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Importance of Business Financial Risk Analysis in SMEs According to COVID-19

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Abstract: Enterprise financial risk analysis is essential to ensure a company's stability and economic solvency. It allows the identification and evaluation of possible financial risks to which the company may be exposed, such as market fluctuations, bad debts or internal fraud. By knowing these risks, preventive and corrective measures can be taken to reduce their impact and avoid economic losses. In addition, financial risk analysis also provides a detailed view of the company's financial performance, allowing informed and strategic decisions to be made for its growth and development. This research is based on the importance of business financial risk analysis in Small and Medium-Sized Enterprises (SMEs), a sector that the COVID-19 crisis has threatened. How good risk management, its analysis, proper monitoring and management make these companies remain in the market; therefore, the case of the airline Avianca is analyzed, with the main financial indicators; the interest in the case starts with resilience and of the company, even though Colombia stands out for its lack of firm resilience and how it reacted to moments of uncertainty caused by mismanagement in temporary situations such as the pilots' strike of 2017 or the current COVID-19 pandemic.

Keywords: Financial Statements; Risks Companies; Analysis Management; COVID-19 Pandemic; Small and Medium-Sized Enterprises (SMEs); Airline Avianca; Financial Indicators.

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1. Introduction

Financial risk analysis is a comprehensive assessment of economic, financial and market factors that could adversely affect a company's or investment's profitability. This analysis identifies potential risks and develops strategies to mitigate them. Financial risks can include market volatility, interest rate, exchange rate, inflation, worsening economic conditions, regulatory and political changes, and company-specific factors such as debt exposure, solvency and liquidity. Various tools and methods can be used to perform a financial risk analysis, including SWOT (Strengths, Weaknesses, Opportunities and Threats) analysis, credit risk analysis, financial ratio analysis, etc. Once the financial risks have been identified, strategies can be proposed to manage them, such as diversifying sources of income, reducing operating costs, obtaining financing on favorable terms, etc. Monitoring the company's financial position to identify and manage these risks is also important. It is also important to constantly monitor economic and financial factors to update the analysis and financial risk management strategies.

The importance of financial risk analysis is reflected in the selection that you want to make when starting or sustaining a business because Colombia and other countries are currently going through a major financial crisis due to COVID-19, where

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companies have been highly affected in the development of their activities, creating greater financial risks and few possibilities of solution; since within the measures that the government adopted to mitigate the pandemic it decided to close the trade, which paralyzed business activities causing a financial imbalance; when we hear or see the word risk, we associate it or understand it as a misfortune or misfortune that can happen, but not necessarily, since the risk is also an opportunity to face something different, many companies have shown resilience and show it by reorienting their markets.

Financial risk is the probability of an event with negative financial consequences for an organization. According to this, the financial risk would be negative events for the entity, such that if it does not act efficiently, it can seriously harm the company. This must be understood as the causes for which the business or investment is not successful, any organization regardless of its size seeks growth and positioning in the market; nobody invests knowing that they are going to lose, but if the pertinent previous studies are not carried out, the percentage of failure would be high. It is about seeing the economic future, something like financial gods. Anticipating events ensures being prepared to mitigate or prevent future damage in the event of an event occurring, and it is clear that the higher the profitability, the higher the risk; these two variables are directly proportional, and there is no low risk when the expected return is high.

Around the world, small and medium-sized companies make up most of the business fabric in numerical terms. In Colombia, "around 94% of the business system is made up of SMEs, which, being the engine of the economy, do not have the importance or the necessary support to survive over time, although this image has already begun to change. During “the last governments, policies have been established to promote the development of these companies through credits and other types of aid.

Despite the state's efforts to activate the economy and support entrepreneurship, starting a project today is difficult; but it is even more difficult to keep it going; you must know the environment, what factors condition the investment, the type of market, population, politics, laws, geographical location, all this and more influences the development of the business. Now for the current situation, we are going through due to the COVID-19 crisis, sustaining it becomes even more difficult and almost impossible.

