

Section 1 - Section A

1) Credit Risk Assessment models are _____ methods to determine prospective borrower's probability of _____.

- A) quantitative.....default
 - B) qualitative.....success
 - C) qualitative.....default
 - D) quantitative.....success
-

2) Securitization enables financial institutions to _____ their long term loans and the associated risks to entities whose _____ are long term in nature.

- A) transfer.....assets
 - B) sell.....liabilities
 - C) sell.....assets
 - D) transfer.....liabilities
-

3) If on any date, if the spot exchange rate is equal to the strike price, then the option is _____.

- A) In the money
 - B) Money
 - C) At the money
 - D) Out of the money
-

4) As per KMV model, _____ the 'statistical distance', _____ is the probability of default.

- A) larger.....lower
- B) smaller.....lower
- C) larger greater
- D) smaller.....greater

5) In a European put option strike price is USD/CCU 72.00 at a premium of CCU 0.38 per USD, what is the spot price at which the holder is indifferent to whether exercise the options or not.

- A) 72.38
 - B) 72.83
 - C) 71.62
 - D) 72.00
-

6) If the expectation (as per pure expectation theory) is that yields will fall going forward. What happens to the flat yield curve then?

- A) Does not change
 - B) Shift in parallel
 - C) Slope upwards
 - D) Slope downwards
-

7) 'Protection Buyer' in a credit default swap wishes to _____ the risk associated with an asset (such as a loan) while 'Protection Seller' agrees to _____ that risk.

- A) take-on.....reject
 - B) shed.....take-on
 - C) take-on.....shed
 - D) shed.....reject
-

8) An independent Central Bank is insulated from _____ pressures hence more likely to work on _____ objectives such as price stability, stable exchange rate, etc.

- A) political.....short-term
 - B) economic.....short-term
 - C) economic.....long-term
 - D) political.....long-term
-

9) When a Bank sells a call option to an option buyer, the _____ of the option contract is shown as an _____ item in the books of the bank.

- A) Value.....on-balance-sheet
 - B) Value.....off-balance-sheet
 - C) Premium.....on-balance-sheet
 - D) Premium.....off-balance-sheet
-

10) 'Basis Risk' refers to risk arising from cost of _____ and yield on _____ being linked to different _____ rates.

- A) liabilities.....assets.....interest
 - B) liabilities.....assets.....benchmark
 - C) assets.....liabilities.....interest
 - D) assets.....liabilities.....benchmark
-

11) Change in the risk profile of the counterparties during the life of the Interest Rate Swap could _____ the fixed rate - floating rate advantage and hence put the Interest Swap Structure in _____.

- A) facilitate.....order
 - B) alter.....disarray
 - C) facilitate.....disarray
 - D) alter.....order
-

12) Eliminating liquidity risk requires the financial institution to hold assets that are highly _____, hence potential _____ in interest income.

- A) liquid.....increase
- B) liquid.....reduction
- C) priced.....increase
- D) priced.....reduction

13) If the domestic currency of a country appreciates, the firms in that country that source their components domestically will _____.

- A) benefit
 - B) lose
 - C) be indifferent
 - D) close down
-

14) Which of the following is/are true in the context of Translation Exposure:

- A) In the process of translating all the line items in the balance sheet of the foreign subsidiaries, there would always be an imbalance
 - B) The financial statements of the parent company to be restated in the foreign currency of the country where the foreign subsidiary is domiciled
 - C) The financial statements of the foreign subsidiary expressed in a foreign currency are to be stated in the foreign currency only
 - D) The financial statements of the foreign subsidiary expressed in a foreign currency are to be restated in the parent company's reporting currency
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15) Long-term debt in the balance sheet are not translated at the current exchange rate under _____ method of translation.

- A) Current Rate
 - B) Monetary/Non-Monetary
 - C) Current/Non-Current
 - D) Temporal
-

16) 'Credit risk' reflects the _____ in the quality of assets of a financial institution and consequent potential _____ to the financial institution.

- A) improvement.....loss
 - B) deterioration.....gain
 - C) No change.....gain
 - D) deterioration.....loss
-

17) Advanced Measurement Approach to operational risk requires the Bank to define _____ loss events in every _____ of the bank.

- A) potential.....business
 - B) definite.....business
 - C) definite.....transaction
 - D) potential.....transaction
-

18) 'Mark-to-market' loss on investments in bonds means the current price is _____ than the price at which the bonds were purchased.

