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Focus of Risk Management

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Abstract: In the contemporary literature and empirical investigation of risk, a clear distinction between risk that is controllable and risk that is out of the range of control for the individual is missing. This paper proposes the idea of a focus on risk management based on the distinction into risks one can control and risks one cannot control. Making this distinction has become essential in light of the constant bombardment with news on social online media. Overall, risks one cannot control may add a layer of complexity and emotional impact to our lives, which may drain cognitive capacity and confidence in control. An overly focus on uncontrollable risks may create negative emotionality and leave the individual with feelings of helplessness and fear. On the contrary, a clear focus on risks one can control may not only help in navigating through life more efficiently. It may also breed feelings of self-confidence and positive affirmation through control and positive outcomes. The paper discusses intervention strategies to avert a blurred or overly focus on uncontrollable risks as a way to enhance productivity and efficiency but also emotional wellbeing of the individual, the family, social groups and society. The discussion also highlights boundary conditions where focus on uncontrollable risks is needed when it comes to long-term intergenerational care.

Keywords: Control, Costs and Benefits, Emotions, Law & Economics, Risk, Risk Management, Uncertainty

Introduction

Risk management is the "systemic process of identifying, assessing, and mitigating threats or uncertainties" (Gibson, 2023). Risk management usually entails analyzing risk factors and the likelihood of their occurrence and impact. Overall, risk management aims at minimizing harm and monitoring effectiveness of measures (Gibson, 2023).

In risk management, a distinction is made between risk and uncertainty. Risk refers to a situation where outcome probabilities can be estimated. Chances of gains and losses propensities over time become the center of attention in risk management. The estimates are derived from historical data and models that make risk measurable in order to derive inferences how to manage risk. Uncertainty refers to situation where outcome probabilities are not known and unpredictable. Lack of information and trying to estimate the likelihood for uncertainty to be turned into risk estimates with clear probability outcomes lies at the core of risk management.

This paper addresses another dimension of coping with risk. It concerns a locus of control angle in risk and suggests that risk can be divided into controllable and uncontrollable risk. Making the distinction about control of risk upfront before measuring and estimating likelihoods of trajectories and outcomes may save cognitive load and emotional distress of uncertainty and feelings of helplessness. Containing emotions arising from framework conditions one cannot change may grant mental space and cognitive capacity to focus on those things one has the possibility to master. The extra boost in calmness and mental focus is thereby meant to allow for better decision making and choice patterns.

This article is structured as follows: First, risk and risk management will be covered. Second, the idea of a locus of control in risk assessment will be introduced. Third, three examples will be given how risk may become the focal point of analysis. Forth, the discussion covers the advantages of a distinction of risk into controllable and uncontrollable

risks in order to then also show boundary conditions what aspects should still be considered even if the primary focus is set on controllable risk.

Risk management

Risk management draws from business studies and organizational decision-making theory. The aim of risk management is to control risks that impact human life. Minimizing risks improves people's lives by less harm and destruction to their daily activities. Fundamental principles of risk management include processes of risk identification, assessment and quantification of potential harm, risk mitigation and constant monitoring for adjustment needs to emerging risks. Risk management benefits from a structured approach to enhance organizational resilience and regulatory compliance. Risk mitigation techniques are relevant for all facets of human life.

For risk assessment the identification of potential changes and estimated outcomes is essential for ensuring resilience and strategic goals (Aven, 2015). Risks are thereby assessed in terms of their likelihood and potential impact. In the systematic evaluation of risk, cognitive complex decision making is tainted with emotional facets, such as joy in mastery but also fear of failure, for instance. Scientific accounts of risk assessment combine quantitative methods – such as probability analysis – with qualitative accounts of expert judgement but also emotional impact analyses (Kaplan & Garrick, 1981). Identifying likelihood and impact of risk but also the prioritization and organization of risk mitigation strategies is a cognitive and emotional task.

Identifying risks requires comprehensive understanding of the environment and personal capabilities to change the environment or adapt (ISO, 2018). While there is a long history in risk management theory and practice with multiple techniques – such as brainstorming, interviews, scenario analysis but also microeconomic decision making as well as macroeconomic modelling – we lack a distinction between risks that one can control and risks one cannot control. Making this distinction would allow cognitive energy and decision-making capacities as well as help conserve and bundle resources for those risk variances one can change.

