

# Essay on calculating risk

[Business](#), [Management](#)



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## **Question 1**

Net expected value of risks and opportunities

Net expected value is the sum of the product of possible outcomes and the attached probabilities. Therefore, the net expected value of the risks will be the sum of the product of possible risks and the attached probabilities while the net expected value of the risks will be the sum of the product of possible risks and the attached probabilities.

## **Question 2**

Contingency reserve budget based

Contingency reserve budget is an estimate of resources to be set aside by to pay for probable undesired outcomes that may occur. It is computed by estimating the expected net value using the five step approach; list contingencies that are likely to increase costs, estimate the costs of those contingencies, estimate the probability of those contingencies, multiply the

cost of each contingency with its respective probability and lastly, obtain the sum of the products.

### **Step 1: list contingencies that are likely to increase costs**

Step 2 and 3: Estimate the costs and probabilities of those contingencies

Step 4: Multiply the cost of each contingency with its respective probability

Step 5: Obtain the sum of the products

Contingency reserve = \$15, 000 + \$875 + \$250 = \$16, 125

### **Question 3**

How much to allocate for the management reserve

Management Reserve is resources that have been set aside to cater for risks that have not yet been identified commonly referred to as “ unknown-unknowns”. It is not possible to estimate financial impact or probabilities of what we do not know yet. Therefore, management reserve is often given as a percentage of the project cost. In practise, 5 per cent or 10 per cent is commonly used. In this case I will use 10 per cent. Assuming the project will cost \$100, 000, the management reserve will be;

Management reserve = 10%\*\$100, 000 = \$10, 000

### **Question 4**

Assumptions for Contingency reserve

- It is possible to identify the potential factors that may increase the cost of the project.
- It is possible to estimate the financial impact of the plausible factors that may increase the cost of the project.
- It is possible to estimate the probabilities of those factors occurring before

the completion of the project.

- The estimated financial impact and attached probabilities will remain constant during the project.

### **Assumptions for Contingency reserve**

- It is impossible to identify all the factors that are likely to increase the costs of a project.

- It is impossible to estimate the financial impact or probabilities of factors that have not been identified.

### **Bibliography**

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