

UNFOLDING ORGANIZATIONAL RISK AND COST ASSOCIATION FROM STAKEHOLDERS PERSPECTIVE: EVIDENCE FROM ASIAN EMERGING MARKETS

Asad Khan, PhD Scholar, IBSLeadership, Abdul Wali Khan University Mardan, Pakistan. Email: asadkhan@uoh.edu.pk

Muhammad Ibrahim Khan, IBSLeadership, Abdul Wali Khan University Mardan, Pakistan. Email: ibrahimkhan@awkum.edu.pk

Shehzad Khan, IBSLeadership, Abdul Wali Khan University Mardan, Pakistan. Email: shehzadkhan@awkum.edu.pk

Zia-ur-Rehman, Assistant Professor, The University of Haripur, Pakistan. Email: zia.rehman@uoh.edu.pk

Abstract. *In this study we extend the conventional risk-return debate to a more intriguing and practically significant conundrum of risk-cost association. The analysis is performed on large sample of 4609 listed companies operating in nine Asian emerging markets, using 2SLS estimation. We established that risk act as a specter and have consequences for long term contractual relationship between key stakeholders and organization. Further, organizational costs are directly affected by organizational risks hence it also provides an immediate opportunity to management to take corrective measures. As whole, the empirical evidence provides an essential perspective and insight to understand the nature of organizational risk, slack, stakeholders and it implication for organizational costs in Asian emerging markets.*

Received 17 April 2021
Accepted 21 May 2021

Keywords: Words: Risk, Organizational Cost, Firm-Specific Risk, Market Risk, Emerging Markets

Introduction

The recent economic turmoil has a huge financial impact on business operations and tactical approaches to manage risk. Hence, key attention is given to the importance of risk and its financial implications. However, despite enhanced management vigilance, the nature of risk is still unpredictable and remains a key concern for stakeholders involved across the various strategic initiatives and business activities. These strategic endeavors may be in shape of diversification strategy to reduce risk, R&D expenditure (Jirasek, 2017) to attain competitive advantage or the extension of firm geographic scope (Bettinazzi & Zollo, 2017) to expand it market share, all requires prudent risk-

return analysis. Previously such issues are investigated under the umbrella of risk-return trade off in financial economics as well as strategy literature (Santacruz, 2020). Furthermore, the domain of financial risk management is responsible to identify various types of risk faced by the organization, pinpointing the sources of those risks, assessing the effectiveness of available tools and techniques to hedge those risks and most importantly what is its performance related implications (Bromiley, McShane, Nair, & Rustambekov, 2015). However, one missing aspect of all those researches and strategies designed for organizational growth and stability across various branches of business management is the organizational cost, associated with those initiatives (Bromiley & Washburn, 2011). Organizational costs have unique characteristics that differentiate it from other performance measures. First, organizational costs directly consolidate and elaborate the financial impact and cautions arising from various key stakeholders due to increasing organizational risk (Miller, 2009). Second, it also provides organizational management an opportunity to take immediate corrective measures in case any market uncertainties. Third, it is also vividly observed that, one of the basic reasons of organizational stagnation and even failure is either high cost or inappropriate expenses to attain organizations strategic objectives (Liu, Liu, & Reid, 2019). Even though, if such organizations do make substantial sales but their profits margins are substantially slash down due to high cost of doing business. Another important dimension of organizations low profits and high costs is their relationship with multiple stakeholders. Such as financial lender, retailers, wholesalers, distributor, customers' and even equity holders have key interest in organizational risk and response to various market uncertainties. Due to undiversifiable nature of their risks, these stakeholders take immediate corrections in their contractual terms, if they observe unusual patterns of organizational risk. Consequently, these stakeholders take much more precaution, time delays in their payments and conservative approach to fulfill their obligations. Thus, it requires much more effort and costs to induce these stakeholders, to maintain their current and future relationship with high risk organizations (Bettinazzi & Zollo, 2017). All those aspects of organization need some thoughtful consideration. However, very little attention is given to the association or the impact of the organizational risk on its costs from stakeholder's point of view (Jones, Harrison, & Felps, 2018).

The direct implication of organizational risk on cost was first tested by Miller and Chen (2003) using sample of US companies. We extended this argument to the organizations operating in Asian emerging markets as a primary objective of this study. To analyze this important proposition, we assert that lower market risk and business risk offer organizations a superior negotiating platform and confidence to settle its terms effectively and

efficiently with diverse stockholders. We also argue that organizational costs bears the immediate and initial financial impact from key stakeholders (Miller, 2009). That negative financial impact subsequently emerges as either losses or decrease in profits. So the financial impact of those diverse stakeholders is noteworthy (Freeman, 2010). Previous studies have also emphasized the impact of effective stakeholder's management on firm performance (Harrison & Freeman, 1999). Studies such Wood Donna (1995) reported positive impact of stakeholders on firm value by building trustworthy relationships in the shape of contracts. His study explains that organization's contracts with different stakeholders are based on ethical principles such as, trusting your partners, cooperative approach in difficult times and avoiding opportunistic relationships offer a unique competitive advantage in marketplace. Similar, conclusion is drawn by Hillman and Keim (2001) whom argue that firm's key stakeholders such as human resources, suppliers, distributors and associated societies increases organizational value by developing long term relationship in the shape of intangible assets. Recent studies such as Patatoukas (2012) and authors like Irvine, Park, and Yıldızhan (2016) highlights the importance of customer base as an important stakeholder. Their findings established that, effective supplier-customer relationship can improve firm operating performance as well as stocks return. However, they also argue that, those relationships are time bound and require consistent risk management approach to take effect. Although, these studies help to establish the importance of stakeholders, but there direct association with organizational risk is a major missing link. To fulfill that void, is a primary objective of this study.

