October – December 2011

Vol. XL

Number 3

Operational Risk Management:
A Study of Practices in Indian Banks

Yogieta S Mehra

The paper investigates the practices followed by Indian banks for management of operational risk. Survey method comprising of questionnaires is used to explore the operational risk management practices employed by Indian banks. The study evaluates the present status of risk management approaches, human resource and outsourcing policies and hurdles in transition to advanced approaches amongst sample banks. Factor Analysis has been used to extract the key determining variables followed by hierarchical clustering leading to formation of three homogeneous clusters.

Global crisis has definitely heightened importance given to operational risk by Indian banks. Collection of external loss data, effectiveness of operational risk framework and internal controls, responsiveness of business to operational risk department is a concern with small and average sized public sector and old private sector banks. The human resource policies need restructuring to combat frauds and asset losses.

Dynamic Interrelationship between Stock and Foreign Exchange Markets:
Evidence from India

P Sakthivel
B Kamaiah

The study attempts to examine the dynamic interrelationship between BSE 30 Sensex and major five world exchange rates, namely, US dollar, Japanese yen, Singapore dollar, Euro and UK pound sterling. Data relating daily closing exchange rates of five countries and also BSE 30 Sensex are collected from 3rd January 2000 to 30th November 2010, and used in the analysis. Both short- and long-run relationships are examined through causality test, Engle Granger cointegration test, Error Correction Model (ECM), and Impulse Response Functions (IRF). The results of the Granger causality test show that there is unidirectional causality from BSE stock returns to US dollar returns and from Euro returns to BSE stock returns. The result of cointegration test discovers that BSE stock prices are found to be cointegrating with US dollar, Japanese yen and Euro, but not with Singapore dollar and pound sterling. Further, results suggests, BSE stock
prices lead US dollar, that indicates any shocks first gets reflected in Bombay Stock Exchange (BSE) and then transmits to US foreign exchange market. Finally, the result shows that most of the foreign exchange markets are found to be largely driven by their own innovations rather than shocks from BSE.

**Estimating the Tails:**
*Application of EVT in Indian Capital Market*

*Malay Kanti Roy*
*Hirak Roy*
*Surajit Ghosh*

Evidence of heavy tails in financial assets is plentiful and the present study also aims to explore tail behaviour of return distribution of Indian stock market. Indian experiences based on robust econometric technique suggest that return distribution of the market has fat tail thickness, it departs significantly from the assumption of normality and extreme values fit well in the theorem of Generalized Pareto Distribution. These findings are particularly important when modeling risk that specifically concentrates in large movements with little history.

**Book Review**

*India Infrastructure Report 2010: Infrastructure Development in a Low Carbon Economy*

*3i Network Infrastructure Development Finance Company*

Oxford University Press, New Delhi, Rs.645.00

Reviewed by Dr Vikas Srivastava, Associate Professor, National Institute of Bank Management, Pune.

**Booknote**

*Banks at Risk: Global Best Practices in an Age of Turbulence*

*Peter Hoflich*