Risk Management and Financial Performance in a Public Sector Context: A case of Ministry of Finance, Planning and Economic Development, Uganda

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Abstract

Financial performance remains at the forefront of maintaining efficient and vibrant public institutions. In pursuit of financial performance goals, risk management has taken center stage in many organizations. This article assesses the risk management process and analyzes its effect on financial performance at the Ministry of Finance Planning and Economic Development (MOFPED) of Uganda. The article leverages on empirical evidence generated from staff employed in risk management and financial performance at the MOFPED. The respondents included 83 randomly selected staff and 7 key informants. Content analysis was used to assess the risk management process while correlation analysis was used to determine the significance of risk management to financial performance. Results established a significant positive relationship between risk identification, risk assessment and risk control on financial performance. Notably, qualitative findings provide insights into the weaknesses in risk management. Specifically, risk conception was observed to often not take into account all possible risks. In addition, the root cause analysis often did not take into account a wider operations environment. Risk assessment faced a critical gap of inability to thoroughly assess risk occurrence and inability to regularly back-up application risk track programs. The underlying reasons for the gaps identified include; limited staff motivation and commitment, limited time and technical skills to undertake thorough information search and comprehensive risk analysis as well as inaccessibility of adequate and accurate information. The article provides recommendations for strengthening risk management.

Key words: risk management, financial performance, Ministry

Introduction

World over, there is a persistent concern about service delivery, accountability and value for money in organizations (Sax & Torp, 2015). Financial performance remains at the forefront of maintaining healthy and vibrant public institutions. In a public sector context, financial performance is considered a yardstick for maintaining reputation and credibility of organizations which depends on risk management. In pursuit of financial performance goals, risk management has taken center stage in many organizations. This is in recognition that risk remains a perpetual challenge affecting financial performance of organizations in the World (Yilmaz & Flouris 2017; Sax & Torp, 2015)

Risk management provides a basis of preventing uncertainties in the rapidly changing

environment (Soin & Collier, 2013). It is associated with great potential to address persistent poor financial accountability of accounting officers (Arena, 2010). Risk management minimizes the direct and indirect costs of the organization (Paape & Spekle, 2012) and improves the decision-making process (Brustbauer, 2016). Overall, it enhances achievement of set objectives and quality service delivery through accountability and efficiency (Bongomin, 2017).

In the context of Uganda and this study, the MoFPED has invested in building a robust risk management framework in a bid to enhance financial performance. To this end, the ministry established a risk management department with the main function to develop risk registers across all government ministries, departments and agencies, develop a risk management framework, develop expert knowledge and skills, and improve governance structures. Other critical departments include Information Technology and Performance Audit Department; and Internal Audit department. These were expected to play a significant role in risk management and works in liaison with other departments such as the Department of Finance and Administration (MoFPED, 2019).

Despite such a risk management framework, the ministry faces critical gaps in financial performance. For instance, the Office of the Auditor General Report (2017) discloses that the MoFPED paid Stamp Duty of UGX.29, 551,909,324 on behalf of UEGCL and UETCL for the registration of debentures issued in November 2015 in favor of the Export-Import Bank of China (EXIM Bank) which was computed on a loan of US$ 1, 435,158,682.48 to UEGCL and US$ 246, 412,437.33 to UETCL for the development of the hydropower dams. The Uganda Public Accounts Committee of Parliament (2018) identifies several unjustified payments from the Treasury in 2014/15, collusion and forgery leading to a financial loss of UGX114b in the MOFPED. Besides, the Auditor General noted that UGX114b was released from the Treasury to various beneficiaries in respect of court awards and compensations posing a financial risk. Such government loss of funds compromises economic development and service delivery (Public Accounts Committee of Parliament, 2018). On the other hand, the losses reflect gaps in the ministry, putting to question the instituted risk management measures. Against this background, this article assesses the risk management and its effect on financial performance in the MOFPED. Specifically, the article assesses the risk management process and analyzes its effect on financial performance at the Ministry of Finance Planning and Economic Development.

