

**Commerce 4FN3
Financial Risk Management
Fall 2022 Course Outline**

**Finance and Business Economics Area
DeGroot School of Business
McMaster University**

COURSE OBJECTIVE

This course focuses on how to use derivative securities to manage financial risks. It includes a discussion of why firms should hedge financial market risk, identification, and quantification of financial risks; the value-at-risk (VaR) measure of risk; credit risk, and capital allocation and difference between speculation and hedging.

INSTRUCTOR AND CONTACT INFORMATION

Wednesday 8:30 – 11:20

Otto Yung

Instructor

yungo1@mcmaster.ca

Office: TBA

Office Hours: To be posted on course portal

Tel: To be posted on course portal

Class Location: Hamilton Hall (HH 305)

Student TA

Shubi Xie

xies38@mcmaster.ca

Office: TBA

Office Hours: TBA

Tel: To be posted on course portal

COURSE ELEMENTS

Credit Value:	3	Leadership:	Yes	IT skills:	Yes	Global view:	Yes
A2L:	Yes	Ethics:	No	Numeracy:	Yes	Written skills:	Yes
Participation:	Yes	Innovation:	Yes	Group work:	Yes	Oral skills:	Yes
Evidence-based:	Yes	Experiential:	Yes	Final Exam:	Yes	Guest speaker(s):	No

COURSE DESCRIPTION

This course studies the way companies, particularly financial institutions, manage risk (e.g., market risk, operational risk, and model risk). The nature of bank regulation and the Basel capital requirements are examined. Other topics include methods for monitoring volatilities and correlations, the calculation of economic capital, and RAROC. Some risk management cases will also be examined.

LEARNING OUTCOMES

Upon successful completion of this course, students will be able to complete the following key tasks:

- Apply risk measures such as VaR and Expected Shortfall for credit, market, and operational risk
- Apply volatility models (e.g., EWMA and GARCH) to calculate and back-test VaR
- Apply Basel standards for regulatory purposes
- Calculate regulatory and economic capital requirements

COURSE MATERIALS AND READINGS

Required: John C. Hull, Risk Management and Financial Institutions, 5th Edition, John Wiley & Sons Canada, 2018

Suggested: Peter Christoffersen, Elements of Financial Risk Management, 2nd Edition, Academic Press, 2011

COURSE OVERVIEW AND ASSESSMENT

Grades are a measure of the performance of a student in individual courses. Each student shall be judged on the basis of how well he or she has command of the course material.

Work Type	Deliverable	Weighting	Due Date
Individual	Mini-Quiz	10%*	Wednesday, October 5 th (in-class)
Individual	Assignment #1	15%	Saturday, October 29 th (11:59pm)
Group (3 to 4 members)	Case Write-Up, Debrief and Feedback	25%	Saturday, November 26 th (11:59pm)
Individual	Assignment #2	15%	Wednesday, December 7 th (11:59pm)
Individual	Final Exam	35%*	During Final Exam Period

* The total weight of the Mini-Quiz and the Final Exam combined will be 45% (note: the allocation will be one of the following: (i) 10% mini-quiz and 35% final exam or (ii) 5% mini-quiz and 40% final exam). The allocation will be based on the higher grade of the two allocations by each student.

COMMUNICATION AND FEEDBACK

Students who wish to correspond with instructors or TAs directly via email must send messages that originate from their official McMaster University email account. This protects the confidentiality and sensitivity of information as well as confirms the identity of the student. Emails regarding course issues should NOT be sent to the Area Administrative Assistants. All students must receive feedback regarding their progress prior to the final date by which a student may cancel the course without failure by default.

- *For Level 1 and Level 2 courses, this feedback must equal a minimum of 20% of the final grade.*
- *For Level 3 courses and above, this feedback must equal a minimum of 10% of the final grade.*

Instructors may solicit feedback via an informal course review with students by Week #4 to allow time for modifications in curriculum delivery.

