Risk Management – Pure Risk and Speculative Risk Explained

Risk management is a relatively new and evolving field. Risk management usually refers to the process of identifying, measuring, controlling, and minimizing uncertainties which may directly or indirectly affect a desired outcome of a system. A great challenge indeed.

Any process or procedure we can think of holds many uncertainties. Risk management tries to identify these uncertainties, assign probabilities and possible harm to each and every one and acts to minimize those risks.

Two of the most basic terms used by risk managers are pure risks and speculative risks. All risks are historically associated to one of the two families. Understanding the motivation and reason behind this differentiation is key to taking your first steps in risk management.

Every risk is at its base a known series of possible outcomes with possible benefits or harms. Each possibility has a known probability of realization (otherwise it is not a risk but an uncertainty and is dealt with differently).

Pure risks are a family of risks in which all possible outcomes are harmful in some way. In other words a pure risk is a situation that can only end in a loss. For example, the risks of an accident, a car theft or earthquake are pure risks.

Speculative risks on the other hand are a family of risks in which some possible outcomes are beneficial. In other words a speculative risk is a situation that might also end in a gain. For example, the risks of stock investment or business venture are speculative risks.

This differentiation between families of risks is very important as each family has its own distinct features. Pure risks are characterized by the following:

1. Small chance of occurrence – The probability associated with risk occurrence is small.
2. Grave results – In case of risk occurrence the results are significant.
3. Instant impact – The impact of risk occurrence is instant.

Let's reconsider pure risks such as an earthquake, a car theft or an accident. These risks have a relatively small chance of occurring, all have grave results and their impact is instantaneous.

Another less mentioned but very important characteristic of pure risks is the fact that these risks do not present themselves due to the small chance of occurrence. There are virtually endless amounts of pure risks around us. One can come up with infinite pure risks by thinking of every process. A boulder might roll on to you when you brush your teeth. Sure, there's a small chance that might happen, but it's there. We overlook pure risks because of those small chances.

Speculative risks are basically all other risks. These risks are dynamic and changing (pure risks are more static due to their nature). Speculative risks have been traditionally dealt with in the confines of financial management. Modern risk management deals with these kinds of risks as well, as their impact might be as significant as that of pure risks.

We invite you to learn more about our approach and how it can benefit the processes and bottom line for your business. Simply contact us at:

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to get started.