



Contemporary Accounting Case Studies

Volume 3, Nomor 1, March 2024

Article 22

THE IMPACT OF COVID-19 IN DETERMINING OF RISK APPETITE IN COMPANY XYZ

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THE IMPACT OF DETERMINING THE LEVEL OF RISK APPETITE IN PT XYZ BEFORE AND DURING THE COVID-19 PANDEMIC

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ABSTRACT

This study aims to analyse the impact of determining the level of risk appetite at PT XYZ before and during the Covid-19 pandemic. PT XYZ is an SME-scale business engaged in water sports in Tanjung Benoa, Bali. The research uses narrative analysis techniques based on the PT XYZ case study. Data were obtained from interviews with informants involved in the decision-making process at PT XYZ, profit and loss reports, and reports on the level of tourist visits to the company's place of business. The research employs Quail's theory (2012) of risk appetite, which is divided into eight aspects (customer, financial development, security, employee relations, technical innovation, shareholder return, corporate image, and environmental) and five determination levels (averse, minimalist, cautious, flexible, and open). Employees at PT XYZ do not understand risk appetite; therefore, decision-making is based on frequently enacted habits. Various recommendations are made: map the strengths and weaknesses of the company and disseminate these to employees to provide a common perception of the company's vision and mission; provide knowledge of the meaning of risk appetite so that employees have more reliable knowledge and can create more optimal business strategies in line with the company's current conditions; the management must understand the capabilities of the company so that when establishing the desired level of risk it can meet the standards of the assessment criteria. If PT XYZ is already aware of its capabilities, Quail's (2012) theory may be used to ascertain the level of risk appetite in the decision-making process. Top-level management could commence periodic evaluations in this area to ensure the company selects the most appropriate risk appetite for its business continuity and that this is aligned with the desired goal.

Keywords: *Covid-19, Level of Risk, Risk Appetite.*

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I. INTRODUCTION

The Covid-19 pandemic has had a major impact on the economies of many countries around the world. It has led to various types and fields of business having to adapt from an operational, financial, and management system perspective. The main problem facing company management in the context of Covid-19 has been how to run their organisations amid the many new rules and regulations implemented by central and regional governments based on the location of the business. One impacted decision concerns how the company determines risk appetite. This reflects changes in regulations linked to the opening of borders, additional business operational requirements, and regulations on visitor capacity in business premises and who is permitted to visit the business location. COSO (2012) defined risk appetite as the type and amount of risk that is acceptable to a company in achieving its desired value/goal/target. Risk appetite is a key aspect and forms the basis for other aspects of risk management. As such, it is used as a reference in the process of developing, implementing, and monitoring strategy. Quail (2012) explained that risk appetite is divided into five levels, influenced by eight determinant spectrums (factors) (i.e. the customer, financial development, security, employee relations, technical innovation, shareholder return, corporate image, and environmental aspects). These eight spectrums/factors are used as a reference by stakeholders in making decisions related to the company's strategic goals. Determination of the level of risk appetite is a matter of continuity and may change depending on the influence of risk and supporting factors.

Due to its impact on the business cycle, companies have been forced to adapt more quickly during the Covid-19 pandemic, reflecting how rules/regulations can change weekly. This impacts companies on an international, national, multinational, large, medium, and small scale, including PT XYZ. PT XYZ is a medium-category company (UU No. 20 of 2008) and as such does not yet have a separate risk management division. The strategic changes that PT XYZ was compelled to make during the pandemic included business promotion to customers. This was aimed at increasing tourist visits to business places, setting the total capacity in terms of tourist visits to locations, and the mandatory requirements for visits by tourists. This change in strategy was influenced by regulatory changes related to community social activities and thus had an impact on changes in risk appetite at PT XYZ.

This research therefore focuses on determining the level of risk appetite based on Quail (2012) at PT XYZ before and during the Covid-19 pandemic. This problem is interesting to study because PT XYZ is a type of business that has been directly affected by the Covid-19 pandemic. This has typically involved disruption to company activities; as such, determining the appropriate level of risk appetite is essential for companies to achieve their strategic goals.

