Risk Management

Multiple Choice Questions

Answers

Question 1.

Answer : A

Question 2.

Answer : A

Explanation : Financial risk entails all the factors that may impact the cash flows/return of a project either positively or negatively. However, the term 'risk' in finance often refers to downside risk i.e. the probability of earning a lower-than-expected return or making a loss.

Question 3.

Answer : C

Question 4.

Answer : C

Question 5.

Answer : C

Explanation : Settlement risk arises when a counterparty refuses or is unable to pay its commitments at the settlement date. Bankruptcy risk refers to the case when liquidation value of assets is less than liabilities. Default risk refers to non-payment of interest or loan by a borrower.

Question 6.

Answer : A

Question 7.

Answer : A

Question 8.

Answer : A

Explanation : Systemic risks are the risks that may originate with just one industry or company but eventually spread to other branches of the economy, effectively threatening the stability of the entire system. A good example is the oil and gas industry. Specific risks arise within a single business or industry. Such risks may include employee strikes and the scarcity of individual inputs.

Question 9.

Answer : C

Question 10.

Answer : B

Question 11.

Answer : A

Question 12.

Answer : C

Question 13.

Answer : C

Risk and reward often move together. Assuming more risk puts the investor in line for more return, although the trade-off between the two is highly variable.

Question 14.

Answer : B

Question 15.

Answer : C

Question 16.

Answer : C

Question 17.

Answer : C

Explanation : Quantifiable risks are those that can be measured in some way. For instance, we can specify the likelihood of borrower default and even specify the distribution function. On the other hand, non- quantifiable risks are those risks that cannot be measured.

Question 18.

Answer : C

Question 19.

Answer : A

Question 20.

Answer : C

Explanation : Enterprise-wide risk management involves the development of structured and consistent business principles that govern the way different business units of a company do business, in regard to risk. By applying consistent risk management principles across the whole of a company, all risks, including inter-departmental risks, are taken into account. ERM differs from the silo-approach, in which different departments are left to manage risks on their own.

Question 21.

Answer : C

Explanation : The risk of strategic weaknesses in a business is a specific risk to the firm. Therefore, it is the most likely form of specific risk from the given choices . Option A is incorrect because changes in CPI or inflation will affect the overall market prices. Option B is incorrect because the change in the aggregate demand of a sector will change the general market risk of that sector. Option D is incorrect as the changes in tax regulations will change the general market risk.

Question 22.

Answer : C

Question 23.

Answer : B

Question 24.

Answer : D

Question 25.

Answer : A

Question 26.

Answer : D

Explanation : Market risk is the possibility of loss resulting from market movements, whereas liquidity risk is the risk that a financial instrument cannot be traded quickly enough to avoid a loss (or take advantage of a price increase and make a profit).

Question 27.

Answer : B

Explanation : Foreign exchange risk is the risk that the foreign exchange rate will change, which in turn affects the value of a financial instrument or asset held in that currency. In the aftermath of ''Brexit,'' investors were generally pessimistic about the economic stability of the U.K, for instance, because of the anticipated shattering of decades-old trade deals between the U.K and other European countries, coupled with the uncertainty associated with renegotiating new bilateral links with individual countries. This loss of confidence led to the weakening of the pound.

Question 28.

Answer : A

Question 29.

Answer : B

Question 30.

Answer : D

Question 31.

Answer : B

Question 32.

Answer : D

Question 33.

Answer : B

Explanation : Financial institutions do not always fail because of the inability to generate a profit. Rather, it's the inability to meet short-term financial obligations that often leads to bankruptcy. This is known as funding liquidity risk. If Tohonday decides to invest in long-term assets, then it must take into account its day-to-day funding requirements, especially because funds invested in long-term assets cannot be realized quickly enough to meet short-term debts and other unforeseen obligations, such as lawsuits.

This is particularly true when we consider that over the last couple of years, several motor-vehicle production companies like Toyota have had to recall some models due to mechanical glitches, sometimes compensating customers in the process.

Question 34.

Answer : C

Question 35.

Answer : A

Question 36.

Answer : C

Risk management entails creating economic value by qualitatively and quantitatively identifying and measuring all major risks associated with a business. It goes further to suggest ways of addressing these risks. It differs from risk taking, which only entails investing in risky but profitable financial ventures.

Question 37.

Answer. D

Question 38.

Answer : D

Question 39.

Answer : C

Question 40.

Answer : B

Question 41.

Answer : B

Question 42.

Answer : B

Question 43.

Answer : C

Question 44.

Answer : D

Question 45.

Answer : B