Second, there is a general consensus that risk management adds value to the wealth of shareholders (Bromiley et al., 2015; Kallenberg, 2007; Smithson & Simkins, 2005). However, it is also argued in academia that excessive risk management diminishes profits and adds regular costs to firm operations (Amaya, Gauthier, & Léautier, 2015; Berghöfer & Lucey, 2014). To address these contradictory claims, the proponents of behavioral theory (Cyert & March, 1963) suggest that, slack play a significant role in managing various uncertainties. Hence, we also introduce the moderating effect of slack to our organizational risk and cost association. Slack is an additional resource which is utilized as response to market change, thus shields organizational returns from various uncertainties. However, there is a clear disagreement between the followers of agency theory and behavioral theory on utility of slack (Daniel, Lohrke, Fornaciari, & Turner Jr, 2004). That is why as a second objective of this study, we empirically investigated this gap for the companies operating in Asian emerging markets. As whole this paper will facilitate the improvement of existing literature in a multiple way. First, it adds another dimension to

understand the nature of risk from stakeholder's perspective. Second, there is very limited empirical evidence on the subject matter in Asian emerging markets (Li, Griffin, Yue, & Zhao, 2013). Third, we address the previously identified endogeneity problem in empirical models by setting up 2SLS as estimation technique (Andersen, 2009; Henkel, 2009; Oviatt & Bauerschmidt, 1991). Fourth, previously reported concern on using standard deviation and variance of companies return as proxies of risk is also managed by using market based proxies (Henkel, 2009; Ruefli, 1990). Fifth, the separation of business risk and market risk as separate proxies identify its distinctive effect on organizational costs. Sixth, this study also addresses the misconception of business risk diversification. Seventh, by using the same sample with actively operating firms throughout our analysis we also managed the survivorship concerns in this research (Chou, Chou, & Ko, 2009). Finally, the results of this study will guide the organizational management to make an informed decisions based on specific and insightful understanding of organizational risk, stakeholders and its implications for organizational costs.

2.0 Theory and Hypotheses

2.1 The concept of risk

Since the classical definition of risk concepts of risk remain a corner stone of management theories and financial research (Andersen & Bettis, 2015; Bromiley et al., 2015). However, researchers often disagree on meaning, measurement, the context of risk being assessed and who it is strategized by different stakeholders across the businesses. That's why there is an extensive academic debate based on the definition of risk (McGoun, 1995) and most importantly the nature of risk-return relationship. The followers of financial-economics theory suggest positive risk return relationship (Winn, 1977). A contrary opinion is founded on seminal work that put forward negative risk-return relationship (Bowman, 1982). Further, the nature and analysis of risk, is also different across the fields of financial economics and corporate strategy (Bromiley et al., 2001). The follower of financial-economics sees risk-return relationship from the prism of efficient markets. Whereas, the researchers in domain of corporate strategy consider organizational risk as an intrinsic phenomenon, reliant upon organizational level strategies and resources closely allied with diverse stakeholders. Further, those firm level strategies and resources are very much firm specific, thus information and access to it is almost nonexistent. Nevertheless, a careful analysis is required to ascertain the impact of various stakeholders on classical risk-return relationship.

The rational for controlling risk is multifold and hold complete academic consensus (Bromiley, Rau, & Zhang, 2017). But different parts of financial risk remain the area on interest for many decades. In this context, the Capital Assets

Pricing Model (Estrada, 2011) break up organization's financial risk into market risk and unsystematic risk. The market risk is affected by changes in macroeconomic conditions, uncontrollable market forces and natural disasters (Fama & French, 1993). On the other hand, the unsystematic risk popularly known as business or firm-specific risk represents the uncertainty in a organization's internal factors (Bharadwaj, Tuli, & Bonfrer, 2011). These internal factors may include decline in sales, employee frauds and theft, financial mismanagement, dwindling customer base, mismanaging research and development or even the decline in key products (Bansal & Clelland, 2004; Low, 2009). However, both market and business risk play a significant role while establishing and extending relationships with various stakeholders (Bromiley et al., 2017).

The cash flow motive highlighted by Amit and Wernerfelt (1990) illustrated two very important aspects of the organization, which are directly affected by its risk. These are organization's operational efficiency and associated stakeholders. The operational inefficiency of the organization can lead to higher inventory cost, destabilize sales, instigate financial constraints and various cost adjustments which directly affect the competitiveness of the organizations (Sanchez, 1995). Similarly the majority of the organization's stakeholders such as supplier, distributors, retailers and buyers etc. are risk averse (Miller & Chen, 2003). This phenomenon becomes more evident in emerging economies. Owing to the narrow market dynamics of emerging markets, different players such as manufacturers and distributors are heavily reliant on a small number of business partners (Khanna & Palepu, 2006). As a result, businesses with a high risk profile exposes its suppliers, distributors and retailers to greater industry risks, such as fluctuations in demand, volatility in supply, as well as costs associated with all out bankruptcy (Khanna & Palepu, 2006; Miller & Chen, 2003). Consequently those market dynamics compel the suppliers, distributors and retailer to commit to higher contracting and transactional agreement (Aybar & Thirunavukkarasu, 2005). Furthermore, high risk is also cautiously analyzed by financial lenders, whether they are creditors or equity investors. Similar finding is documented by El Ghouli, Guedhami, Ni, Pittman, and Saadi (2013) that lower risk corresponds to smaller risk premium. Therefore, organizations can improve their value by insuring lower cost of capital. Moreover, the empirical finding of Lubatkin and Chatterjee (1994) also holds that business risk do effect the cost of capital and hence the value of the organizations. Therefore, to disentangle and analyze a precise impact of financial risk on organizations cost, we consider both market and business risk and how it effect the organization's cost structure in emerging markets.