Risk mitigation entails strategies to manage risks which entails, for instance, risk avoidance, reduction, transfer and acceptance (Hillson, 2009). Controls and contingency plans as well as resilience strategies or risk transfers via insurance are potential ways to mitigate and adapt to risk.

Risk monitoring allows for constant adaptation based on risk levels and changing conditions. It includes proactive and timely cognitive processes of reviewing the environment and adjusting to changed conditions (Aven, 2015).

Locus of control in risk management

The locus of control theory originated from Julian B. Rotter in 1954. This psychological concept describes how individuals perceive control over outcomes of their actions over their lives. There is an internal locus of control, in which individuals tend to believe that they are the masters of their own actions and outcomes. The internal locus of control is contrasted by the external locus of control, by which individuals attribute outcomes as a function of external forces, such as luck, fate and actions of others. Control theory inspired psychology and decision sciences by examining people's motivation based on their locus of control propensities.

Interestingly, the locus of control theory has not been applied in risk management in the sense to distinguish between risk that people can have under control by their own actions (internal locus of control risk) and risk that they cannot control (external locus of control risk). In the case of internal locus of control innovatively applied on risk management, people focus on risk they can control, while abandoning major consideration and emotional engagement with risk they have no control over. This strategy is arguably meant to enhance efficiency but also emotional wellbeing. All these beliefs significantly impact on how

individuals approach challenges, make decisions, and interpret their environments. The locus of control has since become a cornerstone of psychological research, with broad applications in various fields, particularly in the decision sciences.

Unlike Rotter's (1954) assumption that people differ in their propensity to either have an internal or external locus of control which determines their beliefs about whether they can change the course of actions (internal control) or are dependent on external forces (external control); the idea of the internal or external risk focus advocates for a situation change of focus on internal risk that can be controlled and disengagement and abandonment of external risk that cannot be controlled. This newly-proposed angle of risk management allows shaping human behavior towards risk control while abandoning negative consequences of insurmountable external risks. While the original locus of control theory was used to understand motivation, decision making and coping strategies, the application of locus of risk control allows for bundling self-efficacy, persistence and achievement by focusing on internal locus of risk control (Rotter 1966), while reducing stress and helplessness moments by zoning out those external locus of risk control moments that are completely out of control for the individual.

Initial research on the locus of control showed that internal locus leads to higher self-esteem, motivation and goal achievement (Spector, 1988). Internal locus of control is more likely to be associated with proactive behavior and responsibility for decisions (Spector, 1988). External locus of control is more aligned with passive behavior, less goal orientation and more inclined to failures to external factors (Lefcourt, 1982). Applying these insights to risk management, one could extrapolate that primary focus on internal locus of risk control may drive people to more and better targeted action, while neglecting focus on external locus of risk control may help decrease emotional moments of helplessness, lethargy and depression due to a no-way-out perception.

One of the most significant applications of the locus of control theory is its impact on decision-making. Individuals with an internal locus of control are more likely to engage in active decision-making processes, where they consider alternatives, anticipate consequences, and take responsibility for their choices. Conversely, individuals with an external locus of control may defer decision-making to external agents, such as authority figures, or may make decisions based on chance or external guidance, believing they have limited control over the outcome (Buchanan & Seligman, 2007).

Locus of control also influences how individuals assess risk and uncertainty. Research in decision sciences has found that those with an internal locus of control tend to be more confident in their ability to handle uncertainty and are more likely to take calculated risks (Stewart et al., 2003). On the other hand, individuals with an external locus of control may avoid risky decisions or become overly cautious, as they believe that external forces rather than their actions determine the outcome (Vroom, 1964).

Moreover, the locus of control plays a significant role in how individuals process information. Internally-oriented individuals are more likely to seek information actively and to engage in critical thinking when making decisions, whereas those with an external locus of control may rely more on external cues, such as advice from others or societal norms, when faced with uncertainty (Phares, 1976).

