Managing Project Risk in a Period of Economic Recession in Nigeria[1]

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ABSTRACT

The study examined the role of management in the impact of economic recession on Nigerian economy. The survey method of research design was adopted for the study. The population of the study comprised forty-eight (48) manufacturing firms listed on the Nigerian Stock Exchange. Data were collected from primary source through interview of the management accountants in each of the selected firms and analyzed using T-Test Statistics. Findings show that the key roles played by management in managing the impact of economic recession on Nigerian economy include; engaging in bulk purchases of raw materials and competitive buying, sourcing alternative local raw materials, embarking on cost engineering, prompt analyses of segments/products contribution margin, and carrying out comprehensive investment appraisals of every project to know the viable ones. Some other key roles were the use of weighted average costing method for valuing materials and replacement value method for pricing the finished goods. Based on the findings, we recommend that the producers of local raw materials for the manufacturers should endeavor to improve on the qualities of their raw materials to come up to the standard quality desirable by manufacturers. Also, management should perform their duties with meticulous professionalism by reacting promptly to the signs of an economy being in recession and report to the relevant authority.

One of the major consequences of recession is a general slowdown in economic activity over a period of time. It therefore beholds and organization to set up a robust Risk management to assist in consolidating property values, claims, policy and exposure information and provide the tracking and management reporting capabilities to enable the organization monitor and control its overall cost of risk. Unfortunately, unavoidable risks, the category to which recession belongs, is mostly ignored. This study therefore is an attempt at assessing the impact of recession on risk management systems and to

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appraise the effectiveness of the banks general risk management system. The study takes the form of a survey research, with questionnaires and interviews being the dominant source of data collected. Charts and tables have been extensively employed in presenting available data while the chi-square test was used in testing the stated hypothesis. The analysis of data shows that there is a significant relationship between the global financial crisis and the risk management systems of Nigerian banks. The global financial crisis placed a strain on existing risk management systems of banks in Nigeria. The study therefore recommends a strict adherence to the risk management system in place while the practice of constant review of this system should be adopted.

1.0 INTRODUCTION

Background of the study

It is trite knowledge that organizations exist for a purpose; either to deliver service or achieve particular outcomes to enhance the welfare its stakeholders. In order to realize their planned objectives, the organizations embark on several projects. Sometimes some of these projects suffer some setbacks due to unforeseen circumstances. Some of these unforeseen may impact project outcomes by interfering with the scope, completion time schedules, planned project costs and quality delivery. It is these unforeseen in a project that constitutes the projects" risks; which according to Heinz (2010) refers to the uncertainty that surrounds future events and outcomes.

Environmental conditions and constraints within which business organisations operate are the major sources of the risks which not only create negative outcomes but positive ones as well. it therefore stands to reason that the state of the economy within a business organization operates would certainly have significant impact on its project risks profile, nonetheless, in a recessionary economy.

An economy in recession is characterized by; sluggish demand, stagnant output, Business failures and increased unemployment – Chambers (1994). The challenge which an economy in recession poses to project risk management and how to weather the storm is the objective of this paper. Thus, are there risks that have become more critical as a result of recession in the economy, that require new skills and more attention to mitigate their impacts on project realization; or has recession created more opportunities that need to be exploited by project risk managers

2.0 ECONOMY IN RECESSION

According to the National Bureau of Economic Research, a recession is "a significant decline in economic activity spread across the economy lasting more than a few months, normally visible in real gross domestic product (GDP), real income, employment, industrial production and wholesale/retail sales – NBER (2008).

In the words of Onu (2016) “thus, generally, recession is established when there are two consecutive quarters of negative Gross Domestic Product (GDP) growth which result in a business cycle contraction and consequent general slowdown in economic activity with implications for macroeconomic stability; …persistent decline in Gross Domestic Product (GDP), investment spending, capacity utilization, household income, business profits; in addition to rising inflations and unemployment rates”.

Jazzapazza in a blog (2011) states that recession leads to reduction in confidence, which can further reduce consumption or investment spending. He further states that government, in a recessionary economy tend to borrow more money which leads to increased public spending, in an attempt to off-set the reduction in consumption or investment.