2. Importance of business financial risk analysis

Risk measurement and management began when companies found themselves in dangerous situations that harmed their financial stability, where they did not have the knowledge or ability to act against them. In companies or organizations, it has taken on great importance after episodes of crisis presented in the eighties and nineties. These events evidenced the need to implement how to measure and manage risks, a practice carried out in most organizations today.

Vargas [3] establishes that the first probability studies were developed in the 16th century during the Renaissance. Girolamo Cardamo (1500-1571) where in the "Book of your Life," his fondness for games of chance is told, through which he carried out multiple probabilities analyzes. This shows that risks have existed for a long time, where probability was discussed in everyday situations, such as games of chance. He also mentions in 1930, the main tool for risk analysis in companies was the balance sheet, which by itself does not reflect permanence over time or what is known under the principle of continuity or business going on." Based on this, it can be said that with this tool, it is possible to know if a business can remain over time according to its present risk capacities. The following author Haro [1], mentions that the word risk comes from the Latin ricercare, which means dare or walk a dangerous path. They have a negative meaning related to danger, damage, sinister or loss.

However, risk is an inevitable part of general decision-making processes and investment processes. In finance, the concept of risk is related to the potential losses that may be suffered in an investment portfolio. Taking this into account, it is understood that risk is not always a misfortune, but showing a dangerous way to cross an obstacle, because some may inevitably occur. Likewise, Gómez [20] presents that risk is linked to uncertainty about future events, and it is impossible to eliminate it. Given this, the only way to deal with it is by managing it, distinguishing the sources from which it comes, measuring the degree of exposure that is assumed, choosing the best available strategies to control it, and knowing the degrees of vulnerability one has. Uncertainty and risk are part of the reality faced by individuals, companies and countries.

According to Gómez [20], it is not about the risks that are seen at the beginning of investment; these are all that may arise, there may be great uncertainty, but it is about trying to identify those that are most likely to occur, for example, If the company is engaged in activities with a high risk of accidents, it must insure its employees against them, thus ensuring that the company or its finances are not affected if the accident occurs and guarantees the well-being of its employees, this in terms of risks labour.

The same happens with financial risks, and if these are considered when starting the investment, a way will also be found to mitigate them in case of a problem. After this, it is possible to identify the importance of risk; therefore, the importance is observed according to the fact that companies have always lived with risk since its genesis they give the reason in his presence, they manage it and get ahead. Risk management, therefore, has become an issue of vital importance, almost as seen, in the conjuncture, as a profession, given the large set of terms used in many areas. Regarding this, the importance of financial risks is immersed in various areas. It can be spoken of as such in a profession because it is a situation in which entrepreneurs or people who are going to start or maintain a project or an idea of business are vulnerable to how they should manage these risks and what they need to move forward according to the pertinent analyzes that are carried out.

3. Financial crisis due to COVID-19

Despite the efforts of the Colombian government to maintain social welfare at this time, when the number of infections and deaths caused by the pandemic was increasing, the preventive isolation measure at the time was the most appropriate decision that was chosen. FUSADES [19] directs that less than three months after the outbreak of the COVID-19 virus in China, the epidemic has spread throughout the world and has severely affected the largest economies, dragging them towards a deep and transitory economic recession that will add to the human suffering generated by the health crisis; Consequently, state that we are facing a moment in which decisions must be made quickly.

Economic measures are required as never before to limit the economic consequences of the pandemic on people, starting with the most disadvantaged. This measure largely controlled the spread of the virus and managed to minimize the impact. Still, a financial crisis was also unleashed in which the population was increasingly concerned about meeting the preventive measures of staying locked up. Tobías and Fabio, [21] Mentions that the authorities should act firmly to contain the consequences of COVID-19 and prop up the flow of credit to companies. Lor was not taken to a good extent in the case of small and medium-sized companies, they were not in a position to sustain and meet their obligations under these circumstances, and many of them were forced to liquidate their companies.