2.1 Organizational Cost

The importance of organizational cost is not anonymous to managers and researchers. Nevertheless, its true implication to organizations and its stakeholders is still a puzzle. According to Coad and Cullen (2006) the management of organizational cost is as significant as other aspect of business management. According to Reider (2004) organization's cost management have direct value adding potential as compared to boosting sales, which may or may not add to the organization's value. He argues that effective cost management have direct positive effect on profit margins, hence results in "dollar for dollar" contribution. Thus the value adding potential of organization's effective cost management is quite significant as compared to other strategic options, i.e. R&D, innovation, merger and acquisitions (Reider, 2008). Although there is a realization that cost is a significant aspect of business operations, but it is always analyzed as consequence of sales. Hence, its due importance is somehow never realized to its potential. Therefore, a large numbers of researchers consider that, organization's cost is directly associated with sales (Cooper & Kaplan, 1992). If we believe this point of view, then, organization's management must be least worried about organization's cost, as it will strictly follow the sales pattern. Contrary to the above arguments, there is another school of thought, who believe that organization's cost is "sticky" in nature and thus increase and decrease in sales is not perfectly correlated with organization's cost Anderson, Banker, Huang, and Janakiraman (2007). According to that strand, downward trend in sales is not followed by the organization's cost, as in the case of increase in sales. Thus, leaving huge unwanted and uncontrollable expenses at the time of downturn and low sales. This particular situation has further aggravated managerial inability to cut down organizational expenditures and fear of higher substitution cost if future sales are recovered (Hsu & Jang, 2008). Thus, managerial indecisiveness often leave organizations with huge cost with expectation of better opportunities in future. Further, the potential negative effects of organizations sticky cost further increase if there is high variation in firm sales, which is often considered as an organizational business risk.

To address the sticky nature of organization cost the efficient companies always strive to develop capabilities and processes to effectively manage those costs. This requires firm flexibility and most importantly managerial skills to maneuver its cost structure to utilize market opportunities and at the same time avoid market uncertainties. Having said that, still the effective management of organization's cost is not an easy task. In fact, the costs of the firms are spread across multiple layer and activities, which have different implications for different stakeholders. For example, increase in expenses on training and development of employees may be a good strategy for future growth and

competitiveness. But at the same time, it may dry up liquid financial resources for both equity and debt financiers. Similarly, developing new assembly lines on modern technology may result in decrease of operating expenses associated with assembly line worker but at the same time it also exposes organization to high technological, operational and market risk. Furthermore, organizational costs take many shape and categories depending upon the nature of business. Similarly, the managerial objectives are also considered as a significant factor in classification of organization's cost. For instance, organizational cost can be classified as manufacturing versus nonmanufacturing costs, direct versus indirect costs, fixed versus variable costs and financial verses non-financial expenses. All those categories serve some specific purposes and relate to specific types of business operations. The manufacturing cost incorporate firm expense such as direct material cost, direct labor cost and manufacturing overhead which integrate all indirect costs. Whereas, the nonmanufacturing cost include different operational costs, such as operating expenses, administrative overheads, selling, advertising and management cost. Similarly, if management is interested in product costing, pricing, product evaluation and traceability of a cost to it. Target product/service, department or business unit then they may opt for direct and indirect categorization of cost. The direct cost incorporates all those expenses related to direct material and labor cost, selling and marketing expense related to a specific product/service or a segment of a business. The firm expense such as IT, legal, administrative overheads and other shared cost are grouped under indirect cost. The organization may opt for fixed and variable cost, if the purpose is to gauge the extent of variation in organization's cost with changes in scale of operations and activities.

All those categories and subcategories correspond to different stakeholders of the firms. Such as suppliers, retailers, distributors, employees, financiers, regulators, legislators and communities. All have specific association with the firms' operations and future expectations (Liu et al., 2019). Similarly they all have the ability to shape the firms future course of action, especially in uncertain conditions (Crilly & Sloan, 2012). Therefore, variation in cost structure can influence the organization's performance by directly effecting the future growth and risks (Bromiley & Washburn, 2011). Consequently, different stakeholders can adjust their term according to the organization's risk profile. This result further increase in organizational cost, especially those firms which have high risks or lower growth potential, thus expose its stakeholders to range of risks (Dekker, Sakaguchi, & Kawai, 2013). To sum up the above discussion, it is vividly apparent that risks affect the performance and diverse stakeholders play a significant role in organization value creation. But it is not clear that, how the market risk and business risk affect the stakeholders' perception about

the future prospects and contractual relationships. Alternatively, we can say that organization risks will affect the organization costs. Therefore, to better evaluate the effectiveness of cost at different stages of the business, we segregated organization's cost across two very significant components i.e. manufacturing cost and operational cost. Both categories integrate the associations among some of the most key partners and stakeholders involved with the business of the organization (Miller & Chen, 2003).

