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METHODS OF RISK REDUCTION IN THE RISK MANAGEMENT OF AGRI-FOOD COMPANIES

Not only the perspective of their future development depends on the effectiveness of risk management of agri-food sector enterprises, but also the ability of the enterprise to function as a market player at the current moment, as well as the food and environmental security and the possibility of sustainable development of the national economy as a whole.

Precisely because of the high risks in the agri-food sector, risk avoidance or risks tolerating strategies are not widespread in the risk management of agri-food enterprises. The methods of risks reduction in agri-food are summarized in the Table 1 below.

Table 1

Methods of risk reduction in the agri-food risk management

Methods of risk avoiding	Methods of risk acceptance
1. Denial of certain activities	1. Methods of risk self-confrontation
2. Changing place of performance of activities	2. Methods of risk abatement
3. Changing the mechanism of performance of the activity (e.g. leasing instead of purchasing)	3. Distribution (transfer) methods

Source: developed by author on the basis of [1; 2]

The methods of risks avoiding: a/ are the simplest to perform; b/are the most effective methods of risk management; c/ the essence of these methods is evading risk. The methods of risks acceptance are diversified and not intended to eliminate the risk but aim for its consideration and minimization.

The methods of risk self-confrontation allow cover losses, as they occur, from the agri-food enterprise own funds. It includes: self-insurance; risk compensation due to current profit (direct write-off method).

Methods of risk abatement aim to minimize the probability of loss or the amount of negative effects of risks. It includes: organization

improvements; responsibility allocations; staff training; technical capabilities improvement; diversification; limitation; monitoring and control; lobbying etc.

Distribution (transfer) methods aim to share the risks among market participants, i.e. agri-food involved businesses, suppliers and sellers, transport and logistics, insurance, banks, construction, investment, factoring, leasing and other participants and stakeholders. It includes: insurance; hedging; sale of assets and securitization; subcontracting; guarantee and surety; factoring and leasing.

The economic methods of risks reduction in agri-food sector are shown below in the Figure 1.

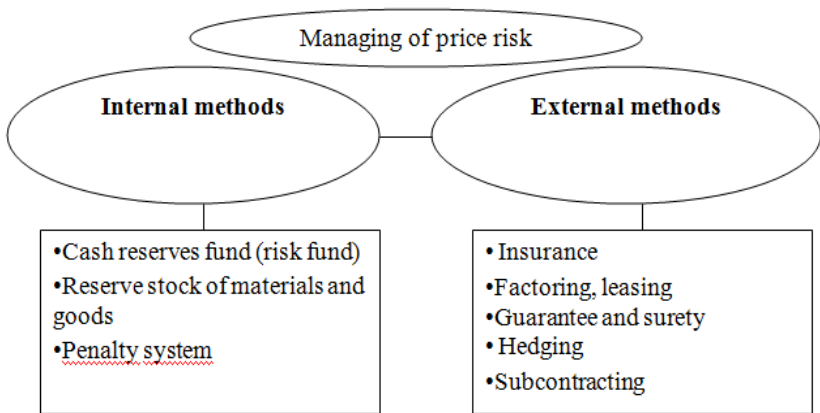


Figure 1. Economic methods of risks reduction in agri-food sector

Source: developed by author on the basis of [3]

The company’s cash reserves are the funds available to meet its needs for cash, especially unanticipated. Mille-Orr Model is used to calculate optimal cash reserves for the company.

The volume of reserve stock of material and goods is determined by a coefficient (1-3 or even more = risk coefficient) from the volumes of average daily goods sales and depends on the market state.

As for the penalty system implementation, types of risk depending on the contract counterparties only may be penalized. The penalty should partially or completely compensate the financial losses of enterprise in a case of risk situation. The ‘perfect’ penalty sum may include price risk losses plus inflation expenses (losses).

Summary. Risk avoidance and risk tolerating strategies are not widespread in the agri-food risk management due to the extra risk involved in this sphere caused by the natural factors. The agri-food enterprise is mostly managing risk by its reducing by themselves when facing it every day with high frequency and little loss. The risk is mostly transferred to the third parties when occurring with the low frequency but medium loss. The catastrophic risks occurring with very low frequency but causing very high loss should be overcome by the Government mostly. The economic methods of risk reduction in agri-food include the internal and external methods. Among the most applied internal methods are forming cash reserves funds, reserve stock of materials and goods, providing of penalty system.

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