Risk or Uncertainty: Which Is Better to Face?

Many successful entrepreneurs recognize the importance of taking risks to build a successful business. And, on a couple of levels, that makes sense: If you choose a risky business model when no one else does, you'll face less competition. And, if you fail, you can always try again.

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On top of that, higher financial risks often come with higher rewards, meaning that a successful attempt at a risk is met with a higher payoff.

Still, though, it's important to understand that "risk" may not be the best concept for prospective entrepreneurs to consider — instead, it might be better to consider a similar, yet distinct idea: *uncertainty.*

Risk vs. uncertainty

If you're using the terms loosely, you might conflate the ideas of "risk" and "uncertainty" — since both relate to an engagement with an unknown potential outcome. But, as described in a nearly century-old book, *Risk, Uncertainty, and Profit*, by economist Frank Knight, risk and uncertainty are distinct, and it's important to understand why.

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"Risk" refers to a known distribution of probabilities. For example, if you roll a six-sided die, you know that your result of getting any single number within that range is approximately 1/6. If you roll three dice, you can calculate the specific odds that you'll get the same number, say, "5,"

on each of the faces (1/216). Rolling those dice will be a *risk* because you'll *know* what your chances of being successful are.

"Uncertainty" also refers to a distribution of probabilities; but with uncertainty, the *distribution* is what's unknown. Using the dice example, this will be akin to volunteering to roll an unknown number of dice, with an attempt to get three 5s showing by the end of the roll. If you start with 100 dice, this is highly likely to happen; but if you start with one or two, it's impossible. Signing up for this bet wouldn't be a risk – it would be an example of *uncertainty* in action.

Business applications

There are many types of risks in business, but most of them share a common architecture. For example, you might debate whether to start a new business in a previously existing category by understanding the success rates of similar businesses, and calculating customer demand in your target area.

But, for a business to be an uncertain move, it has to create a new category, or else move into a niche with so many unknown variables that its risk can't be calculated in any objective way. In the world of marketing, you might think of the difference as targeting keywords that already have a high search volume versus targeting new subjects and phrases you think your target audience would employ.

Why risk is inferior

I began this article by suggesting that risk was inferior to uncertainty, but what makes this the case?

If you know it, they know it. As an entrepreneur, you're going to be dealing with other entrepreneurs who are more

experienced, smarter and wealthier than you are. If it occurs to you to calculate a potential risk, chances are, they've already thought of it and calculated it more accurately. Think of this as mutual knowledge; you both know the objective probability associated with a risk, and are likely unwilling to pay more than its "true" value. Accordingly, you have no real advantage in a risk-based scenario.

Uncertainty has more possibilities. Uncertainty, because it deals purely with true unknowns, simply has more possibilities. Uncertain actions, rather than risky ones, tend to be more innovative and original, opening up entire new categories rather than capitalizing on what's already there.

Risk isn't as calculable as we think. It's important to understand that risk isn't nearly as calculable as we think it is. We tend to overestimate our ability to assess risk, due to a well-established cognitive bias known as the overconfidence effect. Uncertainty embraces the unknown, rather than placing too many bets on a risk-based model that is likely to be inaccurate.

Uncertainty has less competition. Finally, consider the real "fear" factor in probabilities: the unknown. Many people are willing to take risks, but not many people are willing to take on the unknown. That means there's going to be less competition for you when you venture into a realm of uncertainty, and more if you try to take a calculated risk.

The more you know about a situation, the better, but some of the most successful entrepreneurs are ones with less shared information to begin with. Speculating on unknown variables, whether they occur in the context of a new, innovative category, or a peculiarity of your target market that can't be pinned down, has massive potential for success.

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At the very least, you'll have fewer competitors to worry

about in the meantime.https://www.entrepreneur.com/article/306263