As discussed earlier, the manufacturing cost of include the overheads related to various stakeholders such as suppliers of raw material, labor used to manufacture goods or provide services, salaries of administrators and managers overseeing manufacturing, distributors, shipping costs, warehousing, facilities, equipment, and other overhead costs. The nature of all those stakeholders is extremely sensitive to the organization's risk. Therefore, these stakeholders will shape their contractual relationship based on organization's risk. This phenomenon is more crucial in emerging economies which are mostly categorized by unstructured nationwide distribution channels and instable market condition. Thus, we hypothesize that.

H1: The business risk significantly increases manufacturing cost.

H2: The market risk significantly increases manufacturing cost.

The second category is operational cost. The operational cost sums up the cost related to some of the most important stakeholders of the organization. Such as the salaries and benefits of managerial and executive staff, advertising and marketing expenses, commission on products and sales, insurance, consulting and legal fees, overhead expenses to run the offices, warehouse, factories, and other in-house facilities. Although, adjustments in operational cost is easy compared to manufacturing costs. But, the nature of operational cost is very tricky. It is directly associated with revenue generating activities of the organization (Cooper & Kaplan, 1992). For instance, the expenses related to sales and advertising are directly associated with increase in organizational sales. Further, the salaries, parks and privileges are directly linked with employees competence and motivation (Edwards, Ram, & Smith, 2008), technological and process improvement correspond to efficiency and risk management (Hammer, 2015). Therefore, we hypothesize that.

H3: The business risk significantly increases operational cost.

H4: The market risk significantly increases operational cost.

2.2 Moderating effect of Slack

Slack is an additional organizational resource which is utilized as response to market change. A number of researches has been conducted on nature and implication of slack in organizational structure since Cyert and March (1963) explanation of slack as organizational shield against risk. However, there is a

clear disagreement between the supporters of behavioral theory and agency theory (Daniel et al., 2004). The followers (e.g., Lee & Wu, 2016) of behavioral theory argue positive impact of slack on organizational performance. They asserted that organizations under uncertainty absorb the slack to cut down the impact of harmful events. According to Kim, Cho, and Khieu (2014) slack is the most rapidly on hand resource for management to capitalize on market opportunities. Whereas, agency theory cohorts (Jensen, 1986) suggests to insure some additional cautions in that relationship, otherwise it will lead to inefficiency and self-serving behavior of the employees. Similar result are reported by Nohria and Gulati (1996) and Lee and Wu (2016), they hold that slack effects the organizational discipline thus lead to an upturned U-shaped relationship with firm performance. Furthermore, some empirical evidence suggests that slack motivate organizational innovation (Marlin & Geiger, 2015) and instigate managerial risk taking behavior. All these specific concerns have its significance, but organizational risk is totally different preposition. Firm risk management strategies and hedging techniques provide mechanism against know risks (Meulbroek, 2002). However, uncontrollable market risk and some business specific risk are hard to predict. Therefore, it requires spared organizational resource to control the negative effects of those risks (Sax & Andersen, 2019). Therefore, we propose that;

- H5: Slack shields the manufacturing cost from increasing business risk.
- H6: Slack shields the manufacturing cost from increasing market risk.
- H7: Slack shields the operational cost from increasing business risk.
- H8: Slack shields the operational cost from increasing market risk.

Figure 1 illustrates the hypothesized relationship of impact of organizational risk and cost association and the moderating role of slack.

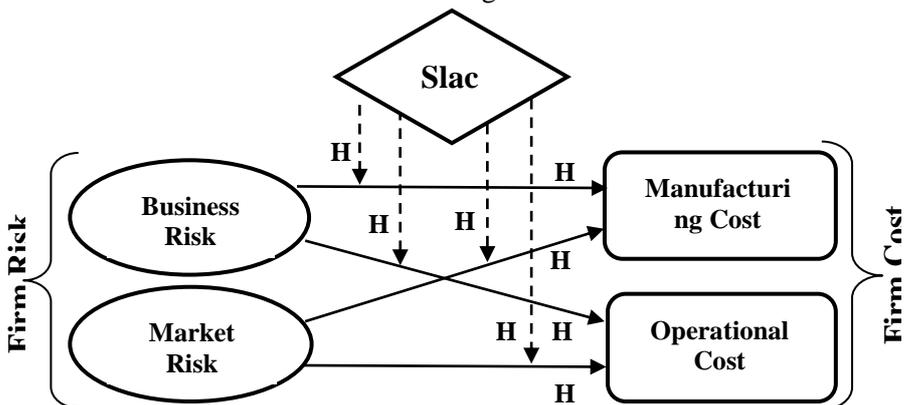


Figure 1 Schematic Diagram

3.0 Methodology

To examine the main propositions this study, we employed cross sectional data modeling technique using nonfinancial organizations listed on Asian emerging markets. The data is obtained from DataStream for a period of 5 years form 2013-2017. For analysis we employed 2SLS estimation, to manage the issues of endogeneity in our models. Further, we excluded all those organizations with missing data, non-consistent and extreme values. The final sample used for analysis constitutes 4609 publicly listed organizations across nine Asian emerging countries, which are China, India, Indonesia, Malaysia, South Korea, Taiwan, Pakistan, Thailand and Philippine.