REQUESTING RELIEF FOR MISSED ACADEMIC WORK

In the event of an absence for medical or other reasons, students should review and follow the Academic Regulation in the Undergraduate Calendar [“Requests for Relief for Missed Academic Term Work”](#) and the link below;

<http://ug.degroot.mcmaster.ca/forms-and-resources/missed-course-work-policy/>

ACADEMIC INTEGRITY

You are expected to exhibit honesty and use ethical behaviour in all aspects of the learning process. Academic credentials you earn are rooted in principles of honesty and academic integrity. **It is your responsibility to understand what constitutes academic dishonesty.**

Academic dishonesty is to knowingly act or fail to act in a way that results or could result in unearned academic credit or advantage. This behaviour can result in serious consequences, e.g., the grade of zero on an assignment, loss of credit with a notation on the transcript (notation reads: “Grade of F assigned for academic dishonesty”), and/or suspension or expulsion from the university.

For information on the various types of academic dishonesty please refer to the [Academic Integrity Policy](https://secretariat.mcmaster.ca/university-policies-procedures-guidelines/), located at <https://secretariat.mcmaster.ca/university-policies-procedures-guidelines/>

The following illustrates only three forms of academic dishonesty:

- plagiarism, e.g., the submission of work that is not one’s own or for which other credit has been obtained.
- improper collaboration in group work.
- copying or using unauthorized aids in tests and examinations.

AUTHENTICITY/PLAGIARISM DETECTION

Some courses may use a web-based service (Turnitin.com) to reveal authenticity and ownership of student submitted work. For courses using such software, students will be expected to submit their work electronically either directly to Turnitin.com or via an online learning platform (e.g., A2L, etc.) using plagiarism detection (a service supported by Turnitin.com) so it can be checked for academic dishonesty.

Students who do not wish their work to be submitted through the plagiarism detection software must inform the Instructor before the assignment is due. No penalty will be assigned to a student who does not submit work to the plagiarism detection software.

All submitted work is subject to normal verification that standards of academic integrity have been upheld (e.g., on-line search, other software, etc.). For more details about McMaster's use of Turnitin.com please go to www.mcmaster.ca/academicintegrity.

COURSES WITH AN ON-LINE ELEMENT

Some courses may use on-line elements (e.g., email, Avenue to Learn (A2L), web pages, TopHat, MS Teams, etc.). Students should be aware that, when they access the electronic components of a course using these elements, private information such as first and last names, user names for the McMaster e-mail accounts, and program affiliation may become apparent to all other students in the same course.

The available information is dependent on the technology used. Continuation in a course that uses on-line elements will be deemed consent to this disclosure. If you have any questions or concerns about such disclosure please discuss this with the course instructor.

ONLINE PROCTORING

Some courses may use online proctoring software for tests and exams. This software may require students to turn on their video camera, present identification, monitor and record their computer activities, and/or lock/restrict their browser or other applications/software during tests or exams. This software may be required to be installed before the test/exam begins.

CONDUCT EXPECTATIONS

As a McMaster student, you have the right to experience, and the responsibility to demonstrate, respectful and dignified interactions within all of our living, learning and working communities. These expectations are described in the [Code of Student Rights & Responsibilities](#) (the “Code”). All students share the responsibility of maintaining a positive environment for the academic and personal growth of all McMaster community members, **whether in person or online**.

It is essential that students be mindful of their interactions online, as the Code remains in effect in virtual learning environments. The Code applies to any interactions that adversely affect, disrupt, or interfere with reasonable participation in University activities. Student disruptions or behaviours that interfere with university functions on online platforms (e.g., use of Avenue 2 Learn, WebEx or Zoom for delivery), will be taken very seriously and will be investigated. Outcomes may include restriction or removal of the involved students’ access to these platforms.

