UNISA EXAM MEMO RSK2601 MAY/JUNE 2015

SECTION A (40 MARKS)

1. 2	11. 2	21. 1	31. 3
2. 2	12. 1	22. 4	32. 3
3. 2	13. 1	23. 2	33. 4
4. 1	14. 4	24. 2	34. 2
5. 1	15. 3	25. 3	35. 3
6. 4	16. 1	26. 2	36. 4
7. 3	17. 3	27. 2	37. 4
8. 4	18. 2	28. 3	38. 1
9. 3	19. 3	29. 1	39. 3
10. 2	20. 3	30. 3	40. 4

SECTION B (30 MARKS)

Question 1 (10 marks)

Corporate governance refers to the relationships among the management of an organisation, its board, its shareholders and other relevant stakeholders. It also refers to the specific responsibilities of boards of directors and management to maintain established relationships.

Corporate governance has an impact on the following business areas of an enterprise:

- the efficient employment of assets
- the attraction of lower cost capital
- meeting social obligations by complying with laws and regulations
- overall performance

Employing assets efficiently
Effective corporate governance promotes the efficient use of resources within a firm and the economy at large. When an efficient corporate governance system is in place, debt, equity and capital flow to enterprises that are capable of investing these resources efficiently in order to produce goods and services that are most in demand and have the highest rate of return. In this regard, effective governance helps to grow and protect scarce resources and to ensure that societal needs are met. Effective governance should make it possible to replace managers who do not put scarce resources to efficient use or who are incompetent in what they do.

Attracting lower-cost capital
Effective corporate governance helps enterprises to attract lower-cost capital by improving the confidence of domestic and international investors and by assuring them that the assets are used in the form agreed upon, whether the investment is in the form of debt or equity. This has a positive impact on both debt and equity. For enterprises to succeed in competitive markets, corporate managers must innovate relentlessly and efficiently, and constantly evolve new strategies to meet changing circumstances.

Meeting social obligations: complying with laws and regulations
To succeed in the long term, enterprises must comply with the laws, regulations and expectations of the societies in which they operate. Most corporations take their corporate citizenship seriously.

They contribute to civil societies' needs while some are opportunistic and have no regard for social or environmental issues. Good corporate governance is essential to ensure adherence to legislation as well as corporate social responsibility principles.

Overall performance
If corporate governance is effective, it gives managers a holistic view of the organisation and holds managers and the board accountable for the management of corporate assets. Such accountability contributes to the efficient use of resources, attraction of lower-cost capital and an increase in the responsiveness of the enterprise to society, and will therefore lead to the improvement of corporate performance. Effective corporate governance may not guarantee improved corporate performance at the individual firm level, but it should increase the likelihood of managers focusing on improving the performance of enterprises and of their being replaced when they fail to do so.

Question 2 (12 marks)

2.1 (6 marks)
The following activities need to be conducted:
- Executing
- Monitoring
- Controlling

Executing
All the actions planned in the risk treatment stage to respond to risks and opportunities must be effectively executed by the business.

Monitoring
When executing action plans, it is vital to monitor progress to differentiate the movement in risk exposure. Monitoring is the collection of information on the risk for later use. The monitoring process must identify the successes achieved in the planned responses to the risks and opportunities and be able to identify the changes in the business environment, which might lead to new emerging risks. Thus, the monitoring and review processes implemented by the business can improve business knowledge on the lessons learned to improve the future ERM process.

Controlling
The controlling process is based on the information gathered in the monitoring process to form decision-making. It means the business must understand who needs what information for what purpose and when.

2.2 (6 marks)

Mechanism	**Explanation**
Probability trees	A probability tree is a method used by a business to ensure that all possible outcomes of a risk event have been taken into account. A probability distribution is a list of possible outcomes with associated probabilities. Thus, a probability tree will illustrate all possible probability distributions for a certain risk event. A probability tree can be used to illustrate both a dependent event and an independent event. The probability of any event (*E)* is a number between 0 and 1. Thus, $0 \leq P(E) \leq 1$ and is the sum of the probabilities of any set of mutually exclusive (only one event can occur at a time) and non-mutually exclusive (the events cover all possible outcomes) events which equals
Expected monetary value (EMV)	In some cases, the decision outcome of an event can have more than one outcome. In such an event, the EMV will be calculated by using the weighted outcomes, which is calculated using the probabilities assigned to each outcome, for example, successes/profit and failures/losses. The theory requires that the probabilities and outcomes be determined. The EMV will be used to select the decision alternative with the highest monetary value.
Decision trees	A decision tree is used to illustrate decision problems graphically. A decision tree consists of different decision nodes, with interconnected branches, which represent the different alternatives for a particular decision.

Question 3 (3 marks)
The three main components of credit risk are:

- default,
- exposure and
- recovery risk.

Default risk is the probability of the event of default.
Exposure risk relates to the uncertainty surrounding the payment of future amounts.
Recovery risk relates to the uncertainty over the likely recovery.

Question 4 (5 marks)
Environmental sustainability is the maintenance of the factors and practices that contribute to the quality of the environment on a long-term basis.

Environmental risk for businesses is considered to include, but not limited to (any 4):

- pollution of land, water, air;
- increased regulation and higher operational costs;
- prosecution arising from the lack of observance of rules set by a regulatory body;
- reputational risk from adverse publicity as a result of pollution events, resulting in a reduced customer base;
- destruction of facilities or loss of manufacturing as a result of severe weather conditions, and
- loss of oil production, resulting in higher energy costs.