II. LITERATURE REVIEW

Zhong et al. (2021) explained that Covid-19 has affected not just one but several or many aspects of the company field, including employee effectiveness, the determination of bonuses or salaries, how to ensure employee safety, and how to organise the company, among other aspects. These considerations have created economic disruption for employees and companies. Economic disturbances for employees were due to widespread lossmaking among companies, leading to workforce reductions or salary cuts. This in turn impacted employees' social lives, while for companies, the economic disruption resulted in losses due to a slowdown in operational activities.

Quail (2012) classified risk appetite into five levels based on the extent to which the organisation is able (wants) to accept the desired risk. The five levels reflect different philosophies, tolerance for uncertainty, choice, and ability to refuse depending on the capabilities possessed by the organisation. They are:

1. Averse

Companies at the averse level view the avoidance of risk as 'sacred'. The company's main goal is thus to avoid risks that can arise from the chosen decision-making. There is a very low tolerance for uncertainty and the selection of risk appetite at this level always involves the lowest-risk option from those available. The ability to refuse risk at this level is non-existent (do not want to) since companies never take big risks, thereby defining the nature of their risk appetite.

2. Minimalist

At the minimalist level, only very conservative risks are considered. This philosophy illustrates that companies consider risk to be something that happens regarding things that have become a habit (customs); as such, companies at this level only make decisions related to risk appetite based on things for which they understand the risks. There is a low tolerance for uncertainty at this level, which means companies will function based on the risk appetite that has always been adopted thus far. The action (choice) taken by the company will accept a risk if it has a significant impact on business continuity and is limited to the possibility/level of failure that can occur. Companies at this level will be very reluctant to take big risks, meaning they will have a relatively large capacity to refuse the risks that occur.

3. Cautious

Companies at the cautious level operate based on a preference for risks that can be deemed safe. As such, their risk appetite is such that they are willing to accept the risks that arise from their decision-making, but only those that are considered safe and can be properly controlled. There is limited tolerance for uncertainty at this level. This can be interpreted as companies knowing that various elements pose a risk to their business and accepting limited risks based on a consideration of those with the potential to yield the greatest benefit. The ability to resist at this level is essentially categorised as trying to avoid.

4. Flexible

At the flexible level, the only acceptable risks are those that are considered true (main). Here, companies will only take risks that they consider to be covered by the most important (main) aspects of the chosen risk appetite to ensure they have the necessary planning in place if the risk should occur. In terms of tolerance of uncertainty, companies at this level have predicted that various risks will arise due to their choice of risk appetite; as such, they choose to take risks while remaining capable of controlling/managing the impacts that arise. In terms of risk refusal at this level, firms accept (are ready for) the risks that will arise but only in the most correct (appropriate) conditions.

5. Open

At the open level, companies will only take risks that they consider appropriate. As such, they will accept all possible risks that arise and consciously understand that this choice of risk appetite will necessarily entail the incurring of various risks. In terms of tolerance for uncertainty, companies at this level will fully anticipate the risks that can occur. As a result, they will choose the option that delivers the greatest impact (highest return) but also accept the possibility of failure. At this level, companies are willing, meaning they will accept the outcome if the chosen option fails to achieve the desired target and will not perceive it as a loss.

