RISK ANALYSIS AND CONTROL

TI &RM Chapter 10

Q: 1In the context of treasury operations in financial institutions, the overall risk profile is broadly divided into two major categories namely__________.

a) Financial Risks and Operational Risks

b) Credit Risk and Liquidity Risk

c) Systematic and Unsystematic Risks

d) Capital Risk and Legal Risk

Q: 2Which of the following is not typically considered a financial risk in treasury activities?

a) Market risks
b) Credit risks
c) Liquidity risks
d) Compliance risk

Q: 3 Operational risks in treasury activities include all of the following except________

a) Systemic risk

b) Market risk

c) Compliance risk

d) Fraud risks

Q: 4 Treasury activities like investments in bonds and forex positions predominantly involve a high degree of__________.

a) Credit risks

b) Operational risks

c) Market risks

d) Systemic risks

Q: 5All of the following are stated as factors affecting interest rates except__________.

a) Demand for money

b) Supply of money

c) Basis risk

d) Inflation rate

Q: 6___________ refers to the potential for loss arising from inadequacies or failures in internal processes, systems, people, or external events.

a) Market Risk

b) Credit Risk

c) Operational Risk

d) Liquidity Risk

Q: 7Which of the following statements correctly describe the key components and causes of Operational Risk in treasury activities?

1. **System deficiencies**, if not properly integrated with workflows and lacking proper authorization controls, can significantly disrupt transaction processing and affect timely payments and settlements.
2. **Non-compliance** with prescribed procedures and authorization protocols can lead to operational errors, processing delays, and financial losses.
3. **Fraud risks—**such as falsifying deals or misappropriating funds—can have a severe impact on both the financial position and reputation of the institution.
4. **Legal risks** may arise from inadequately defined contracts or agreements, leading to disputes, litigations, or regulatory penalties.

a) Only 1, 2, and 3 are correct

b) Only 2, 3, and 4 are correct

c) Only 1 and 4 are correct

d) 1, 2, 3, and 4 are correct

Q: 8To mitigate operational risk, which of the following is a crucial step concerning dealers' activities?

a) Dealers must operate strictly within the single deal, portfolio and prudential limits set for the instrument and counterparty
b) No deviation from approved and implemented work and document flows should be allowed.
c) Deals or transactions exceeding powers it must be immediately reviewed and formally approved by higher management or the board.
d) All of the above

Q: 9Regarding the mitigation of operational risk, which statement is most accurate?

1. Computer systems - hardware, networks and software - should have adequate backups
2. The institution holding securities (the custodian) should have a strong credit rating to ensure the safety of the assets

3. Powers of attorney or authorizations for counterparties must be kept up to date to ensure they are valid and effective.
4. Deal, transaction and legal documentation should be adequate to protect the bank,

a) Only 1, 2, and 3 are correct

b) Only 2, 3, and 4 are correct

c) Only 1 and 4 are correct

d) 1, 2, 3, and 4 are correct

Q: 10 A treasury department discovers that an employee has been falsifying deal records to misappropriate funds. This scenario is a clear example of which type of operational risk component?

a) System deficiencies

b) IT risks

c) Fraud risks

d) Legal risks

Q: 11 Credit risk primarily refers to the possibility of________

a) Fluctuations in overall market conditions.

b) A debt instrument issuer being unable to honor interest or principal repayment obligations.

c) An institution being unable to meet its short-term financial obligations.

d) Software bugs disrupting transaction processing.

Q: 12 In modern financial markets, credit risk extends beyond debt instrument non-performance to include_______

a) Hardware downtime and network failures.

b) Non-performance by a counterparty in off-balance sheet contracts like forward and swap agreements.

c) The impact of natural disasters on the entire financial system.

d) Disruptions due to poorly defined internal procedures.

Q: 13 Which of the following is listed as a mitigation strategy for credit risk?

1. **Better Credit Appraisal:** Thoroughly analyzing a business's cash flows before investing.
2. **Investing Only in Rated Instruments:** Focusing on investments with reliable credit ratings.
3. **Risk Pricing:** Setting appropriate prices to compensate for potential risks.
4. **Adequate Security:** Requiring sufficient financial or physical assets as collateral.

a) Only 1, 2, and 3 are correct

b) Only 2, 3, and 4 are correct

c) Only 1 and 4 are correct

d) 1, 2, 3, and 4 are correct

Q: 14 A bank sets maximum exposure limits for individual counterparties across both fund and non-fund exposures. This action is a direct mitigation strategy for which type of risk.

a) Liquidity risk

b) Market risk

c) Credit risk

d) Operational risk

Q: 15 ___________ refers to the possibility that an, business, or financial institution may not be able to meet its short-term financial obligations due to an inability to quickly convert assets into cash or secure funding.

a) Market Risk

b) Credit Risk

c) Liquidity Risk

d) Operational Risk

Q: 16 Which of the following is a recommended strategy to mitigate liquidity risk?

a) Invest in Liquid Securities

b) Maintain Credit Rating and Reputation

c) Securitize Loan Portfolios

d) All of the above

Q: 17 Market risk is a broad term describing the risk of financial losses due to_________.

a) Errors in transaction processing.

b) Changes in overall market conditions.

c) The default of a single large borrower.

d) An inadequate legal framework for contracts.