Literature

Substantive literature exists regarding risk management and financial performance. Notably however, the literature is inconclusive on the implication of risk management to financial performance. Studies by Greene and Trieschmann (2014), Morin (2014); George and Mallery (2010), Deborah (2015) and Kamau (2016) suggest that financial performance dependents on how appropriate risks are identified. For instance, Morin (2014) observes that correct risk identification ensures appropriate risk conception, analysis and communication to mitigate all possible losses towards enhanced financial performance. George and Mallery

(2010) observe that risk conception is a key element of risk identification which bears a significant association with financial performance. A similar position is shared by Matthew (2017) and Kamau (2016) who identifies a positive statistical significant association between risk identification and organizational performance. Notably, it is believed that the ability to identify a risk is the foundation of mitigating it. The other significant aspect of risk identification is communication. This is underscored by Vieira (2012) who suggests that communication through periodical internal audit within an organization bears a positive statistically significant relationship with financial performance. Similarly, Vieira (2012) asserts that regular communication of identified risks strengthens risk management practices in organizations. Therefore, periodical internal audit reports communicate identified risks and keep track of organization's financial performance.

Risk assessment is another aspect of risk management widely underscored by Studies such as Frelon, (2014), Haditia (2012), Parnell et al. (2015), Yilmaz and Flouris (2017) and Jago (2005) regarding its significance to financial performance. The studies underscore risk assessment aspects of risk measurement, planning and decision making which bear positive significance with financial performance. For example, in account of the significance, Frelon, (2014) observes that risk measurement provides the foundation to assess the verdict of risk which facilitates management of risk and fosters financial performance. Haditia (2012) argues that assessment of risks through planning for the undesirable occurrence bears a positive statistically significant relationship with organizations' financial performance. Parnell et al. (2015) also underscores the significance of risk planning and associates it with high chances of managing risk before and after occurrence towards improved financial performance. Yilmaz and Flouris (2017) also claimed that risk assessment evaluates the potential risks involved in a projected activity or undertaking which bears a positive significant association with organizational performance.

The final aspect of risk management underscored by literature is risk control. Studies by Rheal (2011), Kenton (2016), Ludin (2017), Charles (2012), Nocera (2013), Hamburger (2014) and Alexander (2012) identify a positive significant relationship between risk control and organizational performance. Similar findings are reported by Ezekiel (2013) and Hommel & King (2013) who found that the probability of an organization to realize good or bad performance is linked with risk control measures. Furthermore, Charles (2012) highlights that effective risk control measures entail risk assurance practices, treatment and reporting of risk towards enhanced organizational financial performance. Nocera (2013) argues that risk treatment through avoidance bears a positive significant relationship with an organization's financial performance. Hamburger (2014) argues that reduction of risk through risk treatment bear a positive significant association with an organization's financial performance. Alexander (2012) asserts that sharing of risk through holistic treatment mechanisms supports organizational financial performance.

Methodology

The paper draws mainly from findings of an empirical survey conducted on a statistically representative sample of 83 staff employed in the risk management and financial performance function. They include; Middle and Junior Officers in Finance & Administration, Middle and Junior Officers in Internal Audit as well as Middle and Junior Officers in forensic and risk advisory. They were selected using simple random sampling to avoid bias and therefore allow quantitative analysis in order to test the study hypotheses as recommended by Kothari (1990). A triangulation was made with qualitative views of 7 key informants including; Permanent Secretary, The Accounting Officer and Commissioners who oversee the risk management function and financial performance at all levels in the MoFPED. The key informants were selected using purposeful sampling, theoretical sampling and the principle of saturation point was applied as recommended by Maxwell (1992); Patton (1990) and Creswell (2011). Data was collected using questionnaire survey and face-to-face interviews.

Data analysis first obtained descriptive statistics to provide a statistical description of financial performance and the risk management practices. With the latter, interest was to determine respondents' views on financial performance. A description risk management intended to determine the extent to which the risk management process was adequate, rigorous and appropriately implemented. Secondly the final stage of data analysis was a determination of the effect of risk management on financial performance using regression analysis. Specifically, a multiple linear regression model was fitted with financial performance as a dependent variable and risk management the independent variable.

Results and Discussions

Risk management process and practices at the MOFPED

Risk identification was generally reported as the first stage in risk management at the MOFED. It starts with risk conception to analysis of the root causes. The identified risks are shared with stakeholders for further handling. It was observed that the ministry uses specified criteria to identify risks at all levels. The risk conception process is thoroughly done to capture wider perceptions and facts though it is unlikely that all possible risks can be accounted for. Similarly, a root cause analysis was reported to be thoroughly done by undertaking risk cause checks at various levels of the ministry though it was unlikely that the wider operations environment could be taken into account. The identified risks are often shared with stakeholders through channels which provide feedback.

