Firms’ Activity Risk under a Knowledge Economy

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Abstract—Processes of growing uncertainty and risks in economics are analyzed against a broad background of the “civilizational shift” and globalization. The rapid ageing of equipment, technologies and knowledge leads to numeric growth of bankruptcies and the intensification of their destructive effects. Their mitigation would be possible if an institutional system of threat monitoring and prevention were created.

In order to identify in good time the symptoms of a nearing bankruptcy and, based on them, to take corporate restructuring decisions, it is necessary to have reliable information about the enterprise and its environment. Monitoring and early identification of threats are preconditions for successful economic decision making. It is important that one have the ability to recognize enterprises’ response to changes in economic policy and the institutional and legal environment.

Early warning models, along with synthetic estimates of enterprises’ current operations and risks (such as credit and risk ratings developed by the Basle Committee on Banking Supervision – Basle II Agreement), are becoming an important element of the systems, as well as a tool, to assess the state of enterprises.

Under a new development paradigm and globalization challenges, the synchronization of micro- and macroeconomic policies is becoming a condition of development of entrepreneurship and stabilization of enterprises’ standing. Besides, a corresponding institutional business infrastructure, including that of bankruptcy, is required for enterprises’ correct functioning and growth.

Civilization shift. Consequences for enterprises. Enterprises, as economic agents, often fall «victims» (objects) of the current civilization shift, that is, a shift in the world’s development paradigm. The change dynamics is so dramatic that Toffler’s Third Wave, albeit quite recent, is perceived as a thing of the past. In the contemporary world, the decisive role is played by high technologies, science, and information, which are creating a new economy, based on knowledge, or more exactly, on intellectual potential. This generates such an enormous productivity potential that the most developed societies are in a position to change to the model of development a «leisure and entertainment society», corresponding to the character of the Sixth Wave, now embracing only the more privileged societies. The extant economic models—education, employment, consumption, family, etc.—are quickly losing their topicality. And as it always happens in a watershed, questions arise to which no answers are available. The history of economics itself shows how difficult it is to avoid erroneous decisions and assessments under such conditions. Thus, in the past, not even new paradigms, but, simply, new inventions (especially, in early stages) stimulated growth of social and economic tension and even provoked deep crises. Under the «post-modernist condition» — a specific socioeconomic state of the postindustrial society—the increasingly more complex technology is becoming increasingly important. Weak points of contemporary economics and threats to the global economic system manifest themselves with full power.

1 Based on a report at the 15th Scientific Conference of the Joint Commission of PAS and RAS Economists “Competitive Capacity Factors of Poland’s and Russia’s Economies,” Warsaw, June 20–21, 2005.

2 «The Third Wave» is the title of a book by the well-known American sociologist A. Toffler, which depicts a future society in which thanks to industrial automation consumption and services are greatly increased and ideologies and parties have disappeared.
is appropriate to recall here the warnings of U. Beck, an outstanding German sociologist: «Under the advanced modernity, the public production of wealth keeps pace with the public production of risk... We are witnessing—as subjects and objects—the formation of a crevasse in the sphere of modernity, which is now freeing itself from the bounds of the classical industrial society and taking a new shape, that of “a risk society”» [1, p. 27]. In this situation, threats are becoming an almost day-to-day occurrence: «Quasi-revolutionary situations are, seemingly, written into the unrestrained advance of civilization, they emerge as “civilization destiny”, conditioned by modernization, which contains in itself a permit for a catastrophe under the guise of normalcy.» [1, p. 16]. So, a risk society is something greater – a disaster society. It contains the danger that exclusive situations will become a norm. P. Drucker states quite dramatically that «planning does not work» [2, p.476]. Deviations are becoming the norm.

Under the new development paradigm (knowledge civilization), forms of ownership are subject to change; it is no longer the ownership of means of production which is of decisive importance, as in classical capitalism, but the ownership of intellectual capital. Therefore, the key category is going to be «access to knowledge and information, while the opposite is exclusion.» If intellectual capital is becoming the main source of strategic competitive advantage, persons (legal and natural) lacking it are doomed to exclusion, that is, bankruptcy.

Enterprises’ adaptation to the demands of a competitive environment is a derivative of the growing market tension. As Szimanski emphasizes in his preface to the book [3, p. 23]), under globalization, at least four out of the five competing forces manifest marked growth:

—the buyers’ force, emphasized by the richness of the market offer (which is strongly influenced by the growth of the Internet and its associated e-business);
— the competitive force connected with substitutes;
— the competitive force connected market entry opportunities, accompanied by the free movement of capital and deregulation, which result in a rapid decrease of market entry costs; and
— the force of competitors in particular markets.

What matters is not just the numeric growth of competing entities but also the development of transnational corporations, the firms ranking effectiveness as their top priority and backing it, as needed, by the force of money (“a fat wallet”).

The fifth force, i.e., suppliers, has a mixed impact. It is being weakened by the growing demand barrier, as well as by the Internetization and informatization, to the benefit of buyers, whose awareness of products, costs, and prices is increased.

The interplay of these forces determines the prospects of an enterprise’s survival on the market or exclusion from it, that is, bankruptcy. In a market economy, bankruptcies perform the selection function in business. They have been known, at least, since the industrial revolution times. But, if in the beginning, the effects of bankruptcies were local, now, as the globalization processes are gaining momentum, they manifest themselves more frequently in the so-called domino effect (bankruptcy chain). The closer and more diverse a nonsolvent enterprise’s links with other national and foreign partners, the faster the bankruptcy virus spreads. Globalization acts as a multiplier of bankruptcy diffusion. That bankruptcies are on the rise worldwide (both in absolute and relative figures) is not a coincidence, which is verified by statisticians (including European ones); for several years now, they have made annual comments on repeated record waves of bankruptcies. Bankruptcies are showing a marked upward trend, though the year 2004 proved to be more favorable than before for some countries, e.g., Poland.

Rapid changes increase the risk of bankruptcy. This is true of all economies, including developed ones. In Europe, for example, some enterprises operating in Germany are exposed to bankruptcy (Table 1).

A high bankruptcy dynamics was also observed in Poland, especially in 2000–2003 (Figure)³.

In Poland, even companies listed at the Warsaw stock exchange are exposed to bankruptcy, its membership requires meeting a definite performance standard. And though in 2004, due to faster growth of GDP, 5.3%, against 3.8% in 2003, the number of bankruptcies decreased, but considering GDP forecasts, it should grow again in the future. (According to forecasts by the National Bank of Poland and the European Commission, economic growth in Poland will slow down to 4.4% GDP in 2005, and will be 4.5% GDP in 2006.) Bankruptcies are manifestations of growing business risks, associated, in turn, with sudden civilization changes, including technologi-

³ 2003 data are extrapolated data from the first six months of 2003.