Q: 18 Event Risk is a type of market risk that refers to the potential for significant financial losses resulting from unexpected major events or shocks that impact the entire financial system or markets. Which of the following best represents examples of such events?

a) Changes in interest rates and currency exchange rates

b) Natural disasters, economic crises, and political instability

c) Fluctuations in commodity prices due to market demand

d) Mismatches in asset and liability durations

Q: 19 Interest Rate Risk (Balance Sheet) primarily refers to the potential for financial loss or reduced profitability due to changes in interest rates that affect_________.

a) Only the trading book of the bank.

b) Both the assets and liabilities of a bank.

c) Exclusively the bank's operational efficiency.

d) Only off-balance sheet exposures.

Q: 20 When interest rates fall, what typically happens to the prices of existing fixed rate bonds, especially those of long maturity?

a) Their prices go down.

b) Their prices remain unaffected.

c) Their prices go up.

d) They become more liquid.

Q: 21 If a bank anticipates a rise in interest rates, and assuming market liquidity, how should it adjust its bond portfolio duration to mitigate potential losses?

a) Increase duration by buying long-dated securities.

b) Maintain the current duration without any changes.

c) Lower duration by selling long-dated securities.

d) Diversify into unrated instruments.

Q: 22 __________is a risk management tool used to measure the potential loss in the value of an asset or portfolio over a specified time period, given a certain level of confidence. It helps in quantifying the risk of a portfolio by estimating how much value could be lost due to market fluctuations under normal market conditions.

a) Value-at-Risk (VaR)

b) Credit Risk

c) Market Risk

d) Liquidity Risk

Q: 23 ___________ refers to the risk that one party in a transaction may fail to meet their obligation to deliver payment or assets when due, which could result in a loss for the other party.

a) Settlement Risk
b) Market Risk
c) Operational Risk
d) Liquidity Risk

Q: 24 What does Forex (Market) Risk primarily refer to?

a) Risk of change in commodity prices
b) Risk of interest rate fluctuations
c) Risk of poor marketing strategies
d) Risk of financial loss due to changes in exchange rates

Q: 25 Which of the following is NOT a method of effective forex risk management?

a) Exposure Limits
b) Ignoring market trends
c) Market Monitoring

d) Stop-loss limits

Q: 26 What is an open position in foreign exchange?

a) A fully hedged forex transaction
b) A position where the bank has zero exposure
c) A completely unhedged exposure in a currency
d) A closed forex deal

Q: 27 Which of the following statements are correct about Net Open Position?

1. It is sums long and short positions in one currency.
2. Long positions are assets the bank owns
3. Short positions are liabilities the bank owes
4. It reflects the net forex exposure of a bank.

a) 1, 2, and 3 only
b) 2, 3, and 4 only
c) 1, 3, and 4 only
d) All of the above

Q: 28 ____________ refer to currency positions that a bank or dealer takes during a trading day, with the intention of closing (or "squaring") them before the end of the same trading day.

a) Overnight positions
b) Long positions
c) Daylight open positions
d) Spot positions

Q: 29 Which of the following is not a characteristic of daylight open positions?

a) Held for a few hours
b) Closed before the trading day ends
c) Exposed to overnight risk
d) Involve intraday trading

Q: 30 Which of the following best describes overnight positions in forex trading?

a) Positions opened and closed within the same trading day
b) Positions held for only a few seconds or minutes during the day
c) Positions carried over from one trading day to the next
d) Positions that are squared off before the market closes

Q: 31 What is GAP (Interest Rate/Swap) Risk in forex?

a) Risk due to incorrect exchange rates
b) Risk due to maturity mismatch in positions
c) Risk of customer default
d) Operational risk during currency delivery

Q: 32 What does Customer Credit Risk refer to in forex?

a) The loss due to fall in exchange rate
b) The possibility of country default
c) Risk of customer failing to meet obligations
d) Risk due to legal non-compliance

Q: 33 Which of these is not part of RBI's norms on country risk?

a) Exclude foreign branches' exposure
b) Real-time monitoring for high-risk countries

c) Limit exposures to Tier I and II capital
d) Conduct stress testing