- A) Equal
 - B) Higher
 - C) Not related
 - D) Lower
-

19) The results of a stress test showed that almost 50% of the large banks were declared to have inadequate _____ to cope with a crisis, although all of those banks met the mandated _____ requirements.

- A) capital.....capital adequacy
 - B) liquidity.....statutory liquidity
 - C) liquidity.....capital adequacy
 - D) capital.....statutory liquidity
-

20) All open positions in the futures exchange are governed by _____ mechanisms, to eliminate the risk of defaults (by participants) devolving on the _____.

- A) monitoring.....participants
- B) margining.....exchange
- C) monitoring.....exchange
- D) margining.....participants

Section 2 - Section B

21) Credit rating involves a detailed assessment of the following aspects of the securitization portfolio:

- i. Quality of loans in the securitization portfolio
- ii. Solvency of the borrower
- iii. Legal structure of the portfolio
- iv. Prepayment risk
- v. Solvency of the issuer

Select all that apply.

- A) i, ii, iii and iv
 - B) i, iii, iv and v
 - C) i, ii, iii and v
 - D) ii, iii, iv and v
-

22) In asset securitization, the Special Purpose Vehicle (SPV) performs which of the following functions:

- i. Fund the receivables
- ii. Manage the securitization portfolio
- iii. Issue the asset backed securities to investors
- iv. Trade in the asset backed securities

Select all that apply.

- A) Only iv
- B) Only ii
- C) Both ii and iii
- D) Both i and iv

23) Cash inflows for any financial institution would not include:

- i. Fresh deposits from customers
- ii. Disbursement of fresh loans
- iii. Interest income from loans
- iv. Proceeds from sale of bonds
- v. Interest paid to depositors

Select all that apply

- A) Both ii and iv
 - B) Both iii and iv
 - C) Both i and iii
 - D) Both ii and v
-

24) Central banks have mandated that financial institutions that come out unfavourably in the stress test should do the following:

- i. Pay higher dividends
- ii. Ensure higher plough-back
- iii. Rework their business plan
- iv. Increase the size of their assets portfolio

Select all that apply

- A) Both i and iii
- B) Only iii
- C) Both ii and iii
- D) Only iv

25) Which of the following are applicable to a futures transaction:

- i.Can be bought and sold only through an 'Exchange'
- ii.Identity of Counterparty is known
- iii.Settlement is guaranteed by the exchange
- iv.Price discovery is transparent

Select all that apply

- A) i, ii, and iii
 - B) i, iii and iv
 - C) ii, iii and iv
 - D) i, ii and iv
-

26) Pillar- 1 under Basel II covers which of the following risks:

- i.Liquidity risk
- ii.Operational risk
- iii.Credit risk
- iv.Solvency risk
- v.Market risk

Select all that apply.

- A) i, iii and v
- B) ii, iii and v
- C) ii, iv, and v
- D) i, ii and iv

27) _____ variability in the exchange rate between two currencies implies _____ foreign exchange risk.

- i.high.....low
- ii.high.....high
- iii.low.....high
- iv.low.....low

Select all that apply.

- A) Only iii
 - B) Both ii and iv
 - C) Only ii
 - D) Both ii and iii
-

28) Operational risk in a financial institution could result from:

- i.Breakdown in the institution's information technology platform
- ii.Exponential increase in non-performing loans
- iii.Terrorist attack on the institution's fixed assets
- iv.Increase in fixed assets
- v.Inadequate internal processes

Select all that apply.

- A) i, ii and iv
- B) iii, iv and v
- C) i, iii and v
- D) i, ii, and iii

29) Investors in a securitization portfolio receive cash flows whenever:

- i. Borrowers meet their periodic loan repayment obligations
- ii. Borrowers pre-pay/pre-close their loans
- iii. Servicing agent fulfills the periodic loan repayment obligations
- iv. Servicing agent (the Originator) make good the loss by invoking the available credit enhancement

Select all that apply.

- A) Both ii and iii
 - B) Only iii
 - C) i, ii and iii
 - D) i, ii and iv
-

30) In the context of Risk Weighted Assets, rank order the following in ascending order of risk-weight:

- A. Unsecured loans given by a bank
- B. Cash
- C. Mortgage loans
- D. Investment in government securities (Treasury Bonds)
- E. Investment in corporate bonds issued by AAA rated firms

- A) D --> C --> E --> B --> A
- B) E --> D --> B --> A --> C
- C) B --> D --> C --> E --> A
- D) B --> C --> D --> A --> E

31) Net Demand and Time Liabilities (NDTL) would be the sum of:

- i. Positive Net Inter Bank Liabilities (NIBL)
- ii. Long Term liabilities
- iii. Current and Savings Account
- iv. Time Deposits
- v. Negative Net Inter Bank Liabilities (NIBL)

Select all that apply.