3.1 Variables

The main criterion variable of our study is organization cost. We divided organization cost in two sets, which is manufacturing cost and operational cost. Following the proxies defined by Miller and Chen (2003) we measured the manufacturing cost (MC) as cost of goods sold over annual sales. Similarly, operational cost (OC) is measured by selling general and administrative expense divided sales. Financial risk as explanatory variable is also divided in two categories, i.e. market risk and business risk. The market risk (MR) is measured by stock Beta (β_i) from CAPM equation (Bromiley et al., 2017; Miller & Reuer, 1996; Narang & Kaur, 2014). Whereas, the business risk (BR) is measured by the standard deviation of the error term σ (ϵ_{it}) of CAPM equation $[(R_{it} - R_{ft}) = \alpha_i + \beta_i (R_{mt} - R_{ft}) + \epsilon_{it}]$ over the estimation period of each firm (Bromiley et al., 2017). The financial leverage and firm size are taken as control variables. The financial leverage (FL_{lev}) is measured as ratio of total debt to equity (Narang & Kaur, 2014). Whereas, firm size (FS_{ize}) is measured by natural log of firm sales (Narang & Kaur, 2014; Saunders, Strock, & Travlos, 1990) and slack (Slack) which is a moderating variable is measured as current asset divided by current liabilities (Wiseman & Bromiley, 1996).

3.2 Econometric Models

In model I and model II we test our basic hypotheses of study, that business risk and market risk positively affect the firm manufacturing and operational costs. The model I empirically estimates H1 and H2.

$$MC_i = \alpha_i + \beta_1 \text{LogBR}_i + \beta_2 \text{LogMR}_i + \beta_3 \text{FL}_{lev_i} + \beta_4 \text{LnFS}_{ize}_i + \mu_i \dots (\text{Model I})$$

Whereas, model II corresponds to H3 and H4.

$$\text{LogOC}_i = \alpha_i + \beta_1 \text{LogBR}_i + \beta_2 \text{LogMR}_i + \beta_3 \text{FL}_{lev_i} + \beta_4 \text{LnFS}_{ize}_i + \mu_i \dots (\text{Model I})$$

In model III and model IV, we introduce slack as a moderator. We proposed that accessibility to slack negatively affect the positive association between business risk and market risk with firm manufacturing cost and operational

costs. Model III empirically evaluates H5 & H6 and model IV analyzes H7 and H8.

$$MC_i = \alpha_i + \beta_1 \text{LogMR}_i + \beta_2 \text{LogBR}_i + \beta_3 \text{LnSlack}_i + \beta_4 \text{FL}_i + \beta_5 \text{LnFSize}_i + \beta_6 \text{LogMR}_i \times \text{LnSlack}_i + \beta_7 \text{LogBR}_i \times \text{LnSlack}_i + \mu_i \dots\dots\dots \text{ (Model III)}$$

$$\text{LogOC}_i = \alpha_i + \beta_1 \text{LogMR}_i + \beta_2 \text{LogBR}_i + \beta_3 \text{LnSlack}_i + \beta_4 \text{FL}_i + \beta_5 \text{LnFSize}_i + \beta_6 \text{LogMR}_i \times \text{LnSlack}_i + \beta_7 \text{LogBR}_i \times \text{LnSlack}_i + \mu_i \dots\dots\dots \text{ (Model IV)}$$

4.0 Analysis and Discussion

The result of descriptive and correlation statistics are shown in Table 1. The descriptive statistics describe the nature and dispersion of data in our sample. The results show that on average the manufacturing cost is 70.278 percent of the total organizational sales across the sample. This represents major overhead of the organizations cost structure. Any significant changes in this head with respect to business and market risk can affect its current and future course of operations. The operational cost which is the second dependent variable has an average value of 18 percent. This shows that average operational cost of the organizations are 18% of its total sales. Although it is not as significant in terms of its proportion to the overall cost, but still represents a considerable part of the organization’s total cost. However, the nature of operational cost is very important and directly associated with revenue generating activities of the organizations (Cooper & Kaplan, 1992). For instance, the expenses related to sales commissions and advertising are directly associated with increase in organization sales. Further, the salaries, perks and privileges associated with employees competence and motivation (Edwards et al., 2008), technological and process improvement also correspond to the quality of work force, efficiency and better risk management practices (Hammer, 2015). The average market risk and business risk of organizations across the sample is 0.958 and 0.056 respectively.

Table 1 *Descriptive and Correlation Statistics*

Variables	Mean	Std.Dev	(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. MC	70.28	19.03	1						
2. OC	18.53	35.25	-0.30*	1					
3. MR	0.96	0.25	-0.03*	0.02	1				
4. BR	0.06	.02	0.05*	0.07*	0.02	1			
5. Slack	2.62	4.22	-0.14*	0.25*	-0.05*	0.01	1		
6. LnFSize	11.68	1.91	0.19*	-0.26*	0.13*	-0.29*	-0.28*		
7. FL _{ev}	32.61	21.94	0.20*	-0.08*	0.00	0.05*	-0.22*	0.15	1

* $p < 0.01$, ** $p < 0.05$

The correlations statistics displayed in Table 1 illustrate that, manufacturing cost is significant and negatively correlated with market risk. However, manufacturing cost exhibit positive correlation with business risk. These results demonstrate that, increase in business risk and market risks have contrary effects on the manufacturing cost of the firm. Such as, increase in market risk subsequent leads to decline of manufacturing cost. However, increase in business risk results in rise of organization's manufacturing cost. On the other hand, operational cost is positively correlated with both business risk and market risk. This signifies positive association between organizational risks and operational cost. The available slack is negatively associated with manufacturing but shows positive association with operational cost. Furthermore, the correlation statistics confirm negative and significant association between available slack and market risk.