RISK APPETITE SCALE				
Rating	Philosophy	Tolerance for Uncertainty	Choice	Trade-off
5	Open Overall risk-taking philosophy	Willingness to accept uncertain outcomes or period-to-period variation	When faced with multiple options, willingness to select an option that puts objectives at risk	Willingness to trade off against achievement of other objectives
5	Open Will take justified risks	Fully anticipated	Will choose option with highest return; accept possibility of failure	Willing
4	Flexible Will take strongly justified risks	Expect some	Will choose to put at risk, but will manage impact	Willing under right conditions
3	Cautious Preference for safe delivery	Limited	Will accept if limited, and heavily outweighed by benefits	Prefer to avoid
2	Minimalist Extremely conservative	Low	Will accept only if essential, and limited possibility/extent of failure	With extreme reluctance
1	Averse "Sacred" Avoidance of risk is a core objective	Extremely low	Will select the lowest risk option, always	Never

Figure 2.1 Risk Appetite Scale

Source: Quail (2012)

Quail (2012) explained the three steps involved in determining the scale of risk appetite, namely:

1. Determine the target risk appetite

This step is performed by the main management when making decisions. They must develop targets for each desired strategic objective based on the agreed risk appetite. Each rank is plotted along a separate axis according to its strategic objective. The numerical values increase along the longitudinal line from the centre; thus, the greater the risk appetite for the strategic objectives, the larger the total area in the net, representing a large overall risk appetite for the organisation.



Figure 2.2 Target Risk Appetite

Source: Quail (2012)

Quail's risk appetite radar (RAR) is a graphic visualisation of both the pluralistic values of the organisation and the strategic-level decision-making steps that influence management decision-making, namely the factors of safety, customer, environment, revenue growth, shareholder return, corporate image, employee relationship, and technical innovation. The lines on these factors arise based on the result of a management assessment of the factors that have the greatest influence on the company versus those with relatively little impact, on a scale of 1–5. This scale provides a measure of risk appetite that will ultimately make executives hold joint discussions and determine their ability to accept all possible risks that arise and whether certain things should be sacrificed if these risks occur.

2. Assess the selected risk appetite

The second step is to rank the same objectives by making comparisons on the same scale, to determine the current level of risk appetite that applies to all organs in the organisation.



Figure 2.3 Target vs Exhibited Risk Appetite

Source: Quail (2012)

Figure 2.3 is the same depiction as Figure 2.2. Quail aimed to show that after assessing/determining the desired target appetite, management must reassess this target appetite in terms of its alignment with the exhibited risk appetite. The same components (safety, customer, environment, revenue growth, shareholder return, corporate image, employee relationship, technical innovation) must be used for the reassessment because Quail wished to determine whether a significant difference existed between the target and exhibited risk appetites. If a significant difference is identified, it can be concluded that the company has not been able to determine the target appetite in line with the conditions of the company. If no significant difference is identified, the company already understands its strategic goals and the appropriate risk appetite needed to achieve them.

3. Evaluate the selected risk appetite

The final step is to evaluate the selected risk appetite by collecting data related to risk appetite perceptions (using the same scale) at all levels of the organisation and comparing this to the targets set by the management. This assists in determining the signals received by employees regarding the organisation along with their expectations for taking risks related to the desired goals.

III. RESEARCH METHOD

This research used a descriptive qualitative approach with a case study at PT XYZ located in the Tanjung Bena area, Bali. Data were obtained from the company's profit and loss reports (2020, 2021, and 2022), reports on the level of customer visits, and interviews with selected informants aimed at obtaining direct information regarding the condition of PT XYZ. Narrative analysis was then used to describe the results of the interviews to understand the risk appetite level based on the Quail approach (2012). The Quail (2012) approach was employed to assist in determining the risk level category of PT XYZ. Interviews were conducted separately with four PT XYZ management informants who played a role in determining the company's risk appetite to achieve the desired goals. It was hoped that the informant interviews would yield detailed information regarding the process of determining the company's risk appetite for the conditions (positions) currently being experienced by PT XYZ.

The interview activities were conducted between the second and fourth weeks of May 2022 (08–20 May 2022) using Zoom meeting technology. Eight assessment criteria were used with five levels of risk appetite, based on Quail's (2012) theory of risk appetite levels and adapted to the conditions at PT XYZ. The assessment criteria were divided into the security, customer, environmental, financial development, shareholder return, corporate image, employee relations, and technical innovation aspects, as described by Quail (2012), as the factors influencing companies to make decisions. The five risk appetite levels described reflect the organisation's ability to accept the desired risk.