Also, Frieden [4] observes that every government faces difficult decisions when taking the appropriate measures: what restrictions to impose and when to relax them, where the money will be spent and how it will be collected, and what national issues can be imposed. Limited to favour international cooperation. Likewise, the crisis with the risk that is being presented against decision-making, adequate analysis and being able to face future situations such as it presents [5]. To combat the pandemic, they have combined drastic public health interventions with fiscal measures amounting to around USD 8.7 trillion, thus observing the amount of cash that simply the health sector may need, which is the most vulnerable and with higher risk today to combat the pandemic.

As governments launch large-scale fiscal programs to counter the pandemic, it is important to understand the economic landscape over the coming years and decades. Therefore, they will be affected by foreign trade since the presented situation involves many financial risks. Likewise, Sayeh and Chami [6] comment that this pandemic presents an even greater threat to countries highly dependent on remittances than previous economic crises. This means that despite the efforts made by governments, the risk remains and becomes greater each time. NU ECLAC [15] shows that Latin America and the Caribbean are facing the pandemic from a weaker position than the rest of the world. Before the pandemic, ECLAC forecasted that the region would grow by a maximum of 1.3% in 2020.

However, the effects of the crisis have led to changes that forecast and forecast a drop in GDP of at least 1.8%. Thus, the financial risks are greater since what was expected to be obtained has changed drastically until it was negative and influential in market positions. Cosio [18] positions that "volatility has skyrocketed, in some cases to levels last seen during the global financial crisis, amid uncertainty about the economic impact of the pandemic. With the uptick in volatility, market liquidity has deteriorated significantly, including in markets traditionally considered deep, such as the US government bond market, contributing to wild asset price movements." This is crucial on the affectation of the entities in the different types of countries, showing a great change in the markets, thus making it difficult, the exits and entrances of the same, according to the processes that must be developed to avoid the deterioration of the market and continue with the same price movements towards the assets and not their decrease.

This crisis that we are going through and that it is not known for sure when it will end is something that was never foreseen by any government and even less by any company, so much so that when it started in China in December 2019, it was not believed that it would come out and would affect other countries, but the reality is different. Companies have been forced to close and liquidate their employees. The ones that have suffered the most are the small and medium-sized companies, those that, for their operation and investment, had high debts and other obligations they could not cover. Although risk management is essential, in these circumstances, it would be thought that no power or strategy can mitigate the overwhelming impact that the pandemic is leaving behind; but it's not like this crisis.

4. Types of financial risks and financial indicators

Knowing the types of financial risks is necessary when carrying out a risk assessment, even though you must first have the tools you want to use and thus be able to carry out the methodology and observe what type it belongs to Citing Quijano et al., [16], they establish the most important risks as:

- Market risk (variations in price changes)
- Credit risk ("variations deriving from the possibility that the counterparties refuse or are unable to comply with them

4.1. Contractual Obligations

- Legal risk (sudden regulatory changes, lawsuits)
- Fiscal risks (fiscal cost of hedging operations)
- Accounting risks (distrust that the financial reports do not reflect the financial position, the results of the operation, the variations in the capital, as well as the use and application of resources due to not properly using the accounting regulations or specific legislation of which risk management will make use of)