Risk assessment was the second stage in risk management which was reported to involve three stages; risk measurement, risk planning and decision making. Key informant interviews revealed that the ministry's activities and the respective financial provisions are often scrutinized thoroughly. The likelihood of risk occurrence is thoroughly assessed and regular back-up of risk track programs done. Such a risk measurement process was followed by thorough risk planning which involved; allocation of the necessary resources to effectively manage risks and devising a contingency plan to capture risk. Risk planning in the MOFPED was also characterized by regular reviews and plans update to assess the risk magnitude, a process which is guided by a risk track system.

The last stage of risk management involved controlling the identified and assessed risks. To this end, the Ministry was found to have instituted appropriate standards to control risks. Among the control measures included; holding the responsible staff accountable for their actions during implementation of activities and collective making of management decisions and compliance with organizational policies and procedures to protect misuse of financial resources. It is also an institutional culture that management decisions are often carried out with due diligence and objectivity. During risk treatment, appropriate decisions are often taken on whether the residual risk levels are tolerable. In addition, the risk management staff often implement feasible corrective action to manage risk while the management committee often provides oversight to the entire risk treatment process. Risk control was reported to end with risk reporting. At this stage, financial performance reports are often displayed and shared with relevant stakeholders and recommendations on risk management often implemented as desired.

Overall, risk management featured good practices in identification, assessment and control of risks though critical gaps. Extensive interviews with key informants revealed that the risk management process is quite often compromised by challenges of information inadequacy and lack of enough time and technical skills among the staff engaged in risk management. Moreover, risk conception and analysis was considered a complex process necessitating sufficient time and skill to gather and analyze data. To affirm these arguments some respondents had this to say;

I may not believe that the risk analysis process is thorough amidst challenges of inadequate information and skills constraints among staff. Risk analysis is a highly technical area necessitating adequate time and commitment to do comprehensive information search and analysis. I believe this is lacking among our staff and the risk assessment process in our ministry (KII, Oct, 2019).

I believe skill and time is crucial but let’s not forget the issue of staff motivation to undertake risk assessment to desire standards. Basically the challenge in public service is low motivation of the staff and negative mindset to performance because of low pay. The ministry of finance is not exceptional. If you compare a salary for risk analysts in private sector organizations, you will get to appreciate the issue of low salary and motivation of risk management staff in the ministry (KI3, October, 2019).

The above verbatim extract clearly indicates that risk identification is compromised by limited staff time amidst huge workloads as well as technical skills which renders staff unable to adequately gather and analyze information. Besides, staff motivation is low due to low salary payment to risk management staff.

Despite existence of risk monitoring standards, as well as organizational policies and procedures to protect misuse of financial resources, compliance with such remain a challenge mainly due to laxity and weaknesses in the monitoring system. Although responsible persons are often held accountable through sanctions on financial mismanagement, the deterrent mechanisms and consequences of action associated with misuse of funds are weak to deter

actions of misuse which are associated with higher gains than costs. Besides, it is less likely that misuse of funds will be identified. On the other hand, some staff engaged in risk management and financial performance lack public service ethos. They trade off the objectives and benefits of financial management and service delivery for their personal gains. Some respondents share affirmative sentiments;

What sometimes is observed in Auditor General's Reports is a tip of an ice bag. It is likely that many actions of misuse of funds and non-compliance with standards and procedures go un identified due to some laxity and weakness in the funds monitoring system (KI3, October, 2019)

Unethical behavior, like corruption characterize public service. Here in the ministry and other public service organizations, we handle highly capitalized projects which are tempting to the poorly paid staff. Despite existence of risk management procedure policies and standards, compliance is a challenge. The staff opt to run a risk for example to misuse funds for their personal gains well knowing of the cost implications (KI1, Oct, 2019).

Policies, standards and procedures for risk management in my view are necessary but not sufficient to foster financial performance. The critical issue is the negative mindset of those who handle mega projects. They trade-off accountability and service delivery to the citizens for their personal gains. They lack public service ethos and are not patriotic" (KI5, October, 2019).