In his own contribution, Stacey (2016) states that in a recession, the economy slows down and the level of sales and production orders starts declining, production facilities become underutilized, and companies respond by reducing the work rate, casual workers are laid off; and this reduces their disposable income. The prospects for growth become gloom; banks increase interest rates to counter the rise in risk of default of loans. Ile capacity of production facilities reduces the output and most companies are forced to reduce operations.

2.1. NIGERIA IN RECESSION

After some prevarication, the National Bureau of Statistics released the much-awaited Gross Domestic Product (GDP) figures for the second quarter of 2016 with the GDP growth rate sliding further from -0.36 percent in the first quarter to -2.06 percent, year on year (PUNCH) This was quickly followed by the announcement from Nigeria’s Minister of Finance (Adeosun) that the country is technically in recession.

Again Onu (op.cit); in confirming the on-set of recession in the Nigerian economy states that…there has been a marked negative growth of GDP from -0.36 percent in the first quarter of 2016, to .0.26 percent in the second quarter and currently, at -2.24 percent in the third quarter. This bleak situation is also accentuated by persistent rise in inflation rate from 17.61 percent in August to 17.85 percent in September; and 18.33 percent in October 2016.

From the above, obviously Nigeria’s economy is in recession; that has seen our GDP drop to negative growth for two consecutive quarters, inflation rising to 18.33 percent, Direct foreign Investment (DFI) decline from $894.76 million in August to $694.76 million in September 2016. There is also sustained capital flight and massive depreciation of the local currency. The Federal Government is borrowing to fund the 2016 capital Budget and most private sector organizations are posting huge losses with many of them laying off staff, especially the banking sector.

3.0 RISKS AND PROJECT RISK

3.1 RISKS

Risk is the chance and, or probability of suffering loss, injury, damage or failure; Chambers. (1994) To Treasury (Orange book), risk is the uncertainty of outcome, whether positive opportunity or negative threat of actions and events. Heinz (2010), risk refers to the uncertainty that surrounds future events and outcomes. It is the expression of the likelihood and impact of an event with the potential to influence the achievement of an organization's objectives.

In general terms therefore, risk is a future event that may or may not happen, and if, and when it happens can impact on the planned outcomes either positively or negatively. Risks include both threats and opportunities because both have uncertainty associated with them. Risks to any task arise mostly from the requirements, assumptions, constraints or conditions surrounding its execution which may create the possibility of negative or positive outcomes. Risk is unavoidable in every human endeavor, and every organization needs to take action to manage it to a tolerable level that balances the possible negative consequences of risk against the potential benefits of its associated opportunity.

3.2 MANAGING RISK

Organizations are faced with many different types of risks ranging from Policies, Programs, political, operational, projects, financial, human resources to technological, health and safety. Any process involved with identifying and analyzing risks with a view to responding to them, is a risk management. No wonder Heinz (2010) defines risk management as 'a systematic approach to setting the best course of action under uncertainty by identifying, assessing, understanding, acting on, and communicating risk issues' An activity which integrates recognition of risk, risk assessment, developing strategies to manage it, and mitigation of risk using managerial resources.

3.3 STRATEGIES FOR MANAGING RISKS

Risk management involves the following processes:

- Establish goals (Risk environment)
- Identify Risks
- Analyze the identified Risks
- Evaluate the Risks
- Monitor and Control Risks

3.3.1 Establishing the goals

This involves establishing the strategic goals of the organization and its risk management context, and there from, identify the constraints and opportunities of the operating environment of the organization. This may include, but not limited to reviewing the regulatory requirements, codes, standards and industry guidelines as well as the relevant corporate documentation.

Identifying the Risks

Having established the organizational goals and its risk environment, the next logical step is to identify the risks that are likely to affect the achievement of the goals of the organization. Identifying the sources of the risks is the most critical stage in the risk assessment process. The possible sources of risk may include the suppliers, contractors and stakeholders and even the employees, and they need to be understood for an effective pro-active management.

Analyzing the Risks

Analysis of the risk involves screening the identified risks and defining for each risk, a profile using likelihood and consequences criteria, and applying the risk matrix, hazard matrices or risk graph. This is with a view to determining the likelihood of the event occurring. Higher risk requires more complex quantitative techniques to assess the associated risks.

