SECTION A: MULTIPLE-CHOICE QUESTIONS

Indicate the correct alternative in respect of each question on the mark-reading sheet.

1   It is important to classify risks because ___

   1   some risks can be managed by an enterprise while others cannot
   2   this provides vital information on the physical/financial environment of the enterprise
   3   it allows the risk manager to effectively manage these risks
   4   of all of the above

2   The incompetence of production staff working for a motor manufacturer can be considered a/an ___ for the specific organisation

   1   incidental business risk
   2   event risk
   3   core business risk
   4   fundamental pure risk

3   South African enterprises should strive for good corporate governance because ___

   1   it is important in order to attract both foreign and domestic capital
   2   there is an increasing demand for investment funds in developed and developing countries
   3   investors' trust in companies has decreased and company ethics are being ideally criticised
   4   of all of the above

4   Which of the following is **not** a peril?

   1   explosions
   2   a container of a flammable product
   3   earthquakes
   4   fires

5   Indicate the **correct** statement

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

6   Which of the following methods can be used in the evaluation of loss frequency?

   1   maximum possible loss (MPL)
   2   accumulation
   3   Pareto rule
   4   business interruption

7   Indicate the **correct** statement

   1   According to the traditional approach some risks are managed using derivatives
   2   The traditional approach adopts a comprehensive approach to managing risks
   3   The traditional approach integrates the efforts of operating managers and risk managers
   4   The traditional approach views risk management as part of everyone's job

8   Displaying disclaimer notices in a parking area is an example of ___

   1   physical risk control
   2   procedural risk control
   3   risk elimination
   4   legal risk control

9   In assessing risk it is important to consider ___

   a   determining the root causes of the identified risk
   b   setting time horizons for the development of financial statements
   c   identifying and communicating the top risks currently faced by the enterprise
   d   identifying the risk attached to intangible assets crucial to value creation

   Choose the **correct** combination

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

10 Which one of the following fire losses would you regard as the most serious?

   1   R5 m which occurs every 10 years
   2   R3 m which occurs every seven years
   3   R1 m which occurs every three years
   4   R9 m which occurs every 17 years

11. Which of the following is **not** a risk identification method?

1 SWOT analysis
2 insurance reviews
3 statutory records
4 standing charges

12 Internal factors that may influence the corporate and risk management objectives include the following:

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

13. The following benefits are obtained through the effective implementation of enterprise risk management (ERM):

a increased organisational effectiveness
b strong and visible support from senior management
c increased business performance
d better risk reporting

Choose the **correct** combination

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

14. Indicate the **incorrect** statement.

1 Individual risks and interdependencies can best 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.

15 Hijackings in the centre of Johannesburg are a category four type of risk characterised by

1 low frequency and low severity
2 low frequency and high severity
3 high frequency and low severity
4 high frequency and high severity

16 Indicate the **incorrect** statement.

1 Hedging limits profits.
2 Interest collars protect both the lender and the borrower
3 A short position entails the buying and keeping of an asset
4 The buyer of an option commits himself/herself to buy or sell a specified asset at a specified price on (or before) a specified date

17. Which one of the following is **not** a class of risk management objectives?

1 operational objectives
2 reporting objectives
3 strategic objectives
4 compliance objectives

18 Enterprises can use the following methods to identify risks that should be included in their framework:

a internal interviewing
b external sources
c tools, diagnostics and processes
d production flowcharts

Choose the **correct** combination

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

Answer questions **19** and **20** by making use of the following information:

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

Nominal amount	R1 000 000
Current date	4 April
Rollover/settlement date	20 July
Spot rate on 20 July	16,50%

FRA spot rate offer   17,60%
The treasurer wants to hedge the next rollover by buying a (Forward Rate Agreement)
FRA at 17,60%

19 In order to lock in a discount rate of 17,60%

1   the bank will have to pay R2 712,33 to Company A
2   Company A will have to pay R2 712,33 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

20 The cost (discount) of issuing the BA will be

1   R40 684,93
2   R38 219,18
3   R35 506,85
4   R 3 452,05

21 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

Choose the **correct** combination

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

22 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 for enterprise
     risk management

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

Based on the aforementioned 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 on the market
3   exercise the option and make a profit of R0,75
4   exercise the option and make a profit of R0,50

24 Indicate the **incorrect** statement. Alternative Risk Transfer (ART)
   techniques involve the following:

1   the transfer of risk to capital markets
2   giving investment banks a new field of activities
3   powering the trend towards global operations
4   providing insurance companies with an extension of their capacity base

25 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   assesses the extent to which risk is centralised or decentralised within the
     enterprise
4   serves to identify risks in the internal and external enterprise environment

26 The reasons for aggregating the activities directed at achieving enterprise-
   wide risk include the following:

a   the cumulative effect of risk
b   increased efficiency and better decisions
c   improved reporting and capital allocation
d   simplicity

Choose the **correct** combination

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

27 Indicate the **correct** statement

1   Aggregation methods provide qualitative means to transfer, avoid and
     securitise 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
     in order to manage them better
4   Aggregation of multiple risks improves reporting and capital allocation.