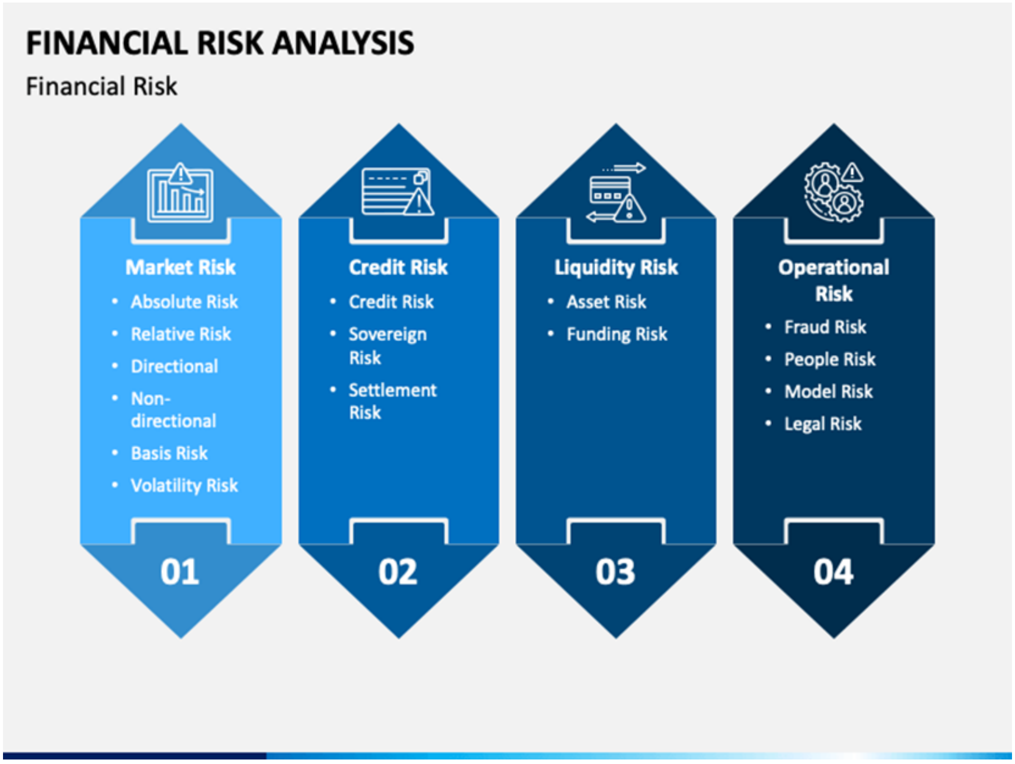

Figure 1: Financial Risk Analysis [13]

Accordingly, risks represent something important for business due to issues on which action is often not achieved, leading to failure itself. However, these risks can be mitigated by trying to prevent them and thus eliminate them (fig.1). Thus, it is clear that Carvajal and Escobar [2] present different types of tools to identify risks, such as Structured interviews with experts in the area of interest. Meetings with managers and people at all levels in the entity. Individual evaluations using questionnaires. Brainstorming with the entity's servers. Interviews and inquiries with people outside the entity. Use flowcharts. Scenario analysis. Make periodic reviews of economic and technological factors that may affect the organization. Likewise, these tools work to better understand financial risks and be able to act against them to mitigate them.

4.2. Main financial indicators to determine risks

The most common indicators to determine financial risk are used according to the short term in which entities can cover their obligations, and the indicators are liquidity, indebtedness and portfolio management.

4.3. Current ratio liquidity formula

Current ratio = Current Assets / Current Liabilities

borrowing formula

Debt Level = Total Liabilities / Total Assets
Formula for portfolio management
Portfolio turnover: (Accounts receivable x 360) / Sales

For Aristizábal [17] the current ratio, "it can be deduced that the higher the value of the index, the better for the company, and it is considered good if it is greater than or equal to 1" likewise for the level of indebtedness "the appropriate proportion of indebtedness for a company cannot be easily defined since many factors influence this decision to determine it. For example, in 1975 in Colombia, there were debt levels of 50%". Also, in turn, that portfolio turnover "In this indicator, errors may occur according to the seasonality of sales, since in a certain period, depending on the type of company, the values of accounts receivable may be very high or very low." In turn, a general remuneration is expected for the 60-day portfolio.

This specifies how it can be observed when an entity is at risk according to the financial indicator used. Thus, it can conclude the management of the situation that arises to support those areas and avoid remaining at financial risk. These indicators are used in a pertinent way to observe the results and act effectively (table 1).

