continuity.

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