The regression analysis results are shown in Table 2. In Model I, we analyzed the impact of business risk and market risk on organization's manufacturing cost. The empirical results confirm that, business risk has positive and significant impact on manufacturing cost. Similarly, the coefficient of market risk is positively and significantly associated with manufacturing cost. Hence, we accept H1 and H2. Those empirical results validate our developed theory that increase in business risk and market risks have a domino effect of increasing manufacturing related costs. Such as purchase of goods, raw materials and indirect costs related to warehousing, facilities, equipment and labors. Therefore, various stakeholders related to those overhead costs will ask for tough contractual agreement (Jones et al., 2018). In case of operational cost, the coefficient of business risk and market risk is significant and positive. This shows that, increase in business and market risk also upshot the operational expenses. Such as higher employee's remuneration, organizations have to bear higher insurance, selling, marketing and administrative costs. Thus, we also accept H3 and H4.

Table 2 Regression Analysis

	(M I) MC	(M II) LogOC	(M III) MC	(M IV) LogOC
LogMR	22.81** -9.42	3.60*** -0.53	73.55*** -20.75	4.55*** -0.76
LogBR	64.44*** -5.77	0.51*** -0.13	99.76*** -12.27	0.17 -0.38
LnSlack			-162.87*** -23.89	-0.03 -0.69
FLev	0.07** -0.03	-0.01*** -0.00	0.06 -0.05	-0.01*** -0.00
LnFSize	4.53*** -0.38	-0.19*** -0.02	4.71*** -0.58	-0.19*** -0.02
LogMR×LnSlack			-41.69*** -11.38	-2.13*** -0.49
LogBR×LnSlack			-54.82*** -8.07	0.03 -0.24
Cons	207.70*** -16.05	6.70*** -0.47	311.636** *	5.66*** -1.03
Endogeneity Test of Endogenous variables	285.21***	111.39***	279.02***	117.54***
Kleibergen-Paap rk LM Statistic	83.58***	64.72***	46.14***	48.70***
Hansen J Statistic	0.176	0.604	0.003	1.617
Cragg-Donald Wald F Statistic	33.439ψ	27.985ψ	18.570ψ	19.679ψ
Obs.	4609	4609	4581	4581
F Stat	65.21***	57.15***	22.38***	35.61***

Standard errors are in parenthesis *** p<0.01, ** p<0.05, * p<0.1
 ψ Yogo weak ID test Maximum IV relative critical value is 13.43

In Model III we introduced an interaction effect of slack with business risk and market risk to estimate its impact on manufacturing cost. In this model the interaction terms LogMR×LnSlack and LogBR×LnSlack significantly and negatively impacting the relationship between manufacturing cost and organization’s business risk and market risk respectively. This shows that, the organizations with adequate accessibility to slack have weakened the positive association of organizational risks and manufacturing cost. Hence, we accept H5 and H6, that slack act as buffer during market and firm-specific uncertainties and reduce its negative consequences of increase in manufacturing cost. In case of operational cost, the interaction term of LogBR×LnSlack is insignificant; consequently we cannot confirm our

predicted proposition. Thus we reject H7. However, the interaction term of $\text{LogMR} \times \text{LnSlack}$ is significant and negative. This shows that available slack is fading the negative effects of increasing operational cost as a result of increase in market risk. Therefore, we accept H8.

5.0 Conclusion

In this paper we extended risk-return tradeoff into risk and cost association of the organizations operating in Asian emerging markets. The emerging markets exhibits a unique set of characteristics, such as, volatile market dynamics, low income population, non-standardized contracts, unstructured supply chain mechanisms and fast-growing economies. As a result, risk embedded in every strategic decision must be taken with caution and its implication cannot be underestimated. We established that organizational costs bear the instant financial impact of higher risk form key stakeholders. Afterward, that negative financial impact emerges as either losses or decrease in profits. So, the negative financial impact of diverse stakeholders is very critical and insightful for organization managers and its long term objectives. We also provided substantial evidence that organizational risk is a function of both market risk and business risk. Therefore, untangling risk into market risk and business risk ascertain more specific impact on different level of the business operations. Overall our empirical results established that, risk act as a specter, which affects every stakeholder. On one side the uncertainty in the minds of those stakeholders is transformed into tough contractual agreements, thus have a direct impact on organizational cost. On the other side, the organizational cost shows sticky behavior, thus further aggravate the organizational performance in uncertain market dynamics. Further, we also established that availability of slack is very important to deal with the consequences of increasing market and business risk. As whole, the empirical evidence provides management an essential perspective and insight to identifying and understand the nature of organizational risk, slack, stakeholders and it implication for organizational costs in Asian emerging markets.

References

- Amaya, D., Gauthier, G., & Léautier, T. O. (2015). Dynamic risk management: investment, capital structure, and hedging in the presence of financial frictions. *Journal of Risk and Insurance*, 82(2), 359-399.
- Amit, R., & Wernerfelt, B. (1990). Why do firms reduce business risk? *Academy of Management Journal*, 33(3), 520-533.
- Andersen, T. J. (2009). Effective risk management outcomes: exploring effects of innovation and capital structure. *Journal of Strategy and Management*, 2(4), 352-379.

