SOME IMPORTANT CONCEPTS

TI &RM Chapter 5 part 1

Q: 1 Risk Exposure Analysis primarily refers to the assessment and evaluation of___________.

a) Employee performance

b) Market competition

c) Potential risks a bank may face

d) Customer satisfaction

Q: 2 Why is understanding and managing risks crucial for a bank's stability and success?

a) To increase marketing budget

b) To reduce operational costs only

c) To ensure financial stability and growth

d) To simplify regulatory compliance

Q: 3 A periodic overview of risk exposure by which parties is considered necessary?

a) Junior staff members only

b) External auditors

c) The Board and senior management

d) Individual traders

Q: 4 What has RBI introduced to provide market participants a tool to transfer and manage credit risk in an effective manner?

a) Credit Cards

b) Credit Default Swaps

c) Debit Cards

d) Personal Loans

Q: 5 What are the two types of liquidity risks banks face in their trading activities?

a) Credit risk and operational risk

b) Legal risk and market risk

c) Interest rate risk and compliance risk

d) Risk related to specific products/markets and overall funding risk

Q: 6____________ is a process where financial institutions evaluate how their portfolios or systems would perform under adverse conditions, such as economic downturns or market shocks.

a) Performance Evaluation

b) Financial Auditing

c) Stress Testing

d) Market Analysis

Q: 7Which of the following is NOT a direct benefit of stress testing?

a) Identifying potential risks.

b) Measuring the impact of adverse events.

c) Guaranteeing a profit every quarter.

d) Ensuring institution resilience.

Q: 8Which of the following characteristics best describes a Simple Sensitivity Test?

a) It identifies the most damaging combination of market risk factors.

b) It assesses the impact of large movements in financial variables on portfolio values without specifying their reasons.

c) It formulates scenarios based on historical events common across portfolios.

d) It primarily uses statistical theory on low frequency, high severity.

Q: 9 What is a limitation of the Simple Sensitivity Test?

a) It is too complex to run quickly.

b) **It lacks historical and economic content**.

c) It can only be used for long-term decisions.

d) It requires extensive data analysis.

Q: 10 Which stress testing technique involves identifying a portfolio's key financial drivers and formulating scenarios where these drivers are stressed beyond standard VaR levels?

a) Simple Sensitivity Test

b) Maximum Loss Approach

c) Scenario Analysis

d) Extreme Value Theory (EVT)

Q: 11 The core idea behind the "Maximum Loss Approach" is to assess portfolio risks by focusing on___________

a) The average performance of all market factors.

b) The least volatile financial variables.

c) Historical events with minimal market impact.

d) The most potentially damaging combination of moves of market risk factors.

Q: 12 Extreme Value Theory (EVT) is a statistical theory specifically concerned with the behavior of events that are____________.

a) High frequency and low severity.

b) Low frequency and high severity.

c) Always predictable and easily quantifiable.

d) Related only to daily market fluctuations.

Q: 13 The Asian financial crisis of 1997 and the Russian default of 1998 are given as examples of historical scenarios used in which stress testing approach?

a) Simple Sensitivity Test

b) Maximum Loss Approach

c) Extreme Value Theory (EVT)

d) Standard VaR calculation

Q: 14 Which of the following are qualities of effective stress tests ?

1. They should be relevant to the current position/situation.
2. They should ignore changes in market rates for simplicity.

3. They should consider market illiquidity
4. They should consider the risk in aggregation in an integrated manner.

a) 1, 2, and 3 only
b) 1, 3, and 4 only
c) 2, 3, and 4 only
d) 1, 2, 3, and 4

Q: 15 The "Exposure Document" is designed to contain information about a bank's existing exposures to which of the following risks?

a) Human resource risks only
b) Market, credit, and liquidity risks
c) Operational and legal risks exclusively
d) Reputational risks and public relations issues

Q: 16 Which of the following bodies is responsible for discussing and approving the organizational format for managing and controlling a bank's overall risk exposure?

a) The Risk Manager
b) Internal Audit
c) The Board of Directors
d) Individual Branch Managers

Q: 17 Which of these is a role of risk manager in risk management ?

a) On-going management of exposures, directing the various units involved in managing the bank's financial instruments.

b) Making recommendations to the board of directors and management on all matters related to exposure management.

c) Regulating, monitoring, reporting, and controlling procedures for matters related to exposures management.

d) All of the above

Q: 18 RBI's new Risk Based Supervision (RBS) system aims to improve risk management by__________.

a) Replacing all existing risk assessment tools with a single automated system.

b) Focusing on present and future risks to identify incipient problems and facilitate early corrective action.

c) Eliminating the need for banks to maintain their own internal audit departments.

d) Strictly increasing the amount of capital banks must hold regardless of their risk profile.

