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MNK203-R (469181)
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BUSINESS MANAGEMENT (RISK) 202

Duration : 2 Hours
100 Marks

EXAMINERS :

FIRST : 　MS LM MALOBOLA 　　　　　　　　　　MS CJ DE SWARDT

　　　　　MR JS DE BEER

SECOND : 　PROF GS DU TOIT

Use of a non-programmable pocket calculator permissible.

This paper consists of eight (8) pages plus the instructions for completion of a mark-reading sheet.

This paper adds up to a total of 70 marks. This mark will be adjusted to a percentage mark.

This paper consists of **TWO** sections, namely A and B.

Section A is compulsory. It consists of thirty multiple-choice questions that each counts 1 mark. The answers to this section must be completed on the mark-reading sheet provided.

Section B consists of four discussion type questions. You must answer **ALL FOUR** of these questions. Each question counts 10 marks.

SECTION A: 　　MULTIPLE CHOICE QUESTIONS

This section consists of thirty multiple-choice questions that must be filled in on the mark-reading sheet that is provided.

1. Indicate the **correct** statement.

　1 　The area under the curve of a continuous process is equal to 10%.
　2 　The most widely used measure of central tendency is the standard deviation.
　3 　If all the possible outcomes and associated probabilities are known a continuous probability distribution can be developed.
　4 　When the probabilities of all the possible outcomes are exactly the same the mean and the standard deviation will differ.

2. Indicate the **correct** statement.

　1 　The degree of risk is calculated as the frequency with which an event occurs.
　2 　Risk is present in situations of certainty.
　3 　Risk is the deviation of actual results from expected results.
　4 　All events have a probability of between 0 and 10.

3. If we do not define risk when we speak about it...

1 people will have different perceptions of risk.
2 people will not have any understanding of risk whatsoever.
3 people will tend to avoid talking about risk.
4 people will understand what risk is and what it involves.

4. Event risk...

1 offers a chance of gain or loss.
2 gives rise to risks but are not risks themselves.
3 includes the possibility of loss only.
4 relates to the environment surrounding the cause of loss.

5. Indicate the **correct** statement.

1 Speculative risk deals only with those risks that have a loss or no-loss outcome.
2 Core business risks include activities, decisions and events that have an indirect impact on the operating profit of the organisation.
3 The major subcategory of incidental risks is financial risk.
4 Unsystematic risk arises from events that affect the economy as a whole.

6. Various factors contribute to the successful implementation of Enterprise Risk Management (ERM), including, inter alia:

a Strong and visible support from senior management.
b Separating the risk-taking activities from performance evaluation.
c Proceeding incrementally and leveraging "early wins".
d Treating ERM as a stand-alone process.

Choose the correct combination.

1 a,b
2 a,c
3 b,c
4 c,d

7. Indicate the **correct** statement.

1 Individual risks and interdependencies can better be addressed by an integrated team.
2 Traditional risk management is consistent and generates reliable reports.
3 The only objective of risk reporting is to increase risk transparency.
4 Business risk management adopts a portfolio view of all risks.

8. SWOT analysis...

1 is normally applied with the assistance of insurance intermediaries.
2 is a graphic representation of any form of flow within and to the enterprise.
3 assess the extent to which risk is centralised or decentralised within the enterprise.
4 serves to identify risks in the internal and external enterprise environment.

9. In order to establish potential loss frequency for an enterprise a risk manager would consider:

1 National and international trends.
2 Accumulation of losses.
3 Physical inspections of the premises.
4 Personal interviews with the divisional heads.

10.   The destruction of a factory by fire is an example of...

   1   fundamental event risk.
   2   particular event risk.
   3   operational risk.
   4   incidental risk.

11.   Which **one** of the following is considered a traditional risk control practice?

   1   Failure mode analysis
   2   Safety management programmes
   3   Hazard and operational studies
   4   Failure tree analysis

12.   In terms of the King II Report, businesses should report on their

   a   transformation policy.
   b   environmental management practices.
   c   risk management policy.
   d   remuneration packages of directors.

   Choose the correct combination:

   1   a,b,c
   2   b,c,d
   3   a,b,c,d
   4   a,c,d

13.   The need for a more integrated and holistic view of risk management is emphasized by...

   a   change
   b   globalisation
   c   technology
   d   increased concentration of risk
   e   the increased value of intangible assets

   Choose the correct combination:

   1   a,b,c,d,e
   2   a,b,c,e
   3   a,b,d,e
   4   a,c,d,e

14.   Which **one** of the following is a key characteristic of the traditional approach to risk management?

   1   Function driven
   2   Proactive
   3   Value based
   4   Integrated

15. Which of the following are examples of alternative risk transfer (ATR) techniques.

a   Futures
b   Captive insurance
c   Commercial insurance
d   Swaps

Choose the correct combination:

1   a,b,c,d
2   a,b,d
3   a,d
4   b,c

16. In assessing risk it is important to consider…

1   the root causes of the identified risk.
2   the time horizons for the development of financial statements.
3   the top risks currently faced by the enterprise.
4   the risk attached to intangible assets crucial to value creation.

17. Which of the following factors is determining in the successful implementation of ERM?

a   A positive risk management culture
b   Effective reporting processes
c   Leverage of 'early successes or profits'
d   Acceptance of ERM as an isolated process.

Choose the correct combination:

1   a,b,c
2   b,c,d
3   a,b,c,d
4   a,b

18. Indicate the **incorrect** statement:

1   A common language facilitates communication.
2   A common language decreases the risks in the organisation.
3   A common language facilitates the aggregation of risks in the organisation.
4   A common language forms a fundamental building block of enterprise risk management.