Table 1: Financial Indicators [12]

Measure	**Ratio/Indicator**	**Norm**[1]
Profitability		
Rate of return on assets (ROA)	Return on farm assets[2]/Average farm assets	Exceed real interest rate
Rate of return on equity (ROE)	Return on farm equity[3]/Average farm equity	Exceed ROA
Dividend return	Dividend payment/Share price	>0
Liquidity		
Current ratio	Current assets/Current liabilities	>1
Interest coverage ratio	Return on farm assets[2]/interest paid	>1
Solvency		
Debt/Asset ratio	Total liabilities/Total assets	<0.3-0.5
Leverage	Total liabilities/Farm Equity	<1
Growth	Absolute & relative change in share value[4] over period	Should be monitored over time
Workers' total return	Dividends, capital gains, wages, and other benefits & interest received by workers	Should be monitored over time

[1]Norms were taken from [9]; [10]; and [11].
[2]Net farm income from operations (excludes interest, tax, rental payments, and salary paid to management) + other net income from farm assets before tax [10].
[3]Net farm income from operations – (interest + rental payments + salary paid to management) + other net income from farm assets before tax [10].
[4]Net asset value/Total number of shares issued.

5. State loan to the airline Avianca

The present case is presented about the entity Avianca Holdings [8], which provides air transport services to carry loads of merchandise and people to obtain income; it is a for-profit entity that remains time under these services. It has an office in Colombia and, likewise, through the crisis that has been occurring due to the pandemic caused by COVID-19, it has found itself in a delicate situation, leading to the dismissal of many workers and a decrease in the number of employees. The provision of services due to the temporary closure of its activities, in turn, has greatly impacted obtaining income, thus managing to encounter a financial risk. To carry out this financial risk analysis, the comparative financial statements (December 2019 - June 2020) presented on August 2012 were taken, thus applying the main financial analysis to specify an opinion on whether the entity is at risk.

5.1. The beginnings of AVIANCA, the airline of Colombia

More than 100 years ago, on December 5, 1919, this airline was founded in Barranquilla; its initial name was Colombian German Air Transport Society (SCADTA). That day began the path that today has Avianca as a key airline in Latin America. With a somewhat timid beginning, today it is a giant in the air transport industry; today, Avianca is the second oldest airline in the world, only a few months younger than the international KLM (Royal Dutch Airlines). The first flight of this Colombian airline was made without passengers since the purpose was to dispatch some letters between Barranquilla and Puerto Colombia. This flight was made with a Junker F-13 aircraft. However, great challenges would come later for this airline, such as the first commercial flight with passengers from Barranquilla. This flight followed the Magdalena River, lasted eight hours and had four emergency landings. In the mid-1920s, SCADTA inaugurated its first international routes to the United States and Venezuela, its most attractive markets then.

5.2. Changes in AVIANCA during the Second World War

As a result of World War II, the German partners were forced to leave Colombia, resulting in the sale of the company to the American airline Pan American. Strategically, SCADTA'S new shareholders agreed to a merger with Colombian Air Service (SACO), a competing company. The product of the merger, sealed on June 14, 1940, was called National Airways of Colombia, thus beginning the history of AVIANCA in Colombia and its current name. Thus began a great period of expansion. The main destinations were the United States and Europe, aboard the best aircraft. At that time, there were acquisitions of iconic aircraft such as the Super Constellation 1049L and the Boeing 720, and the honour of being the first Latin American airline to operate a Boeing 737 in the 1970s and a Jumbo 747 in the 1980s. Thus, from the beginning, Avianca would set out to be an airline at the forefront, being up to date with technological advances and willing to adopt them in the service of its customers.

5.3. Avianca Holding S.A.: The Modern Era

The events that took place in the USA in September 2001 meant for Avianca sought the growth and consolidation of the company; in addition, during the crisis that commercial aviation was going through at that time, its directors decided to merge with SAM and ACES, thus creating the Summa Alliance. However, in 2003 the company took another turn when it decided it best to consolidate the Avianca brand. Sometime later, a Brazilian businessman bought 75 percent of Avianca's shares for US$64 million, according to the company (fig.2).