IV. ORGANISATION PROFILE

PT XYZ is an organisation engaged in tourism, particularly water sports activities, in the Tanjung Benoa area of Bali. Tanjung Benoa is a tourist destination for both local and foreign tourists visiting Bali. PT XYZ was established in 2018 and five shareholders each hold a 20 per cent share of the company. The company has held an NPWP, business licence, location permit, and environmental permit since 2018; it has therefore operated in line with the provisions in force in Indonesia. PT XYZ is a limited company that, when viewed from the scale of its working capital (Rp 500,000,000 – Rp 10,000,000,000) and the number of employees (> 20), is defined as an SME (Articles 35 & 36 PP UMKM). It has assets in the form of buildings and various water sports equipment used to support its business activities. Since its establishment in 2019, PT XYZ has always maintained a positive financial position and has therefore always been able to make payments for trade payables and employee salaries. In 2019, PT XYZ earned a sufficiently large income to exceed the required monthly repayments on its bank loans. The management expected the company to achieve a return on the business capital provided by shareholders in mid-2020. However, this was not achieved due to the emergence of the Covid-19 pandemic in Indonesia at the beginning of 2020, which negatively impacted the company's business sector.

PT XYZ began to experience difficulties in running its business in mid-2020 when the number of tourists visiting its place of business fell by 90%. With fewer tourists, the company was forced to modify its strategy, although this was ultimately unsuccessful in increasing the number of tourists visiting the place of business. The management then decided to close the business until 2021 in the hope of reducing the burden. The company also switched to only paying the interest on its bank loans. It also reduced the size of the workforce, amended work contracts, and cut employee salaries.

V. RESULT AND DISCUSSION

Based on the interviews conducted, the employees at PT XYZ define risk appetite as something that naturally occurs, based on recurring events, and that must be faced by the company due to its operational activities. This indicates that PT XYZ employees do not understand the company's strengths and weaknesses. It is important to understand the strengths and weaknesses of a company to ensure a more effective and efficient decision-making process. However, due to the lack of such an understanding, the company did not understand its risk appetite. This meant that risk control was conducted solely based on the aspects that they did understand.

Figure 5.1 indicates the target and exhibited appetites at PT XYZ. The target appetite describes the company's position in the pre-pandemic period while the exhibited appetite is the realisation that occurred during the pandemic.

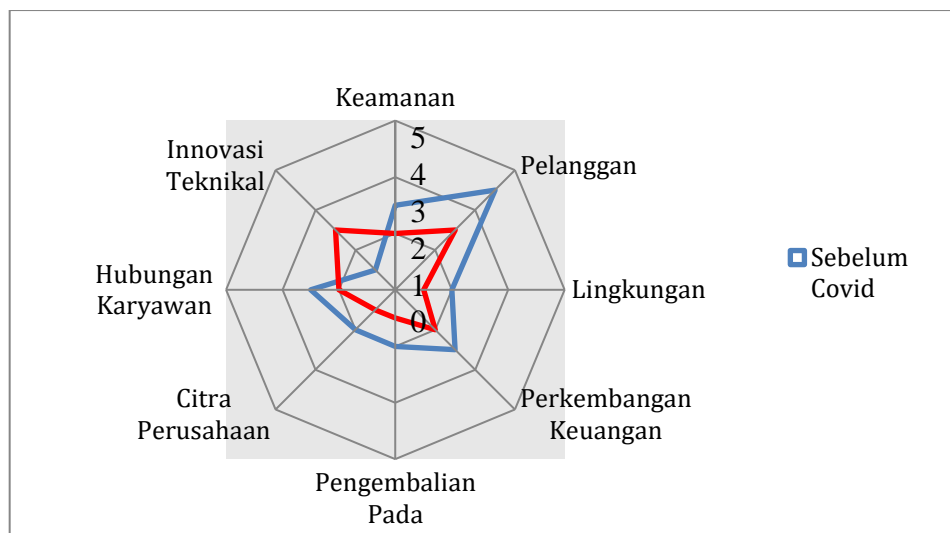


Figure 5.1 Target vs Exhibited Appetite at PT XYZ

Resource: Writer analysis (2022)