- A) i, ii, and iii
 - B) ii, iii and iv
 - C) i, iii and iv
 - D) i, ii and iv
-

32) Early warning of likely default could be indicated by which of the following:

- i. Delays in repayment of loan (principal or interest) by the borrower
- ii. Significant increase in credit turnover in the borrower's bank account
- iii. Significant decrease in debit turnover in the borrower's bank account
- iv. Actual financial performance vs financial projections

Select all that apply.

- A) i, ii, and iii
- B) i, iii and iv
- C) i, ii and iv
- D) ii, iii and iv

33) Which of the following would be classified as risk sensitive assets or as risk sensitive liabilities in the balance sheet of a financial institution?

- i.Home mortgages
- ii.Investment in bonds
- iii.Cash
- iv.Commercial loans
- v.Off-balance sheet asset

Select all that apply.

- A) i, iii and iv
 - B) i, ii, and iii
 - C) ii, iii and iv
 - D) i, ii and iv
-

34) The major manifestations of Subprime mortgages were:

- i.Home loans given to people who were creditworthy
- ii.Banks started to lend willy-nilly as they became very flagrant and adventurous
- iii.Banks had a perverse incentive to give as many housing loans as they wanted to because they would then be able to sell it as Mortgage backed securities in the financial markets
- iv.Loans were given to customers who would otherwise not even be eligible for a loan

Select all that apply.

- A) Both ii and iii
- B) i, ii, iii and iv
- C) i, ii and iii
- D) ii, iii and iv

35) To hedge against a loan of CCU 100 million that the firm wishes to take three months from now, its CFO is like to use the futures market. Place the following actions in the correct sequence in order to help him hedge the risk:

- a) Borrow CCU 100 million in the spot market three months from now;
- b) Sell CCU 100 million in the futures market now;
- c) Buy CCU 100 million in the futures market three months from now.

- A) a --> b --> c
- B) b --> a --> c
- C) a --> c --> b
- D) c --> b --> a

Section 3 - Section C

36) A US firm has exported goods to a Utopian importer worth CCU 100,000 today for which the payment is due 90 days hence.

Based on the rates prevailing today:

- CCU/USD spot rate: 0.5750
- CCU/USD 90 day Forward Rate: 0.5720
- CCU 90-day interest rate 5.70% per annum
- USD 90-day interest rate: 3.60% per annum

How much USD cash flow can the US firm realize today using the money market hedge?

- A) 57589
 - B) 56692
 - C) 57208
 - D) 56976
-

37) A Bond with a face value of CCU 100 is currently trading at CCU 103, coupon rate 8% to be paid annually. The bond has a yield to maturity of 7% p.a. and has three more years coupon payments to maturity. What is the duration of the bond?

- A) 2.631
- B) 2.887
- C) 2.776
- D) Need more information

38) A Bank has the following table of credit score parameters:

Parameters	Score				
Annual Gross Income (in CCU)	< 100,000	100,000 - 300,000	300,000 - 500,000	500,000 - 1,000,000	> 1,000,000
	0	10	20	30	40
Age	< 25	25 - 35	35 - 45	45 - 60	> 60
	10	20	35	20	10
Academic Credential	High School	Under-graduate	Graduate or Higher		
	5	15	25		
Current Debt Service Ratio	> 50%	35 - 50%	15 - 35%	5% - 15%	< 5%
	0	10	20	35	50
Credit Bureau Score (FICO)	300 - 600	600 - 725	725 - 850		
	0	10	20		
Major Credit Cards	None	One or More			
	0	10			
Nature of Current Relationship with the Bank	None	Savings Account	Savings A/C + Other		
	0	30	50		
Current Residence	Rent	Own, Mortgage	Own, Outright		
	5	20	40		
Length of Service in Present Job	< 1	1 - 5 years	> 5 years		
	0	15	30		
Maximum Possible Score	300				

Below information belongs to a customer:

- Length of service in present job: 11 years
- Age: 38 years
- Has only a savings account with the Bank
- Holds two credit cards
- Graduate from a recognized University
- Currently living in a rented home
- Current FICO score : 650
- Current Annual gross income: CCU 575,000
- Current DSR: 30%

What would be the computed credit score for this customer based on the above information?

