

**NATIONAL UNIVERSITY OF SCIENCE & TECHNOLOGY**  
**FACULTY OF COMMERCE**  
**DEPARTMENT OF FINANCE**  
**BACHELOR OF COMMERCE HONOURS DEGREE IN FINANCE**  
**PART IV - 2<sup>ND</sup> SEMESTER FINAL EXAMINATION – MAY 2006**  
**RISK MANAGEMENT [CFI 4204]**  
**TIME ALLOWED: 3 HOURS 10 MINUTES**

**INSTRUCTIONS**

1. The paper is 3 hours 10 minutes, of which 10 minutes is reading time.
2. Answer Question **ONE** and Any Other **FOUR** questions.
3. Write legibly

**Question 1**

Assume that Investor Pvt Limited expects to receive CHF 500 000 in one year. The existing spot rate and the one-year forward rates of the swiss CHF are USD 0,60 and USD 0,62 respectively. Investor Pvt Limited created a probability distribution for the future spot rate in one year as follows:

<b>Future Spot Rate</b>	<b>Probability</b>
\$0,61	20%
\$0,63	50%
\$0,67	30%

Assume that one-year put options on CHF are available, with an exercise price of \$0,63 and a premium of \$0,04 per unit. One-year call options on CHF are available within an exercise price of \$0,60 and a premium of \$0,30 per unit. Assume the following money markets rates.

	<u>US</u>	<u>Switzerland</u>
Deposit rate	8%	5%
Borrowing rate	9%	6%

- a. Using, this information, determine whether a forward hedge, money market hedge or currency option hedge would be most appropriate. [Show all your workings in each case]. **[15]**
- b. Compare the most appropriate hedge [from (a) above ] to an unhedged strategy, and decide whether Investor should hedge its payable position or not. **[5]**

**Question 2**

Discuss the credit risk management techniques that could be used by banks. **(20)**

**Question 3**

Examine the strategies a bank in Zimbabwe could use to manage interest rate risk exposure in the current environment where rates have peaked at over 500% per annum. **(20)**

**Question 4**

Explain the foreign exchange exposures and how they can be managed. (20)

**Question 5**

Discuss the importance of adjusting returns for risk and performance evaluation and show how the process helps in managing risks. (20)

**Question 6**

Analyse how banks in Zimbabwe measure and manage their liquidity risks. (20)