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QUESTION 1

Which one of the following four statements best describes challenges of delta-normal method of mapping options positions?

Delta-normal method understates

A. Risks of long and short positions for both calls and puts.

B. Risks of long option positions for puts and overstates risks of short option positions for calls.

C. Risks of long option positions for calls and overstates risks of short option positions for puts.

D. Risks of short option positions and overstates risks of long option positions for both calls and puts.

Correct Answer: D

QUESTION 2

All of the following performance statistics typically benefit country\\'s creditworthiness EXCEPT:

A. Low unemployment

B. Low inflation

C. High degrees of investment

D. Low degrees of savings

Correct Answer: D

QUESTION 3

Which one of the following four features is NOT a typical characteristic of futures contracts?

A. Fixed notional amount per contract

B. Fixed dates for delivery

C. Traded Over-the-counter only

D. Daily margin calls

Correct Answer: C

QUESTION 4

What is a difference between currency swaps and interest rate swaps?

A. Currency swaps do not require the exchange of notional principal on maturity.

B. Currency swaps allow banks and customers to obtain the risk/reward profile of long-term interest rates without having to use long-term funding.

C. Currency swaps are OTC derivative contracts.

D. Currency swaps generate foreign exchange rate risk in addition to interest rate risk.

Correct Answer: D

QUESTION 5

If the yield on the 3-month risk free bonds issued by the U.S government is 0.5%, and the 3-month LIBOR rate is 2.5%, what is the TED spread?

A. 0.5%

B. -2.0%

C. 2.0%

D. 3.0%

Correct Answer: C

QUESTION 6

A proprietary trading desk for a large bank hedges an Arab light OTC forward position with Brent crude oil forwards. The trading desk benefits from using the most liquid OTC market to hedge, the market for the Brent crude, but hedging its using the Brent contract, exposes itself to the following type of risk:

A. Basis risk

B. Term risk

C. Correlation risk

D. Seasonality risk

Correct Answer: A

QUESTION 7

Using a forward transaction, Omega Bank buys 100 metric tones of aluminum for delivery in six-months\\' time. However, after two months, the bank becomes concerned with the potential fluctuations in aluminum prices and wants to hedge its potential exposure against a possible decline in aluminum prices. Which one of the following four strategies could the bank use to offset the risk from its current exposure to aluminum as it sets the price for selling the commodity in four-months\\' time?

A. Sell an aluminum futures contract

B. Buy an aluminum futures contract

C. Sell an aluminum forward contract

D. Buy an aluminum forward contract

Correct Answer: A

QUESTION 8

Which one of the four following statements about back testing the VaR models is correct? Back testing requires

A. Plotting VaR forecasts against the proportion of daily losses exceeding the average loss.

B. Comparing the predictive ability of VaR on a daily basis to the realized daily profits and losses.

C. Plotting the daily profit and losses along with the ranges predicted by VaR models

D. Determining the proportion of daily profits exceeding those predicted by VaR.

Correct Answer: B

QUESTION 9

Which of the following statements regarding CDO-squared is correct?

A. CDO-squared use other CDOs and CMOs as collateral.

II. Risk assessment of CDO-squared is almost impossible due to their complexity.

III. CDO-squared have lower credit risk than CMOs but higher than CDOs.

B. I only

C. I and II

D. II and III

E. I, II, and III

Correct Answer: B

QUESTION 10

Arnold Wu owns a floating rate bond. He is concerned that the rates may fall in the future decreasing his payment amount. Which of the following instruments should he buy to hedge against the fall in interest rates?

A. Interest rate floor

B. Interest rate cap

C. Index amortizing swap

D. Interest rate swap that receives floating and pays fixed

Correct Answer: A

QUESTION 11

Which one of the following four metrics represents the difference between the expected loss and unexpected loss on a credit portfolio?

A. Credit VaR

B. Probability of default

C. Loss given default

D. Modified duration

Correct Answer: A

QUESTION 12

Bank Omega is using futures contracts on a well capitalized exchange to hedge its market risk exposure. Which of the following could be reasons that expose the bank to liquidity risk?

A. The bank may not be able to unwind the futures contracts before expiration.

II. Prices may move such that a loss results on the hedge.

III. Since futures require margins which are settled every day, the bank could find itself scrambling for funds.

IV. Exchange margin requirements could change unexpectedly.

B. III, IV

C. I, III, IV

D. I, II, III, IV

E. I, IV

Correct Answer: A

QUESTION 13

For a bank a 1-year VaR of USD 10 million at 95% confidence level means that:

A. There is a 5% chance that the bank would lose less than USD 10 million in a year.

B. There is a 5% chance that the bank would lose more than USD 10 million in a year.

C. There is a 5% chance that the worst loss would be USD 10 million in a year.

D. There is a 5% chance that the least loss would be USD 10 million in a year.

Correct Answer: B

QUESTION 14

Which one of the following four statements about preferred shares is INCORRECT?

A. Preferred shares refer to a class of securities that is a cross between equity and debt.

B. Preferred shares represent residual of a corporation after its other liabilities have been paid.

C. Preferred shares are subordinated to debt.

D. Preferred shares can be perpetual or have maturities far exceeding debt maturities.

Correct Answer: B

QUESTION 15

To estimate the required risk-adjusted rate of return on a highly volatile energy stock, a risk associate

compiled the following statistics:

Risk-free rate = 5%

Beta = 2.5

Market Risk = 8%

Using the Capital Asset Pricing Model, she estimates the rate of return to be equal:

A. 10%

B. 15%

C. 25%

D. 40%

Correct Answer: C