- A) 145
- B) 215
- C) 195
- D) 180

39) The average return on a Portfolio of loan is 22% and the standard deviation is 35%. There is another loan that gives a return of 28% with a standard deviation of 42%. If the correlation coefficient is 0.27 and equal weightage on the new portfolio, calculate the return and risk for the 'New Portfolio'.

- A) Return=25 ; Risk=29.17
 B) Return=26 ; Risk=31.28
 C) Return=26 ; Risk=29.77
 D) Return=25 ; Risk=30.75

40) Please go through the summarized balance sheet of a Bank given below and answer the questions that follow:

<u>Assets</u>		<u>Risk Weight</u>
Investment in Treasury & Municipal Bonds	500	5%
Investment in Corporate Bonds	700	100%
Commercial Loans (Unsecured)	1000	100%
Mortgage Loans	900	60%
Fixed Assets	600	0%
Cash	100	0%
TOTAL ASSETS	3800	

<u>Liabilities</u>	
Equity Capital	55
Retained Earnings	125
Provision for Bad Loans	150
Subordinated Debt	50
Customer Deposits	3420
TOTAL LIABILITIES	3800

<u>Off-Balance Sheet Items</u>		<u>Risk Weights</u>	<u>Conversion Factor</u>
Letter of Credit Issued	1000	100%	50%
Foreign Exchange Contracts	1000	100%	15%
Interest Rate Swaps	500	100%	10%

Compute the Capital Adequacy Ratio based on the above information.

- A) 11.15%
 B) 12.82%
 C) 12.14%
 D) 11.67%

41) Data for the last two years interest rate for a 15 day (fortnight) deposit is:

- (a) Mean value of 6%
- (b) Standard deviation of 0.60%
- (c) 26 fortnights in a year

Estimate the likely interest rate range (maximum and minimum) for a 15 day deposit commencing the coming fortnight at 95% (two sigma) confidence level.

- A) 6.235 - 5.765
- B) 6.142 - 5.553
- C) 6.432 - 6.292
- D) 6.325 - 5.597

42) Based on the balance sheet data below for the Bank of Utopia, analyze the interest rate risk pertaining to assets and liabilities whose maturity is one year or less:

Abridged Balance Sheet of Bank of Utopia		(All figures in CCU Million)	
<u>Liabilities</u>		<u>Assets</u>	
1.0 Equity Capital	200	1.0 Consumer Loans	2175
Retained Earnings	500	< 1 yr	1050
		1 to 2 years	400
2.0 Inter-bank Borrowings	875	> 2yrs	725
(< 1year)		2.0 Home Mortgages	770
3.0 Call Money (Fed Funds)	325	Floating(Variable) Rate	520
4.0 Deposits from Customers		Fixed Rate	250
4.1 Transaction Accounts (Cur & Sav)	500	3.0 Investment in Bonds & Securities	1630
4.2 Certificate of Deposits	2600	< 1 yr	890
Variable Rate CDs	950	1 to 2 years	250
Fixed Rate CDs (< 1 year)	500	> 2yrs	490
Fixed Rate CDs (1 year-2yrs)	300	4.0 Fixed Assets	275
Fixed Rate CDs (> 2 yrs)	850	5.0 Cash	150
Total Liabilities	5000	Total Assets	5000

The Treasurer wishes to evaluate the impact on the Bank's net interest income, should interest rate be reduced by 0.75%. Based on past data, the Treasurer believes that:

- At least 35% of the fixed rate, home mortgages will be 'pre-closed' when the interest rate falls by 0.75%
- 25% of the Current and Savings Account (transaction accounts) are also rate sensitive

Estimate the impact on the bank's net interest income, based on the above information.

- A) Increase by 1706250
- B) Reduce by 236250
- C) Increase by 2362500
- D) Reduce by 1706250

Answer Keys**Question Paper No: 60913_8**

1	A	22	C
2	B	23	D
3	C	24	C
4	D	25	B
5	D	26	B
6	D	27	B
7	B	28	C
8	D	29	D
9	B	30	C
10	B	31	C
11	B	32	B
12	B	33	D
13	B	34	D
14	D	35	B
15	C	36	B
16	D	37	C
17	A	38	C
18	A	39	D
19	A	40	C
20	B	41	A
21	B	42	A