



Roll No.....

Membership No.....

**The Institute of Chartered Accountants of India  
Forex & Treasury Management Certificate Course  
Evaluation Test Booklet**

**Paper 1  
2<sup>nd</sup> NOV, 2014**

**Duration- 3 Hours**

**Total Marks- 100**

**INSTRUCTIONS:**

1. Please read the instructions carefully given in the question paper and solve it in the space provided.
2. The candidates are not allowed to carry the evaluation test booklet with them. This should be tied up with sheets provided to answer the question Paper.
3. Use Blue/Black pen only.
4. Do not write your Roll No. or Name or other identification other than in the space (perforated) provided on this sheet.
5. Please show Identity Card to the invigilator for verification of your identity, when asked.
6. The candidates may use the simple calculator.
7. The candidates should allocate their time wisely. Use the number of marks assigned to each problem as your guide.
8. In order to get full credit on the problems, the candidates must show all their rough work/ other workings.

\_\_\_\_\_  
(Participant Signature)

\_\_\_\_\_  
(Invigilator Signature)

**PLEASE RETURN THIS BOOKLET BEFORE LEAVING THE EXAMINATION HALL**

**Date : 2<sup>nd</sup> Nov, 2014**

**Centre : Delhi/ Mumbai /Chennai/Kolkata/Bangalore/Ahmedabad/Baroda/Cochin & Pune.**

(Do not write your Roll No. and Membership number anywhere in the answer sheet except as mentioned above)

**Checked by**

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**CERTIFICATION COURSE ON FOREX AND TREASURY MANAGEMENT**

<b>S. No.</b>	<b>Total Number of Questions</b>	<b>Questions to be answered</b>	<b>Total Marks</b>	<b>Marks Obtained</b>
Multiple Choice - Section A	65	65	65	
Short Notes – Section B	7	5	25	
Case Study – Section C	2	1	10	
Total	74	71	100	

**Section A**

**Number of questions: 65**

**Marks: 65**

**Multiple choices: There may be more than one correct answer, but there is at least one. Please [✓] mark for the answer.**

**Part A: Answer all questions.**

**1 mark each**

1. Considering the nature of work, in your opinion, a training program in valuation of securities/financial assets as per the regulator's guidelines and IFRS should be given to officials working in the following segment of a treasury:
  - a. Front office
  - b. Back office**
  - c. Mid office
  - d. Every segment
2. Understanding of systematic risk and its impact on treasury operation is relatively more relevant to
  - a. Official working in treasury front office
  - b. Official working in treasury back office
  - c. Official working in treasury mid office**
  - d. Only treasury head
3. Whom among the following you will prefer if you were to recruit new dealers for your bank dealing room?
  - a. Young science graduate with no banking experience**
  - b. Elderly experienced existing branch manager
  - c. A doctorate in international economics with two decades of teaching experience
  - d. The union leader who is good in bargaining
4. A treasurer of a corporate can avail different varieties of treasury products from the bank only if
  - a. Necessary ISDA agreement has been executed
  - b. The person who avails the facility is different from the person who has signed and forwarded the board resolution to the bank
  - c. Bank has sanctioned necessary limits for availing such products
  - d. All the above conditions have been pre-complied with**
5. To ensure that assets & liabilities are managed in any bank,
  - a. All larger credit proposals are sanctioned only by the treasury head
  - b. All credit proposals are routed through treasury
  - c. Treasury head is also the head of credit department
  - d. Treasury head is associated with ALCO**
6. Following is true in respect of nostro accounts maintained by banks
  - a. A bank can have only one nostro account in one currency

