2016-FRR[Q&As]

Financial Risk and Regulation (FRR) Series

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QUESTION 1

What are some of the drawbacks of correlation estimates? Which of the following statements identifies major problems with correlation calculations?

I. Correlation estimates are not able to capture increases in factor co-movements in extreme market scenarios.

II. Correlation estimates tend to be unstable.

III. Historical correlations may not forecast future correlations correctly.

IV.

Correlation estimates assume normally distributed returns.

A.

I and II

B.

I and IV

C.

I, II and III

D.

II, III, and IV

Correct Answer: C

QUESTION 2

Which of the following risk measures are based on the underlying assumption that interest rates across all maturities change by exactly the same amount?

I. Present value of a basis point.

II. Yield volatility.

III. Macaulay\\'s duration.

IV.

Modified duration.

A.

I and II

B.

I, II, and III

C.

I, III, and IV

D.

I, II, III, and IV

Correct Answer: C

QUESTION 3

A bank customer expecting to pay its Brazilian supplier BRL 100 million asks Alpha Bank to buy Australian dollars and sell Brazilian reals. Alpha bank does not hold reals so it asks for a quote to buy Brazilian reals in the market. The market rate is 100. The bank quotes a selling rate of 101 to its customer and sells the real at this quoted price. Then the bank immediately buys the real at the market rate and completes foreign exchange matched transaction. What is the impact of this transaction on the bank\\'s risk profile?

A. This transaction eliminates credit risk.

B. This transaction eliminates counterparty risk.

C. This transaction eliminates market risk.

D. This transaction eliminates operational risk.

Correct Answer: C

QUESTION 4

A bank has a large number of auto loans and would prefer to sell them to raise cash for more funding. However, selling individual auto loans is difficult. What could the bank do?

A. Package the loans into a securitized vehicle and sell the low risk portion of the portfolio.

B. Obtain a stronger credit rating so that the bank could borrow at a cheaper rate.

C. Set up a marketing team to sell individual loans to investors.

D. Merge with another bank.

Correct Answer: A

QUESTION 5

Which one of the following statements correctly identifies risks in foreign exchange forwards?

A. Short-term forward price fluctuations are driven by changes in the spot exchange rate, since most inter-country interest rates differentials are significant, and the effect of compounding is large for short periods of time.

B. Short-term forward price fluctuations are driven by changes in the spot exchange rate, since most inter-country interest rates differentials are small, and the effect of compounding is small for short periods of time.

C. Long-term forward price fluctuations are driven by changes in the spot exchange rate, since most inter-country interest rates differentials are small, and the effect of compounding is large for short periods of time.

D. Long-term forward price fluctuations are driven by changes in the spot exchange rate, since most inter-country interest rates differentials are significant, and the effect of compounding is small for short periods of time.

Correct Answer: B