**NMIMS**

**Treasury management**

**Internal Assignment for June 2020 Examination**

**1. Explain the various approaches to measure risks. As a treasury manager of a bank, which approach will you follow to evaluate stress events of liquidity position of your bank**.

**Answer**: Risks in the organisation are usually considered as trade-off between reward and threat. Only if the risks are accepted, there will be greater opportunities to reap benefits. The main objectives of risk management include maximising profits, creating opportunities out of risks, protecting organisation’s assets etc. Risk management deals with balancing risks and controls. Banks are exposed to different types of risks that may have a negative effect on their business.

**Risk measurement by banks**

Management of risks enables the organisations to reduce risk levels in order to meet the profit targets. It deals with

**2. Explain duration GAP analysis in banks. Calculate the duration Gap of the following excerpts from the balance sheet of a bank. Also calculate the impact on the equity of the bank in the different interest rates scenarios**.

**Balance Sheet for Hypothetical Bank**

**Particulars Assets Duration Liabilities Duration**

**Current Assets 1000 7 years Current Liabilities 700 5 Years**

**Fixed Assets 300 Other Liab. 300**

**1300 Equity 300**

**1300**

**Scenarios for Impact analysis:**

**1. Interest rates increased by 1%**

**2. Interest rates decreased by 1%**

**Answer**: Gap analysis is a technique which is used to measure the interest rate risk. The unexpected changes occurring in interest rates which hamper the organisation’s profits and market value of equity can be measured using gap analysis. The various forms of gap analysis used for measuring interest rate risk are:

* **Duration gap analysis** – This method evaluates the sensitivity between the net worth market value of financial instruments to the changes in interest rates.

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**3. Maruti Suzuki Ltd. has imported machinery worth 1 million USD and the invoice is payable in 90 days. Current Spot rate in the market is USD/INR 75 while 90 Days forward is quoted at USD/INR 76. The prominent economists predict the spot rate after 90 days at USD/INR 76.5. Cost of Borrowing for Maruti in India is 10% and USD Interest Rate = 2%. A 90 days Call option with exercise price of USD/INR 75 for 100,000 USD is available at premium of INR 2. You are required to calculate impact on transaction exposure under following scenarios:**

**a. Company decides to use Forwards & Options for hedging**

**b. Company decides to use Money Market hedging**

**Answer**: a) i) At forward, obligation would be

$10,00,000\*76 = 7,60,00,000

ii) At call option

Call option of 75 bought at premium of Rs. 2

Initial amount paid for premium = $10,00,000\*2= 20,00,000

As spot rate after 90 days is 76.5 which is more than the call price i.e. Rs.75, hence, Maruti will exercise call at 75.