- b. Nostro accounts are always in the currency of the country of the account holder bank
  - c. **For dealing in a currency, bank needs nostro account in that currency**
  - d. Nostro account is maintained as RBI mandates the same for banks
7. Globally, US dollar dominates the currency for international trading. This means
- a. USA is the dominant trade partner globally
  - b. USA has the largest trade surplus globally
  - c. **Nostro accounts in USD are the most active**
  - d. US Banks have opened nostro accounts all over the world
8. For a bank in India, following is correct statement
- a. Vostro account is reconciled regularly
  - b. Nostro account is not maintained with banks who have Vostro accounts
  - c. Nostro account is the mirror image of Vostro account
  - d. **The currencies of nostro and Vostro accounts are always different**
9. A corporate treasurer maintains accounts with several banks in different banks.
- a. This results in additional cost to the corporate in the form of balances
  - b. This results in improved relationship with several banks
  - c. **Both the above may be true**
  - d. This is an impossible statement
10. Tax haven is
- a. **A place where there is tax advantage in the form of low or nil taxation**
  - b. A banking system in which interest earned is not reported to authorities
  - c. Where there are no financial regulators
  - d. Where there is an ideal taxation system
11. Following is not an organization belonging to 'world bank group'
- a. **WTO**
  - b. IFC
  - c. MIGA
  - d. IDA
12. Promoting exchange rate stability
- a. **Is a responsibility of IMF**
  - b. Is the overall objective of world bank
  - c. Is achieved by the central banks of various countries in consultation with IMF
  - d. Is not planned by anyone
13. Asian Development Bank [*mark the most appropriate choice*]
- a. Is a subsidiary of World Bank
  - b. **Helps member countries to reduce poverty**
  - c. Is headquartered in Singapore
  - d. Supports Government efforts only
14. System audit to ensure accurate accounting of deals done are needed primarily at
- a. Front office
  - b. Mid office
  - c. **Back office**

- d. Chief Dealer's office
15. Finacle, a product of Infosys is mainly for
- a. Treasury functions of a bank
  - b. Treasury functions of a corporate
  - c. Credit delivery functions of bank
  - d. Enabling CBS environment in banks**
16. When an exporter submits the documents to the bank before the dates mentioned in the relative forward contract [FC]
- a. It is referred as early delivery of FC**
  - b. It invariably results in cancellation of the FC
  - c. The documents are then not linked to the FC
  - d. The exporter will be penalized for default on the FC
17. The USD rate quoted today by the bank is: spot Rs 60; six months forward Rs 63. We can say that the USD
- a. Is at an annualized premium of 10%**
  - b. Is at an annualized discount of 10%
  - c. Is at an annualized premium of 5%
  - d. Is at an annualized discount of 5%
18. Which of the following statement is *not* true in respect of quotation of currency rates with reference to one another?
- a. The question of premium or discount arises only while quoting forward rates
  - b. If two currencies have same interest rate, then there should be no premium or discount between them
  - c. If a currency is pegged to another currency, then there is no premium or discount between them
  - d. When we say one USD is equal to Rs 60, it automatically means that USD is at premium.**
19. If the interest rate in a country is increased, conceptually speaking, its currency should
- a. Appreciate against other currencies**
  - b. Depreciate against other currencies
  - c. Not have any movement against other currencies
  - d. Face devaluation
20. An Indian importer has booked forward contract for his proposed imports. Before the actual import documents are received, the Indian rupee strengthens substantially.
- a. He will therefore incur a loss
  - b. He will earn a handsome profit
  - c. He is unaffected**
  - d. The bank will cancel the contract as per FEMA guidelines
21. An Indian exporter has sent the USD denominated 3 months usance export documents on collection basis. On the date of giving the documents to the bank, USD was being quoted at Rs 60. Forward premium for USD was 10% pa on that day. The spot rate on the day the bill realized was Rs 61. What is the exchange rate, bank will apply to this transaction?
- a. Rs 60