28. Which of the following should be considered in order to facilitate the optimal alignment of strategy, processes, people, technology and knowledge?

   a   evaluating risk capacity and appetite
   b   determining the effects of pooling on risk strategy
   c   identifying sources of competitive advantage
   d   establishing an oversight structure

Choose the **correct** combination

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

29. The following procedures are all enablers of the continuous improvement philosophy except for one, namely ____

   1   benchmarking of performance to identify best practices
   2   interactive communications and sharing of knowledge
   3   integrating the enterprise's risk language and risk management process into its employee learning programme
   4   tracking changes in the business context and risk environment

30. Indicate the **correct** statement.

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

SECTION B: PARAGRAPH QUESTIONS AND CALCULATIONS

Question 1

Compare the riskiness of the following sets of share prices collected over a four-month period. The expected value of share A is R1 152,5 and that of share B is R1 287,5

SHARE A

Price	Expected value	Deviation	Squared deviation
R1 120			
R1 140			
R1 170			
R1 180			

Variance	Standard deviation	Coefficient of variation

(4)

SHARE B

Price	Expected value	Deviation	Squared deviation
R1 510			
R1 360			
R1 120			
R1 160			

Variance	Standard deviation	Coefficient of variation

Comment on the riskiness of the two sets of share prices (2)

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[10]

Question 2

2 1   Differentiate between the **narrow** and **broader** meanings of corporate governance (4)

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2 2   Outline how corporate governance impacts on the business areas of enterprises (6)

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[10]

Question 3

3 1 Explain the **four** alternative methods of determining the real value of an asset for risk evaluation purposes (4)

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3.1 Outline the main aspects of **infrastructure** addressed in the risk management framework.

(4)

1) central + independent risk Mngmt unit
2) formalised policies + procedures
3) consistent methodologies for risk mngmt
4) limit structures that set maximum tolerances
5) comprehensive mngmt reports
6) information technology

3.2 With reference to examples, distinguish between **risk transfer** and **risk insurance** (2)

* Risk transfer is when the actual risk is transferred as is the case when you hire computer equipment - the risk of obsolescence is transferred.
* Risk insurance is when the financial consequences of the risk is transferred - take out insurance to cover you for the financial implication should the computer equipment be stolen etc.
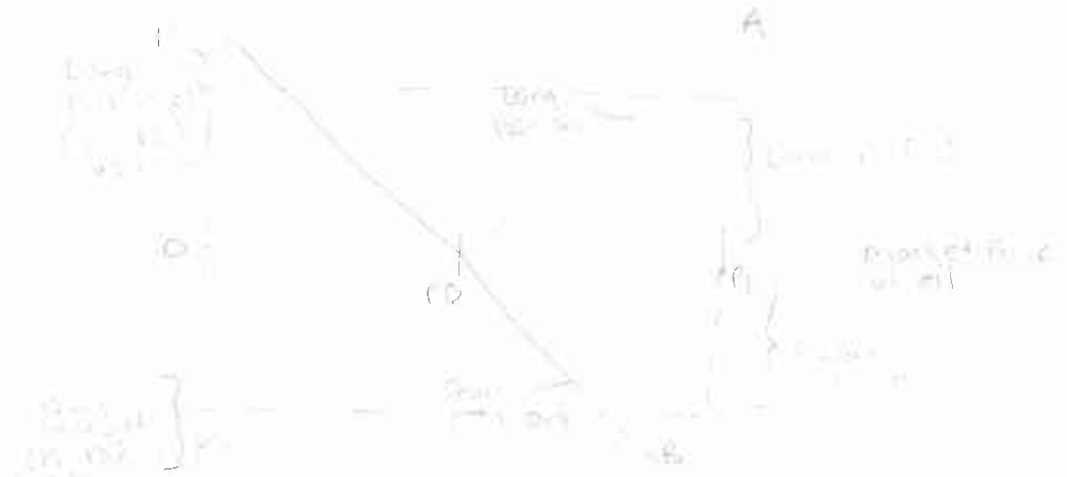
[10]

Question 4

4.1 You are the risk manager for South African Airways (SAA). You expect the price of oil to increase over the next year and decide to make use of futures contracts to hedge this risk. **Graphically illustrate** the concept of a **perfect hedge** for purposes of managing the risk of an increase in the price of oil (5)

4.2 List the five steps in establishing a base from which to launch an Enterprise Risk Management (ERM) strategy. (5)

1) Establish oversight structure
2) Define common risk mngmt framework
3) Target risks + processes
4) Develop overall goals, objectives + processes
5) Assess risk mngmt capabilities

[10]