



**UNIVERSITI KUALA LUMPUR
BUSINESS SCHOOL**

**FINAL EXAMINATION
OCTOBER 2024 SEMESTER**

COURSE CODE	: EBB20603
COURSE NAME	: RISK MANAGEMENT IN ISLAMIC FINANCIAL INSTITUTIONS
PROGRAMME NAME	: BACHELOR OF BUSINESS ADMINISTRATION (HONS) IN ISLAMIC FINANCE
DATE	: 3 FEBRUARY 2025
TIME	: 2.00 PM – 5.00 PM
DURATION	: 3 HOURS

INSTRUCTIONS TO CANDIDATES

1. Please **CAREFULLY** read the instructions given in the question paper.
2. This question paper has information printed on both sides of the paper.
3. This question paper consists of **TWO (2) Sections; Section A and Section B.**
4. Answer **ALL** questions in **Section A and Section B.**
5. Please write your answers on the OMR answer sheet and answer booklet provided.
6. All questions must be answered in **English** (any other language is not allowed).
7. This question paper must not be removed from the examination hall.

SECTION A (Total: 40 marks)**INSTRUCTION: Answer ALL questions.****Please use the objective answer sheet provided.**

1. What is the primary principle of Islamic risk management?
 - A. Profit maximization
 - B. Risk elimination
 - C. Risk sharing
 - D. Speculation
2. How does Takaful operate in Islamic risk management?
 - A. Based on the principles of Riba
 - B. Through profit-sharing between the insured and insurer
 - C. Mutual contribution to a fund for loss coverage
 - D. By gambling on future risks
3. What is the main difference between conventional insurance and Takaful?
 - A. Takaful is profit-driven
 - B. Conventional insurance is based on speculation
 - C. Takaful operates on mutual cooperation, not profit maximization
 - D. Conventional insurance does not involve risk
4. The concept of *Al Kharaj Bid Dhaman* (Return assume liability) refers to _____.
 - A. the benefit from a certain thing is in return for the liability that accompanies that thing.
 - B. no reward without risk.
 - C. entitlement of gain to the responsibility of losses.
 - D. where the return gained is adequate to the risk borne.

5. What is the role of the Shariah Committee at the bank's level in Islamic risk management?
- A. Approves all speculative investment
 - B. Reviews and approves compliance with Islamic principles
 - C. Eliminates all forms of risk
 - D. Promotes gambling for higher returns
6. How we can say that the risk is manageable?
- A. When involved the types of risk that are inevitable, insignificant and unintentional
 - B. When it can occur loss and threats to the financial performance
 - C. Risk can be tolerated and become eliminated
 - D. The firm's financial performance faces deficits
7. Which principle governs the ethical practices of Islamic risk management?
- A. Profit maximization at all costs
 - B. Fairness, transparency, and risk-sharing
 - C. Avoidance of all types of risk
 - D. Focus on speculation
8. How to identify the risk in *Mudharabah* contract?
- A. During the process of application the applicant.
 - B. During the investment life of the agreement.
 - C. During the process of asset allocation.
 - D. During the process of capital contribution allocation
9. What is Islamic liquidity risk?
- A. The inability to generate profits
 - B. Difficulty in meeting short-term obligations in a Shariah-compliant manner
 - C. Excessive reliance on derivatives
 - D. Prohibition of profit-sharing

10. What is Commodity Murabahah often used for in Islamic liquidity management?
- A. Long-term investments
 - B. Short-term financing
 - C. Speculative purposes
 - D. Managing non-performing loans
11. What is the role of Bank Negara Malaysia in Islamic liquidity management?
- A. Issuing interest-based treasury bills
 - B. Providing Shariah-compliant liquidity facilities
 - C. Encouraging speculative trading
 - D. Promoting derivatives for risk management
12. Which financial tool is used by central banks for Islamic liquidity absorption?
- A. Interest-based treasury bills
 - B. Conventional repos
 - C. Sukuk
 - D. Derivatives contracts
13. Which type of Sukuk is commonly used for short-term liquidity management?
- A. *Ijarah* Sukuk
 - B. *Murabahah* Sukuk
 - C. *Musharakah* Sukuk
 - D. *Mudharabah* Sukuk
14. The major contribution of profit and loss earnings for Islamic bank operations is dependent on economic health. Moreover, given a signal of expansion and contraction of economic scenarios Islamic banks are also exposed to _____ for bank capital management.
- A. market risk
 - B. business risk
 - C. financial risk
 - D. credit risk