- b. Rs 61**
  - c. Rs 61.50
  - d. Rs 63
- 22. In the following situation, there is no case for existence of NDF market for a currency
  - a. The currency is fully convertible on current account
  - b. The currency is fully convertible on both capital and current account**
  - c. The interest rate of the currency is same as that for USD
  - d. The central bank of that country has not permitted NDF
- 23. The exchange rates of INR are decided by
  - a. RBI
  - b. FEDAI
  - c. SBI
  - d. Banks themselves**
- 24. Which of the following sentence is true relating to exchange rates quoted by banks?
  - a. FEDAI has not issued any guidelines
  - b. FEDAI daily issues guidelines fixing the prices
  - c. FEDAI guidelines are on the number of decimal places in the quoted rates**
  - d. Indirect exchange rate quotation is the method adopted by banks in India
- 25. The forward premium relating to a currency
  - a. Represents the future value of the currency
  - b. Represents the time value of the exchange rate
  - c. Is a mathematical function of the interest rate of the currency
  - d. Is directly related to the interest rate differential**
- 26. In a zero coupon bond,
  - a. There is no payout
  - b. There is no payout before maturity**
  - c. There is no yield
  - d. The holder does not have any interest rate risk
- 27. Zero coupon bonds are also known as
  - a. Zeroes
  - b. Deep discount bonds
  - c. ZCCs
  - d. Choices a & b above**
- 28. In case of a normal zero coupon bond with 10 years maturity
  - a. The average maturity is 10 years
  - b. The average maturity is less than 10 years**
  - c. The average maturity is more than 10 years
  - d. The average maturity depends on the terms of issue
- 29. Following is a correct statement with reference to yield curve
  - a. It is also called term structure of interest rate**
  - b. It plots coupon rates against different maturities
  - c. It is also called spot curve
  - d. It is a curve showing the yields

30. The price of a zero-coupon bond can be calculated by using the following formula:

$$P = M / (1+r)^n. \text{ Here } n \text{ represents}$$

- a. Number of years
  - b. Number of years until maturity
  - c. Number of years until maturity X 2**
  - d. Number of years until maturity / 2
31. If short term yields are higher than long term yields, the yield curve
- a. Slopes upwards
  - b. Slopes downwards**
  - c. Remains flat
  - d. Remains vertical
32. The only variety of duration which is measured in number of years is
- a. Macaulay duration**
  - b. Modified duration
  - c. Effective duration
  - d. None of the above
33. If a bond has a duration of 5 years and interest rate increases by 1%, then
- a. The bond price will decline by approximately 1%
  - b. The bond price will increase by approximately 1%
  - c. The bond price will decline by approximately 5%**
  - d. The bond price will increase by approximately 5%
34. In the measurement of VaR, there are three key elements which do *not* include the following:
- a. A specified level of loss in value
  - b. A fixed time period over which risk is assessed and a confidence interval
  - c. A confidence interval
  - d. The quantum of loss**
35. For a corporate, its fixed deposit kept with a bank is
- a. An interest sensitive rate asset class
  - b. Not an interest rate sensitive asset class even though it carries an interest**
  - c. An interest rate asset if it carries an interest rate
  - d. None of the above
36. If the VaR on an asset is \$ 100 million at a one-week, 95% confidence level, it means
- a. There is a only a 5% chance that the value of the asset will drop more than \$ 100 million over any given week**
  - b. That the value of the asset will drop more than \$ 100 million over any given week
  - c. There is a only a 5% chance that the value of the asset will drop more than \$ 5 million over any given week
  - d. During the next week, the assets will fall in value by \$ 100 million
37. While analyzing financial statements, Net profit before tax / total assets is a measure of
- a. Solvency
  - b. Liquidity