Evaluating the Risk

The risks are then evaluated by comparing the analyzed risks against the previously documented and approved tolerable risk criteria. Where the new risk meets the criteria of acceptability given the risk appetite of the organization, it is then accepted but monitored continuously to ensure it remains acceptable.

4.0 PROJECT RISKS

Project, in the words of Osuagwu (1977), is a series of related activities with a goal, a beginning and an end. Ntamere (1995) sees project as a discrete package of investments or endeavor, policy measures and institutional and other activities designed to achieve a specific objective.

To Nwachukwu (2016), a project can be distinguished by the following:

- A well-articulated aim, goal or screened objectives
- A life cycle with a starting and ending points

- Must have a network of time and cost activities to produce a specific product.

That is to say that for any activity to be recognized as a project, it must cardinally be defined by scope, cost and time dimensions.

Projects are regular parts of business; while Risk is part of every project. *Dealing with the risks inside a project isn't much different from dealing with any other business risks that you encounter* (Newton, 2015). The objective of every risk management is always to maximize the results of positive risk, while minimizing the impact and consequences of negative events. Debono (2016).

All project activities carry some element of risk which is a future event that may or may not happen, but if it does happen; it will have an effect on project scope, schedule, budget or quality. Project risks are therefore, those risks that relate specifically to the project objectives as opposed to Business risks that generally relate to the organization. Risks show up the moment a project is conceived, in order to avoid project failure therefore, conscious efforts must be made at all levels to actively identify and pursue effective risk management during the life of the project. Project management is all about successfully **managing the associated risks** of each project to deliver benefit efficiently.

4.1 MANAGING PROJECT RISKS DURING PERIOD OF ECONOMIC RECESSION

As earlier stated, economic recession comes with a bag full of issues; that task the ingenuity of any project risk manager. These include increase in interest rates, rising inflation, depreciation of the local currency, import prohibition, f foreign exchange restrictions reduced investment spending by the public sector and massive job losses. The above economic scenario would certainly change the **business case.**

In response, as access to credit becomes harder, project (risk) managers cut back on spending and laying off staff to increase cash flow; this will in turn affect the schedule of delivery and possibly quality of delivery leading to increase in project risks.

4.1.1 Leveraging on Project Risk Management

The aim of project risk management is to deliver projects successfully. The fundamental principles of project management remain the same, even under the difficult periods of economic recession. Economic recession is only but a change, and project risk management has always provided a rigorous framework to manage change to achieve project objectives. The structure of project management ensures that the risks associated with every investment are fully understood and that necessary resources are available to complete the project. High inflationary rate and foreign exchange restrictions, all hallmarks of economy in recession bring about, the risks of cost over-run on projects.

In the face of the adverse effects of economic recession, project risk management process presents a template that can adjust to meet emerging changes in the business environment.

4.1.2 Positive risks (opportunities) of recession

It is not all bad news for project management in the period of economic recession. In its effort to fight recession, the public sector would usually go out of its way to encourage big spending with a view to refloat the economy. In the words of Sobowale (2016);…*the Federal Government plans to spend its way out of the current recession….this is the classic way governments have handled recessions which are caused by low aggregate demand..*

As government expands spending; new opportunities show up for businesses that significantly scaled down operations in the period of recession. Managing growth can just be as risky as managing cutbacks, perhaps even more so since growth involves significant financial investments. Project (Risk) management provides the structure that ensures the investment necessary to take advantage of a growing economy to deliver the anticipated benefits. It will ensure that each project fits the corporate strategy for growth, that the risks associated with the investments are fully understood and that necessary resources are available to complete the project.

5.0 CONCLUSION

Truly, economic recession increases the riskiness of projects and by extension, business. But at the same time, it is a wake-up call to project managers to become more sensitive to risk management. Economic recession in business parlance represents a change in business case and as such, the well-established fundamentals and process of project risk management presents veritable tools to handle the increased riskiness. This is achieved by modifying the weights of the risk parameters reflecting the changes – such as delivering les, but earlier, cutting costs to gain cash flow, checking assumptions, verifying business cases and examining time scales.

With the same project risk management techniques, principles and skills, project risk managers are not only able to deliver projects efficiently during recession, but also able to accurately advise on the best projects to pursue at the end of recession when growth expands.

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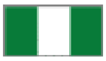

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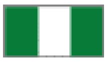

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