Figure 5.1 illustrates the position of PT XYZ before and during the pandemic. Based on this description, the following information is known:

1. Customer Aspect

The customer aspect relates to the people who perform transactions in a business unit of a company, thereby increasing its financial capability. The customer aspect at PT XYZ can therefore be described as the number of tourist arrivals who conduct activities related to PT XYZ’s business. The customer aspect altered as a result of the pandemic, having stood at level 5 before the pandemic. Here, it had many customers, so the company always accepted all criticism and suggestions given and was ready to take responsibility in the event of any unexpected incident.

During the pandemic, however, the company changed to level 3 due to a drastic reduction in the number of visiting customers. In response, the company lowered its position to provide maximum customer satisfaction. This illustrates the various adjustments to customer aspects that companies need to make during a pandemic, such as preparing its facilities to create customer comfort.

Tingkatan Kunjungan Pelanggan			
	2020	2021	2022
JANUARY	1,144	743	1,641
FEBRUARY	658	213	743
MARCH	256	358	742
APRIL	-	479	793
MAY	-	635	3,215
JUNE	-	534	3,380
JULY	14	204	4,978
AUGUST	374	107	3,398
SEPTEMBER	156	478	3,748
OCTOBER	440	720	3,136
NOVEMBER	699	869	2,794
DECEMBER	849	1,816	5,331
Total Aktivitas	4,590	7,156	33,899

Figure 5.2 Customer Numbers

Resource: Writer Analysis (2022)

Figure 5.2 shows the level of customer visits to PT XYZ during the pandemic, with the fewest visits evident in 2020. This mirrors the arrival of the pandemic in Indonesia in February 2020, which was followed by a tightening of the rules regarding foreign tourist visits. It can also be seen that PT XYZ closed the business from April to June 2020 to make changes related to the new regulations and reduce its losses. Customer numbers began to increase significantly in May 2022 due to the loosening of travel regulations by the state and the many international-scale events held in Bali, both of which had a positive influence on the continuity of the company's business.

2. Financial Development Aspect

The financial development aspect is described as the level of financial capacity within the business processes of the organisation. At PT XYZ, financial development concerns the condition for profits/losses on business activities. The company was positioned at different levels in the financial development aspect before compared to during the pandemic. Its position at level 3 before the pandemic indicated that it made sufficient profits to make corporate debt payments while retaining a financial reserve for use in unexpected situations.

However, during the pandemic, the company changed to level 2 since it only generated enough profit to conduct its operational activities and sacrificed several other business support factors. This illustrates how companies are obliged to make several adjustments to aspects of financial development during a pandemic, including their income reserves with existing operating expenses. PT XYZ sold its shuttle cars and submitted requests to postpone its debt payments to improve its financial condition.

3. Security Aspect

Security is described as a guarantee for activities carried out related to the company's business processes. At PT XYZ, security relates to maintaining the comfort and safety of tourists who undertake activities at tourist sites.

The company was positioned at different levels for the security aspect before compared to during the pandemic. Its target (before the pandemic) was level 3, at which point the company employed a limited security team to perform its security activities and prevent any unwanted events arising from its business activities. During the pandemic, however, the position changed to level 2 as the company was forced to reduce the size of the security team due to a fall in revenue and customer numbers. This reflects the changes required to aspects of security during a pandemic, such as selecting who to retain and then allocating tasks for these safeguards, along with reducing the salary paid to the security team.

4. Employee Relations Aspect

This aspect is described as the level between employees in the company's business. Aspects of employee relations at PT XYZ are described as the process of cooperation between employees in conducting the company's operational activities.