- c. Income
  - d. Overall efficiency**
38. In the bank branch's display board, there are variety of exchange rates mentioned such as spot TT & Bill under the head Imports and spot TT & Bill under the head Exports. A customer has received an inward remittance. What is the likely exchange rate the bank will apply to convert the FC into rupee for crediting to customer's account?
- a. The rate mentioned against Spot TT under Imports
  - b. The rate mentioned against Bill under Imports
  - c. The rate mentioned against Spot TT under Exports**
  - d. The rate mentioned against Bill under Exports
39. For a treasury dealer, the ticket size means
- a. The amount of FC a dealer puts through in a transaction in the interbank market
  - b. The standard minimum amount of FC a dealer puts through in a transaction in the interbank market**
  - c. The standard maximum amount of FC a dealer puts through in a transaction in the interbank market
  - d. The standard penalty amount for any violation of FEDAI guidelines in treasury transactions
40. Following is the most popular product offered by a forex treasury of a bank to its customers
- a. Credit Default Swaps
  - b. Foreign exchange forward contracts**
  - c. Interest rate swaps
  - d. Foreign exchange futures contracts
41. When a corporate wishes to set up its treasury which will manage the foreign exchange and domestic funds management of the corporate,
- a. It has to obtain RBI permission
  - b. It has to obtain SEBI permission
  - c. It has to obtain permission from its bank
  - d. It has to adhere to RBI guidelines through the bank**
42. Lock box facility offered by banks helps in
- a. Safe keeping of valuables by individuals
  - b. Collection of receivables by corporates**
  - c. Reducing cash float in the market
  - d. All the above
43. In a GDR issue, the following statement is true
- a. Custodian is situated in India and is appointed by the issuer company**
  - b. Depository is situated in India and is appointed by the issuer company
  - c. Custodian is the registered owner of the shares and is India
  - d. Custodian is situated outside India and holds the shares in its name
44. The following is true in case of dividend issued in respect of GDR holders
- a. The dividend is issued in favour of GDR holders in foreign currency
  - b. The GDR holders do not have any exchange risk

- c. **The issuing company pays the dividend in Indian rupee**
  - d. The custodian converts the dividend amount from INR to USD
45. Which of the following statement is true in respect of factoring and forfeiting services available in the market
- a. Factoring and forfeiting are alternatives available for export credit
  - b. Factoring and forfeiting are alternatives available for post shipment credit**
  - c. Factoring is an alternative for preshipment credit while forfeiting is an alternative for post shipment credit
  - d. Factoring and forfeiting services are not available in India
46. An Indian corporate has exported machinery for a large value on deferred credit basis to a country where there is foreign exchange repatriation issues. The corporate does not want to have any credit risk. It is best then for the corporate to
- a. Forfeit the export bills**
  - b. Factor the export bills
  - c. Discount the export bills through the bank
  - d. Abandon the export idea by cancelling the shipment
47. A certificate of deposit in Indian market
- a. Is issued by banks and FIs**
  - b. Is issued by corporates
  - c. Is considered as risk free investment
  - d. Carries the highest risk
48. Primary Dealers in securities market
- a. Perform the role of brokers arranging funds for participants
  - b. Are the primary traders in securities instruments
  - c. Are the issuers of Government securities
  - d. Are the merchant bankers to Government of India**
49. In a REPO transaction,
- a. One counterparty is invariably Reserve Bank of India
  - b. Both the counterparties have to be necessarily commercial banks
  - c. There is a borrowing and lending of funds taking place
  - d. The term REPO is from the perspective of party acquiring funds**
50. Which of the following is a true statement relating to REPO & REVERSE REPO transactions
- a. RBI uses these as instruments to manage solvency
  - b. Money market returns are achieved with near sovereign risk**
  - c. One bank with SLR surplus and another with SLR deficit form an ideal pair for these
  - d. Cash surplus banks cannot get benefitted by these
51. Which of the following is true of 'when issued market'?
- a. Market for securities yet to be issued but after announcement of the issue**
  - b. There is no such market
  - c. A market information indicating when securities will be issued
  - d. It is a market where trading takes place unofficially

