CHRIST UNIVERSITY, BANGALORE-560029
End Trimester Examination March - 2012
VI Trimester End Semester Examination, March 2012

Code : MBA662/MBA1662/PGDM662
Sub : FINANCIAL RISK MANAGEMENT

Max. Marks : 100
Duration : 3Hrs

SECTION A

Answer any 10 questions.

10 X 2 = 20

1. Employee Risk can be eliminated through sound recruitment policies. Do you agree?
2. Forward Rate is an estimate of what the spot price will be in the future. Do you agree? Why?
3. FDI – a friend or a foe?
4. Expand AFS and explain the accounting norm.
5. Base Rate is the same as BPLR. Is this correct and why?
6. RAROC is a metric that adjusts both return and capital. Explain.
7. Bad assets cannot be sold and hence Problem Loan needs no management. What are your views?
8. Micro hedging is no longer practiced. Is this true? Why?
9. Why are OTC products so popular?
10. Funding Risk can be mitigated through parental support. Elucidate
11. What major change did Basel II usher in when compared to Basel I?
12. Derivatives are popular as there these need not be accounted. Elucidate.

SECTION B

Answer any 6 questions.

6 X 5 = 30

13. How can liquidity risk trigger other risks?
14. What is the need for risk management in an organisation?
15. What is difference between book value and market value of assets and liabilities?
16. Differentiate between secured and unsecured loans on the basis of credit risk exposure.
17. A bank has made a loan @ 10% p.a. Bank expects a probability of default of 5% and if loan is defaulted, it expects to recover 50% of its money through security sale. What is the expected return on loan?
18. What are the credit derivatives? How many kinds of credit derivatives are available in Indian market?
19. Even when the derivatives such as forward, future and options are available, why do the banks need swaps for interest rate risk hedging?
20. What is the rationale behind the rating used by these credit rating agencies?

SECTION C

Answer any 3 questions.

3 X 10 = 30

21. What are the various risk management approaches that an organization can adopt?
22. A corporate treasurer has entered in to the following 3 month Forward Contract –
   Buy USD 2 Mn @ 1 GBP = USD 1.543
   What is the GBP equivalent as per the forward contract?
What would he gain or lose if the after 3 months, the GBP/USD quotes at 1.55 and 1.50?

What are the various reasons for liquidity risk? How does the liquidity risk of asset side differ from liquidity risk of liability side?

How do the regulators manage liquidity in the financial system? What are the various tools used by regulators for liquidity management in the system?

How is an FI exposed to foreign exchange risk? List out the various possible financial transactions involving foreign exchange risk? What are the current norms on open FX positions that banks in India can carry?

SECTION D

Case Study (Compulsory) 1 X 20 = 20

26 Bridgewater Associates, world's biggest hedge fund, emerges as one of the best performers - 27 Jan, 2012, 01.35PM IST, NYT News Service

Bridgewater Associates, which manages nearly $120 billion, posted returns of 23 percent in 2011 - a year when the average hedge fund portfolio lost 5 per cent.

Against the backdrop of fear over European debt and stagnant global growth, the hedge fund, led by one of Wall Street's more enigmatic titans, Ray Dalio, sidestepped the mess. The fund did it with bets on US Treasury's, German bonds and the Japanese yen, according to people familiar with the firm's investment strategy, who spoke on condition of anonymity because the information is private.

Such performance adds up. Over the past 20 years, Bridgewater had annualized returns of 14.7 percent, amounting to $50 billion of gains for investors. Over the same period, the Standard & Poor's index of 500 stocks returned about 8.7 percent a year.

A big chunk of Bridgewater's gains came in recent years, a volatile period that felled many funds. As the financial crisis wreaked havoc, Bridgewater notched positive, albeit modest, returns in 2008 and 2009. The next year, the firm had gains of 45 percent versus about 10 percent for the average hedge fund.

The firm has managed to post big numbers even as assets have swollen, defying conventional wisdom and industry experience. Investors poured money into Paulson & Co in recent years, after the founder, John A. Paulson, earned billions of dollars betting against sub-prime mortgages. Assets at Paulson topped $38 billion at the beginning of 2011, but many of his portfolios suffered last year, with one of the main funds losing 50 percent.

Bridgewater has been able to avoid that fate, in part, because it follows a go-anywhere strategy. The fund's managers assess the political, economic and regulatory environments around the world, and then make bets using commodities, currencies and other assets.

"It's become a more macro world," said Charles T. Cassidy of Cambridge Associates, a consulting firm that advises more than 900 investors with more than $3 trillion in overall assets.

This year, Bridgewater is bullish on gold as a hedge against inflation. The managers are said to believe that governments will need to print more money to help reduce mounting sovereign debt, which could hurt the dollar but help gold. Bridgewater is also betting against the Australian dollar and several emerging-market currencies.

The success comes as Bridgewater finds itself under the microscope for its peculiar culture and odd rules. Dalio, a graduate of Harvard Business School, is a fervent disciple of radical transparency, a set of beliefs that preaches the pursuit of truth at all costs. For instance, mid-level employees can criticize top management if they think a certain market position is foolish.
In an embodiment of his principles, Dalio wrote a roughly 120 page treatise, called "Principles," that is part diary, part philosophical musing and part self-help guide. New employees are required to read it, and it is available to the public online. Dalio, the son of a homemaker and a jazz musician, writes of his poor grades in high school and a sub-par ability to remember names or grasp foreign languages.

Bridgewater's office in Westport, Conn., has a Big Brother vibe, employees say. Overhead video cameras tape employees throughout the day. To root out problematic behavior, employees are subjected to withering critiques from co-workers. These sessions are recorded and, in the interest of transparency, anyone can pull a copy of the video from the hedge fund's library.

Former employees say that while it can be an intense and unpleasant place to work, the intellectual environment is invigorating. Ideas are tested vigorously for their soundness. And employees are constantly pushed to improve their investment skills, even if that can be painful at times.

In the wake of some negative publicity that portrayed the firm as strange and inflexible, Bridgewater has begun an unofficial image campaign. Last year, Dalio appeared on CNBC, where he called the reports "a misunderstanding" and said they had "affected employment."

Bridgewater also began conducting focus groups at Ivy League schools with students bound for Wall Street. Participants in the 90-minute sessions received $100 gift certificates for voicing their opinions on the firm. In true Bridgewater spirit, they were asked to be as honest as possible.

"Bridgewater has done an extremely good job with its culture, where they challenge each other openly to come up with the truth," said Dick Del Bello, a senior partner at Conifer Securities, a brokerage firm. "Their track record over 20 years is pretty compelling."

**Question:**

_Do you think Bridgewater has effectively employed ERM to stay ahead of competition? What do you think they have done differently to achieve consistent growth?_

_Did Bridgewater employ a more robust financial model in running the hedge fund? Can you spot the model used in the case study?_

_One of the key conventional management strategies has been to empower key resources and create a people friendly work environment. Bridgewater, however, seems to have done the opposite and yet succeeded. What is your learning from this?_