There were different levels in the aspect of employee relations before compared to during the pandemic. Prior to the pandemic the company was at level 3, characterised by familial-type employee relations. This changed to level 2 during the pandemic, however, as the company was forced to reduce the size of its workforce, which resulted in feelings of disappointment or loss among employees. In terms of the adjustments to aspects of employee relations required during a pandemic, this illustrates how

companies should ensure that employees understand the company's conditions while explaining that the relationships that have existed up to that point have not changed. This decrease in level was based on the company's income statement and customer activity reports for the period 2020 to mid-2022. The business was closed for three months in 2020, which led to a headcount reduction. The company also eliminated consumption for employees and tips for guides who brought customers, resulting in a decrease in the level of employee trust.

5. Technical Innovation Aspect

Aspects of technical innovation are described as changes that are technical and related to the company's business processes. Technical innovation at PT XYZ is described as the process of amending the company's strategy due to changes in its business conditions. The company occupied different positions on the innovation aspect before and during the pandemic. Level 1, before the pandemic, indicated that the company relied on acquaintances or old customer relationships for its promotional activities. However, this changed to level 3 during the pandemic as companies in general suddenly became aware of the importance of social media for promotion and thus relied solely on this medium to find customers. This reflects the changes to aspects of technical innovation that companies need to make, including creating company websites as well as Instagram and Facebook accounts.

6. Shareholder Return Aspect

The aspect of shareholder return describes the percentage return on loans/capital provided by shareholders for the operation of the company's business activities. At PT XYZ this concerns whether there is a return on the working capital provided by the shareholders. Again, the company occupied different levels for shareholder return before and during the pandemic. The difference reflects the change in the company's financial position, which before the pandemic was at level 2. At this level, the company provided a shareholder return because it had more funds for profits derived from financial developments. During the pandemic, however, the company moved to level 1 due to the decrease in income earned from fewer customers. After deducting operating costs from this figure, no shareholder return was payable during the pandemic.

7. Corporate Image Aspect

The corporate image aspect pertains to the level of public trust in the company. In the context of PT XYZ, this relates to a customer assessment of satisfaction with its business activities. Different levels were recorded for the corporate image aspect before and during the pandemic. Before the pandemic the company was at level 2; here, it had started to consider the direction of the desired corporate image and the steps needed to achieve it. However, during the pandemic, the company moved to level 1 as it considered corporate image to be less important. In addition, customers were already familiar with the service in the business units, so the company chose to shift its focus from the corporate image aspect to other areas.

8. Environmental Aspect

The environmental aspect describes the conditions at the company's place of business. At PT XYZ it relates to how the company pays attention to the business area for the activities carried out. The company was at different levels for the environmental aspect before and during the pandemic. Pre-Covid-19, the target was level 2; here, the company joined environmental organisations in its place of business and engaged in

environmental protection. However, the position changed to level 1 during the pandemic after the company was forced to shift its focus.

It can be seen from **Figure 5.1** that level 3 represented PT XYZ's average risk level before the pandemic (security, business development, and employee relations aspects), while the customer aspect was at level 5, the environmental and corporate image aspects were at level 2, and the technical innovation aspect was at level 1. These differences indicate that PT XYZ considered the customer aspect to be the most important aspect of its business activities before the pandemic and was a determinant of the company's success, with the other aspects supporting the decision-making process. Meanwhile, during the pandemic, level 1 was the average for PT XYZ (environmental, shareholder return, and corporate image aspects), with certain aspects at level 3 (customer and technical innovation) and level 2 (security and employee relations).

These changes in position indicate a shift in the aspects considered most important in decision-making compared to pre-pandemic times. While prior to the pandemic period, the customer aspect was considered the single most important aspect in decision-making, during the pandemic, both the customer and technical innovation aspects played an important role in decision-making. This reflected how during the pandemic, technical innovation helped in determining the level of success from the customer aspect. Technical innovation in the context of this case study concerns the use of social media as a means of promotion, aimed at attracting customers to visit PT XYZ's place of business.