- Andersen, T. J., & Bettis, R. A. (2015). Exploring longitudinal risk-return relationships. *Strategic Management Journal*, 36(8), 1135-1145.
- Anderson, M., Banker, R., Huang, R., & Janakiraman, S. (2007). Cost behavior and fundamental analysis of SG&A costs. *Journal of Accounting, Auditing & Finance*, 22(1), 1-28.
- Aybar, B., & Thirunavukkarasu, A. (2005). Emerging market multinationals: an analysis of performance and risk characteristics. *Journal of Asia-Pacific Business*, 6(2), 5-39.
- Bacon, N., & Hoque, K. (2005). HRM in the SME sector: valuable employees and coercive networks. *The International Journal of Human Resource Management*, 16(11), 1976-1999.
- Bansal, P., & Clelland, I. (2004). Talking trash: Legitimacy, impression management, and unsystematic risk in the context of the natural environment. *Academy of Management Journal*, 47(1), 93-103.
- Berghöfer, B., & Lucey, B. (2014). Fuel hedging, operational hedging and risk exposure—Evidence from the global airline industry. *International Review of Financial Analysis*, 34, 124-139.
- Bettinazzi, E. L., & Zollo, M. (2017). Stakeholder orientation and acquisition performance. *Strategic Management Journal*, 38(12), 2465-2485.
- Bharadwaj, S. G., Tuli, K. R., & Bonfrer, A. (2011). The impact of brand quality on shareholder wealth. *Journal of Marketing*, 75(5), 88-104.
- Bowman, E. H. (1982). Risk seeking by troubled firms. *Sloan Management Review*, 23(4), 33-47.
- Bromiley, P., McShane, M., Nair, A., & Rustambekov, E. (2015). Enterprise risk management: Review, critique, and research directions. *Long Range Planning*, 48(4), 265-276.
- Bromiley, P., Rau, D., & Zhang, Y. (2017). Is R & D risky? *Strategic Management Journal*, 38(4), 876-891.
- Bromiley, P., & Washburn, M. (2011). Cost reduction vs innovative search in R&D. *Journal of Strategy and Management*, 4(3), 196-214.
- Chou, P.-H., Chou, R. K., & Ko, K.-C. (2009). Prospect theory and the risk-return paradox: some recent evidence. *Review of Quantitative Finance and Accounting*, 33(3), 193-208.
- Coad, A. F., & Cullen, J. (2006). Inter-organisational cost management: Towards an evolutionary perspective. *Management Accounting Research*, 17(4), 342-369.
- Cooper, R., & Kaplan, R. S. (1992). Activity-based systems: Measuring the costs of resource usage. *Accounting Horizons*, 6(3), 1-13.

- Crilly, D., & Sloan, P. (2012). Enterprise logic: explaining corporate attention to stakeholders from the 'inside-out'. *Strategic Management Journal*, 33(10), 1174-1193.
- Cyert, R. M., & March, J. G. (1963). *A Behavioral Theory of the Firm*. Englewood Cliffs, NJ, 2.
- Daniel, F., Lohrke, F. T., Fornaciari, C. J., & Turner Jr, R. A. (2004). Slack resources and firm performance: a meta-analysis. *Journal of Business Research*, 57(6), 565-574.
- Dekker, H. C., Sakaguchi, J., & Kawai, T. (2013). Beyond the contract: Managing risk in supply chain relations. *Management Accounting Research*, 24(2), 122-139.
- Edwards, P., Ram, M., & Smith, V. (2008). *Introduction to special issue: Workers, Risk and the New Economy*: Sage Publications Sage UK: London, England.
- El Ghouli, S., Guedhami, O., Ni, Y., Pittman, J., & Saadi, S. (2013). Does information asymmetry matter to equity pricing? Evidence from firms' geographic location. *Contemporary Accounting Research*, 30(1), 140-181.
- Estrada, J. (2011). The Three-Factor Model: A Practitioner's Guide. *Journal of Applied Corporate Finance*, 23(2), 77-84.
- Fama, E. F., & French, K. R. (1993). Common risk factors in the returns on stocks and bonds. *Journal of Financial Economics*, 33(1), 3-56.
- Freeman, R. E. (2010). *Strategic Management: A Stakeholder Approach*. Cambridge University Press.
- Geiger, S. W., & Cashen, L. H. (2002). A multidimensional examination of slack and its impact on innovation. *Journal of Managerial Issues*, 68-84.
- Hammer, M. (2015). *What is Business Process Management? Handbook on Business Process Management*. Springer.
- Harrison, J. S., & Freeman, R. E. (1999). Stakeholders, social responsibility, and performance: Empirical evidence and theoretical perspectives. *Academy of Management Journal*, 42(5), 479-485.
- Henkel, J. (2009). The risk-return paradox for strategic management: disentangling true and spurious effects. *Strategic Management Journal*, 30(3), 287-303.
- Hillman, A. J., & Keim, G. D. (2001). Shareholder value, stakeholder management, and social issues: What's the bottom line? *Strategic Management Journal*, 22(2), 125-139.
- Hsu, L.-T. J., & Jang, S. S. (2008). Advertising expenditure, intangible value and risk: A study of restaurant companies. *International Journal of Hospitality Management*, 27(2), 259-267.
- Irvine, P. J., Park, S. S., & Yıldızhan, Ç. (2016). Customer-base concentration, profitability, and the relationship life cycle. *The Accounting Review*, 91(3), 883-906.