Q: 19 If a bank holds a significant amount of foreign currency without having entered into any derivative contracts or offsetting transactions to protect its value against exchange rate fluctuations, this scenario best describes________.

a) A hedged position

b) A closed position

c) An open position

d) A balanced position

Q: 20 Who among the following foreign exchange market players are typically "speculating on market direction" and "not hedging?

a) Dealers

b) Institutional Traders

c) Retail Traders and Advanced Traders

d) Government Agencies

Q: 21 In the context of foreign exchange, what is the primary role of "Dealers"?

a) To engage in long-term investment strategies for pensions.

b) To act as market makers, setting prices and putting together trades.

c) To manage the import/export accounts for large corporations.

d) To provide educational resources for new traders.

Q: 22 When a bank is ready to buy a foreign currency, the rate it offers is known as the_________.

a) Ask Rate

b) Offer Rate

c) Bid Rate

d) Spread

Q: 23 If the price quote for EUR/USD changes from 1.3085 to 1.3150, what does this indicate?

a) The Euro is depreciating against the US dollar.

b) The US dollar is appreciating against the Euro.

c) One Euro is now worth more US dollars.

d) The spread has decreased.

Q: 24 The "Ask/Offer Rate" is the rate at which a bank is ready to_________.

a) Buy a foreign currency.

b) Set a fixed exchange rate for a year.

c) Sell a foreign currency.

d) Calculate the spread.

Q: 25 ____________ is the difference between the bid (sell) price and the ask (buy) price of a financial instrument, such as a currency pair, stock, or commodity.

a) Margin

b) Commission

c) Spread

d) Premium

Q: 26 Calculate the spread given the following: Bid Price = 1.3000, Ask Price = 1.3005.

a) 0.0005

b) 2.6005

c) 0.0005

d) 1.3000

Q: 27 What is the primary purpose of "closing out a position" in trading?

a) To open a new trade immediately.

b) To increase the overall risk of a portfolio.

c) To hold an asset indefinitely.

d) To exit an existing trade by reversing the initial transaction.

Q: 28 Which of the following actions constitutes "closing out a position"?

a) Buying a new asset to add to the portfolio.

b) Increasing the leverage on an existing trade.

c) Transferring an asset to a different account.

d) Selling a previously bought asset or buying back a previously sold asset.

Q: 29 A "Stop-Loss Limit" is best described as a tool used for___________.

a) Maximizing potential profits on a trade.

b) Automatically entering a new trade when certain conditions are met.

c) Limiting potential losses on a trade by triggering an automatic exit.

d) Predicting future market movements with high accuracy.

Q: 30 What action is typically required when a bank's "yellow" limit is violated in Stop-Loss Limits ?

a) Immediate hedging of the position.

b) Management is simply informed of the loss situation.

c) The position is automatically closed out.

d) The trader must report on the situation's cause and propose a plan for dealing with it.

Q: 31 In a bank's system of violation triggers, which type of limit would necessitate immediate hedging of a position?

a) Green limits

b) Yellow limits

c) Red limits

d) Blue limits

Q: 32 Which of the following are stated limitations of stop-loss limits?

1. They measure single-period market loss retrospectively.
2. Stop-loss limits may not consistently indicate risk
3. They are too complex and difficult for non-specialists to understand.
4. It is challenging to hold traders accountable for specific losses incurred.

a) 1, 2, and 3 only

b) 1, 2, and 4 only

c) 2, 3, and 4 only

d) 1, 2, 3, and 4

Q: 33 Which of the following are benefits of stop-loss limits?

1. They offer simplicity and convenience in their implementation.
2. They are easily understandable by individuals without specialized financial knowledge.
3. They provide precise accountability for every isolated loss incurred by traders.
4. A single risk metric, the stop-loss limit, can be consistently applied across various levels of the organization's hierarchy.

a) 1, 2, and 3 only

b) 1, 3, and 4 only

c) 2, 3, and 4 only

d) **1, 2, 3, and 4**