52. The securities held by banks under SLR requirement are classified into three categories and following is *not* one of them
- Held for trading
  - Available for sale
  - Held to maturity
  - Held to sell**
53. Commodity markets exist in the form of
- OTC markets
  - Exchange based markets
  - Both OTC & Exchange based markets**
  - FMC allowed formats
54. When a corporate in India raises external commercial borrowings for meeting domestic expenses,
- The foreign exchange reserves of the country immediately increase**
  - The foreign exchange reserves of the country immediately decrease
  - There is no impact on the foreign exchange reserves
  - There is no forex risk to the corporate because of this
55. In the following case, the Indian corporate which raises external commercial borrowings does not have forex risk
- The borrowing is fully for import of machinery
  - The borrowing is for importing goods which will be exported
  - Forward contract is booked for its repayment**
  - Where the external commercial borrowing is of short term nature
56. As per SEBI guidelines, Alternative Investment Funds are categorized into different categories, based on their impact on the economy and the regulatory regime intended for them. The number of such categories is
- One
  - Two
  - Three**
  - Four
57. As per SEBI guidelines relating to Alternative Investment Funds, following is true
- They do not raise funds through private placement
  - There is no minimum amount of funds that can be accepted from an investor
  - There is a ceiling on the number of investors in any scheme**
  - All the above are true
58. As per RBI guidelines relating to portfolio management services [PMS],
- Banks need RBI permission for extending PMS**
  - Bank's fee for this service should relate to income earned by the client
  - A bank which accepts funds under PMS scheme can entrust it to another approved bank for funds management
  - The risk of return can be shared between bank and the client
59. Following is *not* a correct condition applicable to a bank which wishes to apply for a licence to function as Primary Dealer

- a. Minimum Net Owned Funds of Rs. 1,000 crore.
  - b. Minimum CRAR of 9 percent
  - c. Net NPAs of less than 3 percent
  - d. A profit making record for the last five years**
60. If an individual is interested in buying Government securities
- a. He can buy it from Government of India directly
  - b. He can buy it only from RBI
  - c. Banks are permitted to sell them to individuals**
  - d. There is no choice; individuals cannot buy such securities
61. When Foreign Exchange Regulation Act was replaced by Foreign Exchange Management Act, the following change happened:
- a. The violation of foreign exchange laws is no more criminal in nature
  - b. There is a clear definition of convertibility
  - c. There is no presumption of mens rea
  - d. All the above**
62. A cheque drawn on a bank is an example of
- a. Bill of exchange**
  - b. Promissory note
  - c. Usance promissory note
  - d. All the above
63. In Foreign Exchange Management Act 1999 [FEMA – replacing FERA], there is a clause referred to as ‘sun set clause’.
- a. This clause refers to the date on which the earlier Act came to an end
  - b. This clause refers to the date on which FEMA will come to an end
  - c. There is no such clause
  - d. It refers to the period within which offenses under FERA can be taken cognizance**
64. Following is true in reference to regulatory provisions
- a. FIMMDA is the regulator for money market participants
  - b. RBI is the regulator for Authorised Dealers**
  - c. SEBI is the regulator for banks which are listed on the stock exchange
  - d. IRDA regulates banks since they are now handling insurance business also
65. If you are the concurrent auditor for the treasury of a bank, you will check the reconciliation accuracy at
- a. The front office
  - b. The back office**
  - c. The mid office
  - d. Head Office of the bank
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## Section B

Number of questions: 7

Marks: 25

**Note: Answer any five questions. Each answer will carries 5 marks**

[Unrelated answers & answers exceeding the brief will attract negative marks]

1. Explain in not exceeding 10 sentences, the benefits of a commodity market

A good answer should cover the following points:

- Price Discovery – Assessment of fair value
- Price Risk Management – hedging the commonest method
- Import- Export competitiveness – hedging and committing
- Predictable Pricing – due to futures market
- Benefits for farmers/Agriculturalists – but only small percentage
- Credit accessibility – due to proper risk management
- Improved product quality – The existence of warehouses

2. Why electronic trading is gaining acceptance all over the world?

A good answer should cover the following points:

- Enhanced internal compliance for corporate clients around their FX trading
- Time saving
- Operationally and functionally easy to use - STP
- Convenience and control
- Comprehensive market access
- Transparency, competitive pricing and liquidity
- Precision pricing
- Place and monitor live orders

3. Good heavy machinery ltd has received an export order for US dollar 5 million for export of machinery to a private limited company in Gambia. While there is a good report on the buyer upto US dollar 3 million, there is uncertainty on the foreign exchange repatriability of the currency of the country. The profit margin is very high and hence the company does not want to miss the opportunity. Suggest alternatives for reducing the risk.