- Jensen, M. C. (1986). Agency costs of free cash flow, corporate finance, and takeovers. *The American Economic Review*, 76(2), 323-329.
- Jirasek, M. (2017). The influence of national culture on changes in R&D expenses among agrochemical firms. *Agricultural Economics*, 63(11), 524-530.
- Jones, T. M., Harrison, J. S., & Felps, W. (2018). How applying instrumental stakeholder theory can provide sustainable competitive advantage. *Academy of Management Review*, 43(3), 371-391.
- Kallenberg, K. (2007). The role of risk in corporate value: A case study of the ABB asbestos litigation. *Journal of Risk Research*, 10(8), 1007-1025.
- Khanna, T., & Palepu, K. G. (2006). Emerging giants: Building world-class companies in developing countries. *Harvard Business Review*, 84(10).
- Kim, S. K., Cho, H., & Khieu, H. (2014). Slack and R&D strategy: The effect of slack on internal R&D and external R&D, and innovation. *Journal of Management Policy and Practice*, 15(2), 33-47.
- Lee, C. L., & Wu, H. C. (2016). How do slack resources affect the relationship between R&D expenditures and firm performance? *R&D Management*, 46(S3), 958-978.
- Li, K., Griffin, D., Yue, H., & Zhao, L. (2013). How does culture influence corporate risk-taking? *Journal of Corporate Finance*, 23, 1-22.
- Liu, X., Liu, X., & Reid, C. D. (2019). Stakeholder orientations and cost management. *Contemporary Accounting Research*, 36(1), 486-512.
- Low, A. (2009). Managerial risk-taking behavior and equity-based compensation. *Journal of Financial Economics*, 92(3), 470-490.
- Lubatkin, M., & Chatterjee, S. (1994). Extending modern portfolio theory into the domain of corporate diversification: Does it apply? *Academy of Management Journal*, 37(1), 109-136.
- Marlin, D., & Geiger, S. W. (2015). The organizational slack and performance relationship: a configurational approach. *Management Decision*, 53(10), 2339-2355.
- McGoun, E. G. (1995). The history of risk "measurement". *Critical Perspectives on Accounting*, 6(6), 511-532.
- Meulbroek, L. K. (2002). A senior manager's guide to integrated risk management. *Journal of Applied Corporate Finance*, 14(4), 56-70.
- Miller, K. D. (2009). Organizational risk after modernism. *Organization Studies*, 30(2-3), 157-180.
- Miller, K. D., & Bromiley, P. (1990). Strategic risk and corporate performance: An analysis of alternative risk measures. *Academy of Management Journal*, 33(4), 756-779.

- Miller, K. D., & Chen, W.-R. (2003). Risk and firms' costs. *Strategic Organization*, 1(4), 355-382.
- Miller, K. D., & Reuer, J. J. (1996). Measuring organizational downside risk. *Strategic Management Journal*, 17(9), 671-691.
- Narang, S., & Kaur, M. (2014). Impact of firm-specific attributes on shareholder value creation of Indian companies: An empirical analysis. *Global Business Review*, 15(4), 847-866.
- Nohria, N., & Gulati, R. (1996). Is slack good or bad for innovation? *Academy of Management Journal*, 39(5), 1245-1264.
- Oviatt, B. M., & Bauerschmidt, A. D. (1991). Business risk and return: A test of simultaneous relationships. *Management Science*, 37(11), 1405-1423.
- Patatoukas, P. N. (2012). Customer-Base Concentration: Implications for Firm Performance and Capital Markets. *The accounting review*, 87(2), 363-378.
- Reider, R. (2004). Cost reduction analysis: A benchmarking guide for treasury managers. *Journal of Corporate Accounting & Finance*, 16(1), 33-41.
- Reider, R. (2008). Sharp ideas for controlling costs. *Journal of Corporate Accounting & Finance*, 19(3), 3-9.
- Ruefli, T. W. (1990). Mean-variance approaches to risk-return relationships in strategy: Paradox lost. *Management Science*, 36(3), 368-380.
- Sanchez, R. (1995). Strategic flexibility in product competition. *Strategic Management Journal*, 16(S1), 135-159.
- Santacruz, L. (2020). Measures of firm risk-taking: revisiting Bowman's paradox. *Managerial Finance*, 46(3), 421-434.
- Saunders, A., Strock, E., & Travlos, N. G. (1990). Ownership structure, deregulation, and bank risk taking. *The Journal of Finance*, 45(2), 643-654.
- Sax, J., & Andersen, T. J. (2019). Making risk management strategic: Integrating enterprise risk management with strategic planning. *European Management Review*, 16(3), 719-740.
- Smithson, C., & Simkins, B. J. (2005). Does risk management add value? A survey of the evidence. *Journal of Applied Corporate Finance*, 17(3), 8-17.
- Winn, D. N. (1977). On the relations between rates of return, risk, and market structure. *The Quarterly Journal of Economics*, 157-163.
- Wiseman, R. M., & Bromiley, P. (1996). Toward a model of risk in declining organizations: An empirical examination of risk, performance and decline. *Organization Science*, 7(5), 524-543.
- Wood Donna, J. (1995). Stakeholder mismatching: A theoretical problem in empirical research on corporate social performance. *The International Journal of Organizational Analysis*, 3(3), 229-267.