The above views arguably suggest that though due diligence is often exercised on financial decisions, it sometimes makes oversight to areas where personal gains may accrue at the expense of public accountability. Similarly, intolerable residual risks may be considered tolerable if they are perceived to accrue personal gains to self-interest individuals. Collective management of decisions does not often mean agreeing on how to minimize risks for enhanced financial performance but rather putting heads together to agree on personal shares on project benefits. Misuse of funds will for instance thrive even in the face regular reviews, reporting and sanctioning of non-compliance with risk management studies. In other words, risk control is compromised by lack of public service ethos which breeds corruption, misuse of funds, non-compliance with risk management policies, standards and procedures by self-interest individuals. Consequently, risk assurance, treatment and reporting practices are rendered ineffective to enhancing financial performance.

The significance of risk management to financial performance: Correlation results

Variable	Coefficient	p-value
Risk identification	0.4***	0.001
Risk assessment	0.5***	0.001
Risk control	0.6***	0.001

****Correlation statistic significant at 1% significance level*

Results revealed a significant positive relationship between risk identification and financial performance (r=0.4; p=0.001). Similarly, the effect of risk assessment on financial

performance showed significant results (r=0.5; p=0.001). Regarding the effect of risk control, correlation results also revealed a significant positive relationship (r=6; p=0.001). The statistics indicated that a positive statistically significant relationship existed between risk management and financial performance. In other words, employing good practices in risk identification, assessment and control would significantly enhance financial performance.

The relationship between risk identification and financial performance in the MoFPED is consistent with the findings in previous studies such as George and Mallery (2010), Deborah (2015) and Kamau (2016). The studies characterize a good risk identification process with appropriate risk conception, thorough risk analysis and communication through periodical internal audit reports towards enhanced financial performance. Risk conception provides an empirical understanding and knowledge to examine at an early stage. The fundamental notion at this stage is that the ability to identify a risk is the foundation of mitigating it, thus requires an investigation.

The significance of risk assessment to financial performance is consistent with findings in other studies such as Frelon, (2014), Haditia (2012), Parnell et al. (2015), Yilmaz and Flouris (2017), and Jago (2005). The studies underscore risk assessment aspects of risk measurement, planning and decision making which bear positive significance with financial performance. For example, Yilmaz and Flouris (2017) observed that risk assessment evaluates the potential risks involved in a projected activity or undertaking, which bear a positive significant association with organizational performance.

A significant effect of risk control on financial performance was similarly reported by Raheal (2011), Kenton (2016), Ludin (2017), Charles (2012), Nocera (2013), Hamburger (2014) and Alexander (2012) that established a positive significant relationship between risk control and organizational performance. Similar findings are also reported by Ezekiel (2013) and Hommel & King (2013) who found out that the probability of an organization to realize good or bad performance is linked with risk control measures.

Conclusion

In light of the study objectives, it is observed that risk management bears a positive significant relationship with financial performance. In other words, undertaking risk identification, risk assessment and risk control appropriately would significantly enhance financial performance. However, the study indicates that risk identification; assessment and control are well executed at the MoFPED though with areas for improvement towards enhanced financial performance.

During risk identification, the risk conception process was observed to often not take into account all the possible risks. In addition, the root cause analysis process often did not take into account a wider operations environment. Risk measurement which is a key aspect of the risk assessment faces a critical gap of inability to thoroughly assess risk occurrence and inability to regularly back-up application risk track programs. Risk control is compromised by unethical behavior among some staff who pursue their self-interest at the expense of financial performance and service delivery to the citizens. In addition, there was limited compliance

with standards, policies and procedures for risk management yet the deterrent mechanisms were weak compared to gains from non-compliance and misconduct.

Recommendations

The MOFPED should strengthen the risk identification process by taking into account all the possible risks. In addition, root-cause analysis should take into account a wider operations environment. Risk assessment should be strengthened by ensuring that measurement of risk thoroughly assesses the risk occurrence as well as provide regular back-up of application risk-track programs. Regarding control measures, the MoFPED should strengthen measures to enhance compliance with risk monitoring standards, policies and procedures to address the challenge of laxity and weaknesses in the monitoring system. The Ministry should also strengthen deterrent mechanisms and consequences of actions associated with misuse of funds which were reported to be weak.

Above all, the ministry should explore the possibility of minimizing the workload of staff employed in risk management by employing more staff. Alternatively, the ministry should explore the possibility of motivating the current staff to undertake extra workload in risk management outside the official working schedule. In addition, the ministry should provide staff with specialized training in risk management to boost their skills particularly in risk analysis.

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