The answer should cover the following possible alternatives:

- Seek ECGC cover for the exports which will cover major portion of the exports [exact percentage depending on the details].
- Export under LC which should be got confirmed by a bank in India or in an acceptable third country
- See whether there is any developmental credit from say World Bank etc and if yes, try to route the export through that.

- If there is any line of credit from our own Exim Bank and if this export is eligible under that, explore that.
  - Insist for advance payment, though may not be feasible [atleast upto major portion of the export order]
  - Forfeiting the bills [i.e. without recourse]
4. An NGO duly registered under FCRA is receiving donations from India and abroad [mainly USA] regularly. While some amounts are small, there are a limited number of large amounts also. They are received both in the form of cheques and electronic remittances. What services of the bank will be useful to this NGO?

The good answer should describe the following services of the bank offered as part of cash management services:

- Banks offer cash letter services through its correspondent banks for collecting US Dollar cheques drawn on banks in USA. This is free of cost to customers and is quick in realization. Cheques received under this category can be collected without cost and delay.
  - Banks have arrangement for lock box arrangement with correspondent banks, mainly in USA. Under this facility, the remitters can draw the cheques favouring the NGO and along with the specified pay in slip [described in the bank's webpage], it can be deposited into this mail box in USA. This again has no cost [except a small local courier cost] to the remitter and is even faster.
  - Banks have electronic remittance arrangement with many banks in select countries, depending on the remittance flows. They are sometimes branded with special features. These can be used by the remitters.
  - Banks have SWIFT remittance arrangement with leading banks all over the world. The SWIFT codes are available in the webpages of the bank. Prospective remitters can use these.
5. Write short notes not exceeding 5 lines on each of the following:
- a. Sweeps
  - b. Volatility of a currency

The answers should cover the following:

- a. Sweeps: concept of sweep [i.e. moving balances across accounts], why it is helpful in managing funds, reducing interest cost or maximizing interest revenue, overview of sweep facility offered by banks [e.g. either for a fees or a minimum balance, at agreed frequency, reverse sweep to meet contingencies...] etc.
  - b. Volatility of a currency: means exchange fluctuating both ways rapidly both intraday and over a period of time, causes [economic like: interest rate movement, fundamentals like forex reserves, CA balance... & political like change in regime, liberalization, rumours...], opportunity to traders & treasurers, briefly role of IMF.
6. Describe the salient features of an NDF market displaying your understanding of the market, in not exceeding ten lines.

This is a text bookish question. The answer should cover what is an NDF market [currency traded outside its jurisdiction with only settlement of the differential] why NDF market comes into existence [viz.: non-resident investors & speculators trying to take advantage of currency movement when rules do not permit onshore intervention], how fuller convertibility automatically makes the market irrelevant, how it acts as indicator of future rate movement [e.g. without any imposed conditions or interventions, it becomes the beacon of the future] and therefore influences the onshore rate movement etc.

The good answer should display that the candidate has understood what an NDF market is & how it is different from an onshore market and briefly other aspects of this market.

7. Explain the concept of time value of money and how the concept is useful in money market for a treasurer. Answer should explain at conceptual level in not exceeding ten lines.

This is a knowledge based topic very familiar to any chartered accountant. The answer should not merely explain present value & future value but dwell on concept of compensation for depriving possession, what happens if interest rate is low or high [or even negative], how this concept is useful for comparing alternative investment classes available etc.

For a treasurer, this is extremely important because the price of G Sec moves because of the underlying interest rate which makes the PV into FV. The volume of assets handled is large and hence the concept is easily recognizable. In interbank settlement, any delay in receipt or payment of funds will affect the revenue due to this.

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### Section C

Number of questions: 2

Marks: 10

**Note: Case Studies. Answer any one.**

1. Bata Exim Ltd is a 15 years old trading company in variety of commodities from electronic gadgets to capital goods. Its annual turnover is in the range of Rs 1000 crores with CAGR of over 20%. Its business model is mainly importing from developed countries like Germany & USA and exporting to African & South East Asian countries. Since Bata is cash rich, it imports generally on cash basis and exports on usance basis. These terms make the exports very attractive to the prospective buyers. Bata is able to load enough margin because of the terms.