Figure 2: Avianca Holding S.A. [14]

Figure 3: Travel route [14]

The financial crisis significantly affected Avianca, one of Latin America's most important airlines (fig.3). The Colombian company suffered a decrease in revenues and an increase in operating costs due to the devaluation of local currencies, the fall in demand and competition from other airlines.

2017 Avianca reported more than US$200 million in losses due to route cancellations, low demand and higher fuel prices. In addition, the company had problems in its relationship with workers' unions, which led to strikes and flight delays.

However, despite the financial crisis, Avianca has managed to stay afloat thanks to its strategy of expansion and consolidation in new markets and its alliance with other airlines such as United Airlines and Copa Airlines. The company has also implemented cost-saving measures and restructured its operations to improve profitability and efficiency.

Calculation and financial analysis of the comparative financial position statements (December 2019-June 2020) of Avianca Holdings [8].

Current ratio: Current assets / Current liabilities

$$Current\ ratio\ December\ (2019){:}\ \frac{1.711.276}{2.732.150}\ Expressed\ in\ thousands\ of\ USD$$

$$Current\ ratio\ December\ (2019){:}\ 0.62$$

$$Current\ ratio\ June\ (2020){:}{:}\ \frac{925.032}{4.952.510}\ expressed\ in\ thousands\ of\ USD$$

Current ratio June (2020):0.19

Through these results and applying what is established in the current ratio for the period between December 2019 and June 2020, being less than 1, the entity is at great financial risk since, in the December period, it corresponds to 0.62, this means that it covers a little more than half of the debt to third parties that are held in the short term, but with the affectation through COVID-19 when observing in June 2020, it can be appreciated that it has dropped considerably and its debts have increased; therefore the result obtained is 0.19, which means that it is not possible to cover even a quarter of what is owed in the short term to third parties, thus generating a great financial risk is:

Debt Level = Total Liabilities / Total Assets

$$Level\ of\ indebtedness\ December\ 2019{:}\frac{7.268.743}{7.273.910}\ Expressed\ in\ thousands\ of\ USD$$

$$Level\ of\ indebtedness\ December\ 2019{:}\ 99\%.$$

$$Level\ of\ indebtedness\ June\ 2020{:}\frac{6.928.536}{6.573.153}\ Expressed\ in\ thousands\ of\ USD$$

level of indebtedness June 2020:105%.

When analyzing the results, according to what is established on the indebtedness index, it is observed that the entity has borrowed up to 99%, which means that with its total assets, it is barely able to meet the needs of its third parties, being this causal to financial risk. Visualizing the same through what has happened due to the COVID-19 pandemic, it is presented that as of June 2020, the result of the level of indebtedness is 105%, which exceeds its payment capacity through its total assets, being. This is a high financial risk because it will not be possible if you want to borrow more due to its high rate.

Portfolio turnover: (Accounts receivable x 360) / Sales

$$Portfolio\ turnover\ December\ 2019{:}\frac{(237.070 * 360)}{2.266.805}\ expressed\ in\ thousands\ of\ USD$$

$$Portfolio\ turnover\ December\ 2019{:}\ 37\ Days$$

$$Portfolio\ turnover\ June\ 2020{:}\frac{(175.125 * 360)}{1.180.297}\ expressed\ in\ thousands\ of\ USD$$

Portfolio turnover June 2020:53 days

According to the results obtained, it can be concluded that the days for the portfolio rotation according to the sales made for December 2019 were 37 days, which does not represent any risk since it has a good rotation as is mentioned about portfolio rotation. Still, growth can be observed when presenting the result of the June 2020 period where the pandemic had already taken place, which was 53 days, greatly increasing the days of portfolio rotation. This shows, then, how the decrease in flights increased credit sales to obtain this income and thus reduce the financial risk present due to their lack of them [11].