In organizational settings, employees with an internal locus of control are more likely to demonstrate higher levels of job satisfaction, commitment, and performance. These individuals believe their actions and decisions contribute significantly to organizational outcomes and are more motivated to work toward organizational goals (Judge et al., 2001). Conversely, employees with an external locus of control may feel less empowered, exhibit lower job satisfaction, and experience greater levels of stress due to their perception that outcomes are largely influenced by external forces such as management decisions or workplace conditions (Spector, 1988).

Taken together and applied on risk control, if focusing on internal risk locus of control targeting those risks one can influence may lead to action and self-motivated reduction of risk while reducing all the cognitive load and negative emotions uncontrollable situations arise.

Cases

When finding cases to describe the internal and external locus of risk control, one case concerns social online media infiltrating users with negative content that aggravates but cannot be changed directly. For instance, the social online media platform X, formerly known as Twitter, is believed to increase negative emotions by featuring dissenting views than one's own in order to engage users into active discussion. Further, TikTok has been said to use emotionally disturbing videos in order to keep users longer on the platform. Now applying a focus on internal locus of risk control, one could argue to control consumption of social online media platforms – e.g., via regulation for age or self-restraint – in order to not be infiltrated with information one cannot control – e.g., videos about war abroad or historical facts that cannot be changed anymore.

Another case of using the internal locus of risk control logic while shrinking attention to external locus of risk control concerns time dimensions. Past experiences that cannot be changed anymore should thereby be viewed as external locus of risk control, while near future events should be seen as internal locus of risk control, on which one should focus their energy. This underlines the present bias that states that the now is most of the time considered as the most important focus. Too far away loci, like in the next generation, can only slightly be changed or put on a right trajectory, which explains oftentimes the lethargy on long-term risks, such as climate change.

Another way to dissect the internal locus of risk control is to integrate various contexts and derive general inferences. For instance, domains like food and drug intake are internal risk locus of control, while natural disasters and weather conditions are external locus of risk control domains. Assigning diversification strategies (e.g., packing sunscreen and an umbrella when one does not know how the weather will be like) but also finding pieces of influence on external locus of risk control decisions (such as personal financial allocation decisions if there is a trade war in two countries one cannot change) in the otherwise non-changeable context are thereby found as creative coping strategies with a complex world (Wallston et al., 1983).

Discussion

Risk management is a way to improve lives by foresighted estimation of risk and mitigation of anticipated risk. Risk management is applied in many domains and industries across a wide range of sectors. Risk management is a forward-looking anticipation of events and a backwards-looking learning to cope with life in the future. Risk management heightens personal resilience and crisis management in organizations and society. Risk management is an integral part of human living, ensuring that potential threats are identified, assessed, and mitigated effectively. A structured approach to risk management enhances an organization's ability to navigate uncertainty and safeguard its resources.

Contemporary developments in risk management enhance data analytics, artificial intelligence, and machine learning techniques to predict and manage complex risks in real time. As risks continue to evolve, especially with the increasing influence of technology and global challenges, organizations must adopt flexible and proactive risk management strategies to stay resilient in a changing environment. By embracing innovative tools and continuously refining risk management practices, organizations can mitigate adverse events and continue to thrive.

The locus of control theory offers valuable insights into human behavior and decision-making. By distinguishing between internal and external locus of control, the theory provides a framework for understanding individual differences in motivation, risk-taking, and coping

strategies. In educational, health, and organizational settings, fostering an internal locus of control can lead to better outcomes by enhancing personal responsibility, goal-setting, and proactive behavior. Future research should continue to explore the dynamic relationship between locus of control, decision-making, and individual behavior, with a focus on how to intervene effectively in various contexts to improve decision outcomes.

Risk management enhanced for locus of control aspects was introduced in the idea of a locus of internal or external risk control. To focus on internal locus of risk control onto those aspects of life one can influence was proposed as a way to boost efficiency but also to maintain a healthy emotional state. While some risk is inevitable, the ability to identify and mitigate parts of it and ignore those aspects that cannot be influenced is vital to improve risk management and benefit personal as well as corporate and societal causes.

Future research should address boundary conditions of the efficiency to focus away from far-distant external risks that are not changeable. For instance, the risk of climate change to future generations may appear far away and inevitable – yet the solution to a trajectory that holds the climate at least constant is set in the current generation. These intergenerational responsibility demands underline the importance of also integrating future conditions and fairness notions in the proposed risk control framework.

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