You have joined the company as the treasurer and the management has asked you to identify the risks if any in this model and suggest protective steps. Describe the same in generic terms.

Answer: the discussions should include the following:

- The credit risk is relatively higher due to profile of buyers. Bata should take care of this by taking ECGC policy or forfeiting the larger value bills on long terms, obtain prior credit report on any new buyer [from agencies like D & B] etc.
- Though the company is not borrowing, there may be opportunity losses. E.g. it could invest in India where returns could be much higher and use borrowed funds at lower overseas costs by taking advantage of arbitrage. Here the candidate should display knowledge of interest and exchange rate arbitration.
- In view of large size and cash rich status, Bata should take advantage of facilities offered by banks. Concessional rate is available for export credit which will be much lower than the investment return in India. Banks can organize buyers' credit if Bata decides to import on deferred terms, which will be beneficial on interest rate terms.
- Bata is likely to have currency risk on both its imports and exports. Since it is a trading firm, the net exposure may be nearly equal to the margin. But if the currency of imports and exports are different [which is likely to be the case], this netting advantage does not work. It is necessary to look at the exchange risk on both the imports and exports separately. That will also give scope for taking advantage of exchange rate movement currency wise.

2. Nag Fabrics Ltd is a family controlled quoted company engaged in manufacture & export of yarns as a 100% EOU. It has recently diversified into production and export of metal fabrication items using imported scraps. Its annual export turnover [which is around 75% of the total turnover] is around Rs 500 crores whereas its annual foreign exchange exposure is nearly double that. The company proposes to professionalize its exposure management and has decided to appoint you as a treasurer in the newly set up treasury of the company. As a first job, you need to write a risk management policy for the company. What essential features you will include in that?

There is no 'correct' answer for this because the policy document is company specific and discussions can only suggest what can be contained. The answer should start discussing what a risk management policy is, what it should in general contain and what are the specific issues relevant here. That will include:

- What is meant by risk management policy [i.e. a document explaining the philosophy of the company versus the risk faced and its own risk appetite], why it should be [it is not merely for making profit but also a ceiling on the urge to make profit so that the company is not adventurous...] and statutory requirement [ICAI guidelines on corporate governance, RBI guidelines relating to forex exposure, SEBI guidelines relating to capital issues].
- Clearly stating the objective. The objective is not merely making profit or that the treasury is a separate profit centre but it should stipulate to what extent, the company can take risk with specific limits on the exposure during the day, overnight, currency wise, counter party wise ... and also that there should not be any profit target for the dealers.
- Decide whether centralized or decentralized monitoring, if the company manages funds at more than one centre
- To cover the following critical parameters
  - Ranking of exposure priorities
  - Establishment of risk thresholds
  - Allocation of treasury responsibility for exposure management
  - Development of specific guidelines for control and reporting requirements
- Hedging policy e.g. not to hedge if loss is  $< x$ , cost is high, hedge not applicable etc. The policy can stipulate that all imports or exports above certain amount should be hedged through either forward contract or through any other derivative contracts, which are the derivative contracts that can be used etc.

Then it should discuss issues specific to this company viz.:

- Transition from family owned company to professionalized company means the owners delegating, which itself is a challenge. It should be recorded clearly to what extent and on what areas, the treasurer has to seek permission from the owners.

- The company has both imports and exports and hence there could be a desire to offset the receivable and payables in terms of FC. While this could be a possibility, estimate the amounts currency wise and time wise and see whether such natural hedging happens. Even if there is natural hedge, suggest whether the company can take advantage of selective hedging and attempt in making profits.
  - Whether the company is satisfied with hedging to the extent of exposures that internally arise or whether it desires to take extra risk by hedging based on past performance basis as allowed by RBI etc.
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