Question #1 of 14

Features of a risk management framework *least likely* include:

A) monitoring the organization’s risk exposures.

B) taking corrective actions against employees who exceed their risk budgets.

C) establishing risk governance policies and processes.

Explanation

Corrective actions against individuals are not specifically part of a risk management framework. Features of a risk management framework include establishing risk governance policies, determining risk tolerance, identifying and measuring risks, managing or mitigating risks, monitoring exposures to risks, performing strategic risk analysis, and communicating risk levels through the organization.

(Study Session 13, Module 42.1, LOS 42.b)

Question #2 of 14

Which of the following statements about an organization's risk tolerance is *most accurate*?

A) The financial strength of an organization is one of the factors it should consider when determining its risk tolerance.

B) Risk tolerance is the degree to which an organization is able to bear the various risks that may arise from outside the organization.

C) An organization with low risk tolerance should take steps to reduce each of the risks it identifies.

Explanation

Financial strength is an important factor in an organization's risk tolerance because it reflects the organization's ability to withstand losses. Even if its risk tolerance is low, an organization may choose to bear some risks that are consistent with achieving the organization's objectives. Risk tolerance includes risks that arise from within the organization as well as risks from outside.

(Study Session 13, Module 42.1, LOS 42.d)

Question #3 of 14

Which of the following is *least likely* to contribute to effective risk governance?

A) Decision-makers throughout an organization should consider risk governance a responsibility.

B) An organization should identify its overall risk tolerance and establish a framework for oversight of risk management.

C) The risks an organization chooses to pursue, limit, or avoid should reflect the overall goals of the organization.

Explanation

Senior management should be responsible for risk governance, which includes determining the organization's risk tolerance and its strategy for managing risks in line with the organization's goals.

(Study Session 13, Module 42.1, LOS 42.c)

Question #4 of 14

An objective of the risk management process is to:

A) eliminate the risks faced by an organization.

B) minimize the risks faced by an organization.

C) identify the risks faced by an organization.

Explanation

The risk management process should identify an organization's risk tolerance, identify the risks it faces, and monitor or address these risks. The goal is not to minimize or eliminate risks.

(Study Session 13, Module 42.1, LOS 42.a)

Question #5 of 14

Measures of interest rate sensitivity *least likely* include:

A) rho.

B) duration.

C) beta.

Explanation

Beta measures the market risk of an asset or portfolio. Duration measures the interest rate sensitivity of the value of a fixed-income security or portfolio. Rho measures the interest rate sensitivity of the value of a derivative.

(Study Session 13, Module 42.1, LOS 42.g)

Question #6 of 14

A portfolio manager uses a computer model to estimate the effect on a portfolio's value from both a 3% increase in interest rates and a 5% depreciation in the euro relative to the yen. The manager is *most accurately* described as engaging in:

A) risk shifting.

B) stress testing.

C) scenario analysis.

Explanation

Scenario analysis involves modeling the effects of changes in multiple inputs at the same time. Stress testing examines the effects of changes in a single input. Risk shifting refers to managing a risk by modifying the distribution of outcomes.

(Study Session 13, Module 42.1, LOS 42.g)

Question #7 of 14

Risk management within an organization should *most appropriately* consider:

A) interactions among different risks. ✓

B) internal risks independently of external risks. ✗

C) financial risks independently of non-financial risks. ✗

Explanation

The various financial and non-financial risks interact in many ways. A risk management process should consider these interactions among risks rather than treating them each in isolation.

(Study Session 13, Module 42.1, LOS 42.f)

Question #8 of 14

The risk of losses caused by human error or faulty processes within an organization is *most accurately* described as:

A) operational risk. ✓

B) solvency risk. ✗

C) model risk. ✗

Explanation

Operational risk arises from faulty processes or human error within the organization.

(Study Session 13, Module 42.1, LOS 42.f)

Question #9 of 14

Which of the following risks is *most accurately* classified as a non-financial risk?

A) Liquidity risk. ✗

B) Credit risk. ✗

C) Model risk. ✓

Explanation

Model risk is an example of a non-financial risk. Credit risk and liquidity risk are classified as financial risks.

(Study Session 13, Module 42.1, LOS 42.f)

Question #10 of 14

An organization's risk budgeting process is *least likely* to:

A) limit the organization’s exposures to the equity, fixed income, and commodity markets.

B) use specific metrics to ensure the organization’s allocation of risks remains within its overall risk tolerance.

C) determine whether the organization needs to purchase additional insurance.

Explanation

Risk budgeting refers to allocating the total risk an organization chooses to accept among its various assets, investments, or activities. Specifying methods for dealing with particular risks is typically outside the scope of a risk budgeting process.

(Study Session 13, Module 42.1, LOS 42.e)

Question #11 of 14

Value-at-Risk (VaR) and Conditional VaR are best described as measures of:

A) model risk.

B) tail risk.

C) liquidity risk.

Explanation

VaR and Conditional VaR are measures of tail risk, the probability of or magnitude of extreme negative outcomes in the tail of a distribution.

(Study Session 13, Module 42.1, LOS 42.g)

Question #12 of 14

Examples of financial risks include:

A) credit risk, market risk, and liquidity risk.

B) market risk, liquidity risk, and tax risk.

C) solvency risk, credit risk, and market risk.

Explanation

Credit risk, market risk, and liquidity risk are examples of financial risk. Solvency risk and tax risk are classified as non-financial risks.

(Study Session 13, Module 42.1, LOS 42.f)

Question #13 of 14

The first step in managing an organization's risks should be to determine:

A) the organization's risk exposures.

B) the organization's risk tolerance.

C) a risk budget for the organization.

Explanation

Risk governance begins with determining the organization's overall risk tolerance.

(Study Session 13, Module 42.1, LOS 42.c)

Question #14 of 14

Buying insurance is *best* described as a method for an organization to:

A) shift a risk.

B) transfer a risk.

C) prevent a risk.

Explanation

Buying insurance transfers a risk to the insurance company. Shifting a risk is changing the distribution of outcomes, typically with a derivatives contract. Preventing a risk refers to taking steps such as strengthening security procedures.

(Study Session 13, Module 42.1, LOS 42.g)