ACADEMIC ACCOMMODATION OF STUDENTS WITH DISABILITIES

Students with disabilities who require academic accommodation must contact [Student Accessibility Services](#) (SAS) at 905-525-9140 ext. 28652 or sas@mcmaster.ca to make arrangements with a Program Coordinator. For further information, consult McMaster University’s [Academic Accommodation of Students with Disabilities](#) policy.

ACADEMIC ACCOMMODATION FOR RELIGIOUS, INDIGENOUS OR SPIRITUAL OBSERVANCES (RISO)

Students requiring academic accommodation based on religious, indigenous or spiritual observances should follow the procedures set out in the [RISO](#) policy. Students should submit their request to their Faculty Office **normally within 10 working days** of the beginning of term in which they anticipate a need for accommodation or to the Registrar’s Office prior to their examinations. Students should also contact their instructors as soon as possible to make alternative arrangements for classes, assignments, and tests.

COPYRIGHT AND RECORDING

Students are advised that lectures, demonstrations, performances, and any other course material provided by an instructor include copyright protected works. The Copyright Act and copyright law protect every original literary, dramatic, musical and artistic work, **including lectures** by University instructors.

The recording of lectures, tutorials, or other methods of instruction may occur during a course. Recording may be done by either the instructor for the purpose of authorized distribution, or by a student for the purpose of personal study. Students should be aware that their voice and/or image may be recorded by others during the class. Please speak with the instructor if this is a concern for you.

EXTREME CIRCUMSTANCES

The University reserves the right to change the dates and deadlines for any or all courses in extreme circumstances (e.g., severe weather, labour disruptions, etc.). Changes will be communicated through regular McMaster communication channels, such as McMaster Daily News, A2L and/or McMaster email.

RESEARCH USING HUMAN SUBJECTS

All researchers conducting research that involves human participants, their records or their biological material are required to receive approval from one of McMaster's Research Ethics Boards before (a) they can recruit participants and (b) collect or access their data. Failure to comply with relevant policies is a research misconduct matter. Contact these boards for further information about your requirements and the application process.

McMaster Research Ethics Board (General board): <https://reo.mcmaster.ca/>

Hamilton Integrated Research Ethics Board (Medical board): <http://www.hireb.ca/>

ACKNOWLEDGEMENT OF COURSE POLICIES

Your enrolment in Commerce **4FN3** will be considered to be an implicit acknowledgement of the course policies outlined above, or of any other that may be announced during lecture and/or on A2L. **It is your responsibility to read this course outline, to familiarize yourself with the course policies and to act accordingly.**

Lack of awareness of the course policies **cannot be invoked** at any point during this course for failure to meet them. It is your responsibility to ask for clarification on any policies that you do not understand.

COURSE SCHEDULE

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Session	Topic	Readings
Week 1 - September 7	Introduction & Financial Institutions	Chapters 1 to 5, 7
Week 2 - September 14	Value at Risk and Expected Shortfall	Chapter 12
Week 3 - September 21	Volatility	Chapter 10
Week 4 - September 28	Correlations and Copulas	Chapter 11
Week 5 – October 5	Regulation	Chapters 15 to 18
Midterm Recess (No class)		
Week 6 – October 19	Regulation (cont'd)	Chapters 15 to 18
Week 7 – October 26	Market Risk (Historical Simulation & EVT)	Chapter 13
Week 8 – November 2	Market Risk (Model Building Approach)	Chapters 14 and 9
Week 9 – November 9	Credit Risk and Credit Crisis	Chapters 19 to 21, 6
Week 10 – November 16	Credit Risk and Credit Crisis (cont'd)	Chapters 19 to 21, 6
Week 11 – November 23	Operational and Liquidity Risk, Economic Capital & RAROC	Chapters 23, 24 and 26

Week 12 – November 30	Enterprise Risk Management and Financial Innovation	Chapters 27 and 28
Week 13 – December 7	Week 12 (cont'd), Course Review	