It is therefore known that PT XYZ's risk level before the pandemic was level 3 (cautious) compared to level 1 (averse) during the pandemic. According to Quail (2012), level 3 means that while the company accepts existing risks, it attempts to avoid them whenever possible. At level 1, however, risk is defined as something that must be avoided and is not desirable. This is appropriate given that, before the pandemic, PT XYZ was better positioned in terms of its customers, finances, and employees, meaning it was able to imagine the potential risks and overcome those that occurred. During the pandemic, however, the company faced constraints on its capabilities from all sides; as a result, it sought to avoid all risks arising from its business activities and conducted more mature planning (innovation) related to its operations. One example was its study into the use of social media as a means of promotion.

VI. CONCLUSION

Based on the results of the analysis, it was found that the employees of PT XYZ did not understand risk appetite and how it differs from risk. This shows that PT XYZ employees are not aware of the strengths and weaknesses of the business, resulting in an irrelevant decision-making process. An understanding of the strengths and weaknesses of the business is crucial for every entrepreneur as it simplifies the task of detecting business risks.

In terms of its risk appetite, PT XYZ was at level 3 (cautious) before the pandemic and level 1 (averse) during the pandemic. This difference reflects a shift in the average

company position on the existing criteria as influenced by the change in the company's capabilities before and during the pandemic. PT XYZ possessed stronger capabilities before compared to during the pandemic due to changes in its position in terms of ensuring operational activities could run well. One of the effects of the company's reduced capability during the pandemic was a fall in revenue due to the temporary closure of the business premises and the low level of customer activity, which prompted a workforce reduction and restructuring of the company's debt payments.

VII. RECOMMENDATIONS

Based on the conclusions from the interviews and analysis, the following recommendations can be made:

1. The management of PT XYZ needs to map the strengths and weaknesses of the company and conduct outreach to employees regarding these to ensure a common perception of the company's vision and mission among all members of the organisation. This should assist in delivering an understanding of the differences between risk and risk appetite.
2. Company leaders should provide knowledge of risk appetite to their employees so that the latter have more reliable knowledge and can create more optimal business strategies in line with the company's current conditions. In addition, coordination with the government or local officials is required to request hearings (training) aimed at improving understanding of risk appetite and good business processes among businesspeople (especially MSMEs), thus enabling them to develop effective strategies to achieve the desired business goals.
3. The management of PT XYZ must understand the company's capabilities so that when designing the desired level of risk, it can meet the standards of the existing assessment criteria. If the management is already aware of the firm's capabilities, it could refer to the theory from Quail (2012) to determine the level of risk appetite for use within the decision-making process.
4. Top-level management leaders should commence periodic evaluations linked to the company's risk appetite to determine whether it has adopted the correct risk appetite for the firm's business continuity. Top-level management can conduct joint evaluations every three months and then monitor those evaluations for the ensuing three months whereby monthly assessments (scoring) are performed followed by brainstorming to consider whether the chosen risk appetite is appropriate for the desired goal.

VIII. SUGGESTIONS

In terms of future research, suggestions are made concerning the method chosen to determine the sample size. Samples should be included from more than one research object in the hope that this will generate a picture that more closely reflects the actual conditions of the existing population related to businesses in the MSME sector. Further research may also seek to conduct interviews with regulators to ensure

a more objective analysis that includes an overview from the regulator's side aimed at understanding the roles and difficulties faced in developing businesses in the MSME sector.

ACKNOWLEDGEMENT

The author is grateful to Mrs Dwi Hartanti as the second author who gave her best effort in guiding, checking, and advising this research. Gratitude is also expressed for the research objective, interviewees, Maksi UI, and others who assisted in the research process and ensured that the study was conducted properly and is expected to provide benefits according to the objectives desired.

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