19. Internal factors that may influence the corporate and risk management objectives include:

a   the natural environment within which the enterprise operates.
b   the infrastructure of the enterprise.
c   the technology used in the enterprise.
d   the personnel the enterprise has at its disposal.

Choose the correct combination:

1   a,b,c,d
2   a,b,c
3   b,c,d
4   b,d

20.   Which of the following are considered when establishing the potential frequency of losses?

   a   Incident reporting
   b   National and international trends
   c   Standing charges
   d   Near misses

Choose the correct combination:

   1   a,b,c,d
   2   b,c,d
   3   a,b,c
   4   a,b,d

21.   Which **one** of the following is not a risk control measure?

   1   Access control
   2   Keeping safety stocks
   3   Contingency plans
   4   Insurance

22.   A six-month call option is written at a strike price of R68,00. The option premium is R0,25. The market price of the commodity at the time the option is written was R65,85. Four months after the option is written the market price of the commodity rises to R68,75.

Based on the abovementioned information the buyer of the option will...

   1   walk away from the option and lose the premium of R0, 25.
   2   walk away from the option and buy the commodity in the market.
   3   exercise the option and make a profit of R0,75.
   4   exercise the option and make a profit of R0, 50.

Answer questions 23 and 24 by making use of the following information:

Company A uses short-term financing by issuing banker's acceptances. The treasurer expects short-term interest rates to rise and wants to hedge his next-BA-rollover. Assume the following applies:

Nominal amount   R 1 000 000
Current date   4 April
Rollover/settlement date   20 July
Spot rate on July 20   18,5
FRA spot rate   16,6

The treasure wants to hedge the next roll-over by buying an FRA at 16,6%.

23.   In order to lock in his discount rate at 16,6%...

   1   the bank will have to pay R2 712 to Company A.
   2   Company A will have to pay R2 712 to the bank.
   3   The bank will have to pay R4 685 to Company A.
   4   Company A will have to pay R4 685 to the bank.

24. The cost (discount) of issuing the BA will be as follows:

1   R45 616
2   R38 219
3   R35 506
4   R3 452

25. Indicate the **correct** statement.

1   When buying interest rate futures one will benefit from a fall in interest rates.
2   When buying interest rate futures one will benefit from a rise in interest rates.
3   When selling interest rate futures one will benefit from an upward move in the market.
4   When selling interest rate futures one will benefit from a rise in interest rates.

26. An organisation's limit framework should include a combination of the following....

a.   Volume limits
b.   Portfolio level limits
c.   Value-at-risk (VaR) limits
d.   Stop-loss limits

Indicate the correct combination:

1   a,c,d
2   a,b,c
3   a,b,c,d
4   a,b,d

27. The benefits of including a monitoring stage in the risk management process include...

a   accumulating evidence to support assumptions and the results of analysis.
b   increasing the cost associated with improper or redundant risk control.
c   identifying new or changing risks.
d   improving the risk management process as a whole.

Indicate the correct combination:

1   a,b,c,d
2   a,b,c
3   a,b,d
4   a,c

28. Indicate the **correct** statement.

1   Hedging results in higher profit margins.
2   The buyer of an option commits himself/herself to buy or sell the specified asset on the specified date.
3   Interest collars protect both the lender and the borrower.
4   A short position entails the buying and keeping of an asset.

29. Indicate the **correct** statement.

1 Aggregation **methods provide qualitative means to transfer, avoid and securitize risk.**
2 Aggregation is a way to summarise an extremely simple set of rules.
3 Risks of which the mutual relationships are not known, are pooled together in order to manage it better.
4 Aggregation of multiple risks improves reporting and capital allocation.

30. Indicate the **correct** statement.

1 The credit risk attached to forward contracts is lower than that of future contracts.
2 Future contracts are more liquid than forward contracts.
3 Future contracts tend to be more expensive than forward contracts.
4 Future contracts are normally used to cover currency risk in the event of international trade.

[1 x 30 = 30]

SECTION B: ANSWER ALL FOUR QUESTIONS IN THIS SECTION

Question 1

1.1 Discuss the concepts **risk and uncertainty** within the context of risk management. (4)

1.2 Explain the **limitations of the Companies Act 61 of 1973** in terms of Corporate Governance (6)

[10]

Question 2

2.1 Discuss the **relationship** between an **organisation's** objectives and strategies and its **risk management objectives and strategies.** (6)

2.2 Outline the roles of the **Chief Risk Officer (CRO)** in term of the generic organizational oversight model. (4)

[10]

Question 3

3.1 Discuss the **main characteristics** of the **enterprise risk management** approach to risk management. (6)

3.2 Outline the **environmental factors** that accompany the successful implementation of an ERM framework. (4)

[10]

Question 4

4.1 Suppose Borrower A can obtain R2 million for ten years at a floating rate of prime plus 0,80% but he has to pay a fixed rate of 20% on a debenture for the same term. Borrower B, who is a bank, can borrow floating funds at the prime rate and fixed funds at 16%. Borrower A and the bank agree to enter into a swap agreement in which Borrower A agrees to pay an additional premium of 3% to the bank.

Use the aforementioned set of information to construct a possible interest rate swap transaction between the two parties. Indicate clearly the benefits accrued to each of the parties involved in the aforementioned swap transaction. (6)

4.2 Explain how the **cost effectiveness** of a risk control programme is determined. (4)

[10]

[4 x 10 = 40]
TOTAL MARKS: 70