There is currently a great controversy over the decision made by the government to grant a credit of 370 million dollars to the renowned airline Avianca; the country's economy is going through a general crisis, and most companies are at risk of bankruptcy; Why does the state decide to make such a big effort to support only this one? With this amount, it could help many Colombian companies, but this and many other doubts are generating disagreement in the country; In interviews carried out by Semana magazine, Vice Minister of Finance Juan Alberto Lodoño states that the decision is made to guarantee connectivity and reactivate trade and tourism. According to the Vice Minister, the interest applied to this credit is a market interest, it is that is, it is higher, and the term is 18 months, which, once this time has elapsed, must be cancelled; the government takes all the necessary guarantees to ensure payment. What the state is looking for is for Avianca to continue operating and to continue providing the service to the country. The vice minister mentions that the resources must be allocated to guarantee the company's operation during this period; it will not be able to cover previous obligations. He tells the official that all necessary measures have been taken to guarantee payment. This decision generates many doubts and reports; Avianca is not a Colombian company, and this company has air routes where it provides the transportation service, but the airspace belongs to the Colombian state, which means that if it is not AVIANCA, it could be another airline that provides this service. They would have been able to open a tender and have another company operate in the country and cover the routes that Avianca currently owns; On the other hand, there is also a concern because the private banks did not grant him the credit.

In the consolidated financial statements issued by the company on August 12 of this year, they confirm in conclusion that they are bankrupt, the same information reflected in their figures, about which they deal with about US$353 million for equity deficit; likewise, their liabilities reflect figures not very encouraging, and that shows a key factor for the sustainability of the organization, data that are not guarantors to access a loan of this magnitude. Doubts and disagreement increase when verifying that the company has requested US support. Why didn't this country give you monetary support? Did the company not meet the requirements that guaranteed the return of the credit? Why did Colombia grant such financing? Is Colombia less conditional on approving and granting this type of credit? What guarantee did Avianca offer Colombia different from the one offered to the US? In turn, the guarantees presented are not too many since presenting such a high deficit and seeing the risk of keeping the business going, a different feasible guarantee on the payment of liabilities is not implied. So, it is not clear where it is specified in the case of non-payment what collection opportunities there are if the entity cannot settle its debts or with all its assets. Since by presenting such a high deficit and seeing the risk of keeping the business going, a different feasible guarantee on the payment of liabilities is not implied. So, it is not clear where it is specified in the case of non-payment what collection opportunities there are if the entity cannot settle its debts or with all its assets. Since by presenting such a high deficit and seeing the risk of keeping the business going, a different feasible guarantee on the payment of liabilities is not implied. So, it is not clear where it is specified in the case of non-payment what collection opportunities there are if the entity cannot settle its debts or with all its assets.

6. Conclusion

Financial risks present a great challenge to companies when they appear; therefore, when situations occur, it can be observed how different entities manage to assume these challenges and look for different ways to mitigate the risk or turn it in their favor, as has happened with the pandemic caused by COVID-19. Showing how some large entities have fallen for these financial risks and have shown their ignorance of this situation, looking for a way to sustain themselves and continue to be a going concern, even if their financial situation is affected. It is necessary to take into account the types of financial risks, even though entities are often not advised or do not perceive that these risks may occur, managing not to comply with the measures in time to take precautions about them and thus avoid a great extent the impact they bring. The application of a case shows the importance of what should be taken according to the financial risks; if you can keep a business going or go bankrupt since the risks are so high, it also presents a way of opportunity to analyze the different aspects that lead to companies not abiding by the risks. Still, it is worth noting if SMEs ever foresee and mitigate their risks so that they can cope with them well. The COVID-19 pandemic has significantly affected the global economy, which has generated a high level of uncertainty in the financial market and has led to the need for financial risk analysis to make appropriate financial decisions and mitigate the risks associated with market volatility. This situation has led companies to re-evaluate their investment and financing strategies and consider factors such as liquidity, solvency, profitability and indebtedness in their risk analysis to face economic uncertainty in times of crisis. In this regard, companies need to consider financial contingency measures, proper cash flow management and investment diversification to protect their assets and ensure their continuity in the market. In summary, financial risk analysis is a critical tool that enables companies to face future challenges effectively in times of economic crisis, such as the current COVID-19 pandemic.

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