15. What is the role of asset-backed in Islamic finance in managing market risk?
- A. It guarantees fixed returns regardless of market conditions
 - B. It provides a real economic value to financial transactions
 - C. It eliminates all forms of risk
 - D. It allows speculative investments
16. What sort of information and data are needed in quantitative assessment?
- A. The past and current behaviour of the market
 - B. The past and current behaviour of the counterparty
 - C. Cumulative data in past year risk evaluation
 - D. Risk assessment in current competitors' events
17. The calculation of the expected and unexpected losses requires the calculation of a few components listed below, EXCEPT _____
- A. the probability of default (PD)
 - B. the loss given default (LGD)
 - C. the exposure at default (EAD)
 - D. the amend default (LAD)
18. Which of the following is a key impact of market volatility on Islamic financial institutions?
- A. Increased exposure to speculative investments due to reliance on derivatives
 - B. Fluctuations in the value of asset-backed investments, affecting portfolio performance
 - C. Greater reliance on interest-based instruments to manage liquidity
 - D. Higher profitability due to risk transfer mechanisms in Shariah-compliant contracts
19. Credit risk management can be done as listed below, EXCEPT _____.
- A. screening.
 - B. monitoring and enforcing restrictive covenants.
 - C. establishment of long-term customer relationships.
 - D. loan contribution.

20. Credit risk can be best defined as _____.

- A. risk due to uncertainty in the customer's/counterparty's ability to meet its obligation or failure to perform according to the terms and conditions of the credit-related contract.
- B. risk is the possibility that an individual or other entity will experience losses due to factors that affect the overall performance of investments in the financial markets.
- C. when the percentage of principal a lender charges for using its funds. The principal is the amount of cash granted.
- D. risk is the potential risk a business faces in pursuing its legitimate objectives.

SECTION B (Total: 60 marks)

INSTRUCTION: Answer ALL questions.

Please use the answer booklet provided.

Question 1

Value at Risk (**VAR**) is a statistical measure used to estimate the potential loss of a portfolio or investment over a specific time frame, given a certain confidence level. It is widely used in financial risk management to quantify and control the level of risk exposure.

- a) From your point of view, explain **THREE (3)** key components of VAR and **THREE (3)** applications in Islamic Risk Management.

(6 marks)

- b) Identify **THREE (3)** credit experts are important in hybrid model risk assessment.

(6 marks)

- c) Determine the VAR value and provide an explanation based on the following circumstances.

Portfolio value (V)	=	RM10,000,00
Portfolio standard deviation (σ)	=	2% daily volatility
Time horizon (T)	=	5 days
Confidence level	=	99% ($Z = 2.33$)

(8 marks)

Question 2

Appraise and justify the following scenarios based on the risk management method involved. Determine the recommendations to avoid any negative influence on Islamic financial institutions.

- a) In a *Murabahah* (**cost-plus financing**) contract, the Islamic financial institution faces credit risk if the client defaults on payment. This risk arises because the Islamic financial institutions have already purchased the underlying asset and delivered it to the client.

(5 marks)

- b) A *Mudharabah* (**profit-sharing**) investment exposes Islamic financial institutions to liquidity risk if there is a mismatch between asset maturity and cash flow obligations, especially during market downturns.

(5 marks)

- c) In an *Ijarah* (**leasing**) agreement, market risk arises when the value of the leased asset fluctuates or depreciates more rapidly than anticipated.

(5 marks)

- d) Ethical violations, such as investing in prohibited industries or mismanaging clients' funds can damage the institutions's reputation and erode customer trust.

(5 marks)

Question 3

- a) An Islamic financial institution has a *Murabahah* financing agreement with a client for RM1,000,000. The client has a 5% chance of defaulting within the next year. In case of default, the expected recovery rate from collateral is 70%. Calculate the Loss Given Default (**LGD**) and Expected Loss (**EL**) and justify the recommendations for mitigations.

(10 marks)

- b) Abu Dhabi Islamic Bank (**ADIB**) has provided a *Mudharabah* investment of RM2,000,000 to a business partner. The Probability of Default (**PD**) is estimated at 8%, and due to the low collateral value, ADIB expects to recover only 50% of the investment in case of default. Calculate the Loss Given Default (**LGD**), Exposure at Default (**EAD**), and Expected Loss (**EL**) and justify the recommendations for mitigations.

(10 marks)

END OF EXAMINATION PAPER