PRM Certification - Exam III: Risk Management Frameworks, Operational Risk, Credit Risk, Counterparty Risk, Market Risk, ALM, FTP - 2015 Edition

1. For a corporate bond, which of the following statements is true:

A. I, II and IV

B. III and IV

C. III only

D. IV only

Answer(s): B

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2. Which of the following is not an approach used for stress testing:

A. Algorithmic approaches

B. Historical scenarios

C. Monte Carlo simulation

D. Hypothetical scenarios

Answer(s): C

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3. Which of the following represents a riskier exposure for a bank: A LIBOR based loan, or an Overnight Indexed Swap? Which of the two rates is expected to be higher?

A. A LIBOR based loan; OIS rate will be higher

B. Overnight Index Swap; LIBOR rate will be higher

C. A LIBOR based loan; LIBOR rate will be higher

D. Overnight Index Swap; OIS rate will be higher

Answer(s): C

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4. A risk analyst analyzing the positions for a proprietary trading desk determines that the combined annual variance of the desk's positions is 0.16. The value of the portfolio is $240m. What is the 10-day stand alone VaR in dollars for the desk at a confidence level of 95%? Assume 250 trading days in a year.

A. 12595200

B. 157440000

C. 6297600

D. 31488000

Answer(s): D

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5. Company A issues bonds with a face value of $100m, sold at $98. Bank B holds $10m in face of these bonds acquired at a price of $70. Company A then defaults, and the recovery rate is expected to be 30%. What is Bank B's loss?

A. $7m

B. $4m

C. $2.1m

D. $4.9m

Answer(s): B

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6. As part of designing a reverse stress test, at what point should a bank's business plan be considered unviable (ie the point where it can be considered to have failed)?

A. Where EBITDA for the year is forecast to be negative

B. Where large known losses have been incurred on the bank's positions

C. When the regulatory capital of the bank has been exhausted

D. When the realization of risks leads market participants to lose confidence in the bank as a counterparty or a business worthy of funding

Answer(s): D

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7. Which of the following statements is true in respect of different approaches to calculating VaR?

A. I, II, III and IV

B. I and IV

C. II and III

D. III only

Answer(s): C

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8. Under the standardized approach to calculating operational risk capital under Basel II, negative regulatory capital charges for any of the business units:

A. Should be ignored completely

B. Should be offset against positive capital charges from other business units

C. Should be included after ignoring the negative sign

D. Should be excluded from capital calculations

Answer(s): B

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9. For a 10 year interest rate swap, what would be the worst time for a counterparty to default (in terms of the maximum likely credit exposure)

A. 10 years

B. Right after inception

C. 2 years

D. 7 years

Answer(s): D

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10. When compared to a low severity high frequency risk, the operational risk capital requirement for a medium severity medium frequency risk is likely to be:

A. Zero

B. Lower

C. Higher

D. Unaffected by differences in frequency or severity

Answer(s): C

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11. A bullet bond and an amortizing loan are issued at the same time with the same maturity and with the same principal. Which of these would have a greater credit exposure halfway through their life?

A. Indeterminate with the given information

B. They would have identical exposure half way through their lives

C. The amortizing loan

D. The bullet bond

Answer(s): D

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12. Which of the following credit risk models includes a consideration of macro economic variables such as unemployment, balance of payments etc to assess credit risk?

A. KMV's EDF based approach

B. The CreditMetrics approach

C. The actuarial approach

D. CreditPortfolio View

Answer(s): D

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13. A Monte Carlo simulation based VaR can be effectively used in which of the following cases:

A. When returns data cannot be analytically modeled

B. When returns are discontinuous or display large jumps

C. Where analytical methods are too complex to effectively use

D. All of the above

E. D

Answer(s): E

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14. If P be the transition matrix for 1 year, how can we find the transition matrix for 4 months?

A. By calculating the cube root of P

B. By numerically calculating a matrix M such that M x M x M is equal to P

C. By dividing P by 3

D. By calculating the matrix P x P x P

Answer(s): B

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15. If the annual variance for a portfolio is 0.0256, what is the daily volatility assuming there are 250 days in a year.

A. 0.0101

B. 0.4048

C. 0.0006

D. 0.0016

Answer(s): A

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16. The sum of the stand alone economic capital of all the business units of a bank is:

A. less than the economic capital for the firm as a whole

B. more than the economic capital for the firm as a whole

C. equal to the economic capital for the firm as a whole

D. unrelated to the economic capital for the firm as a whole

Answer(s): B

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17. Under the contingent claims approach to credit risk, risk increases when:

A. II and III

B. I and III

C. I, II and III

D. I and II

Answer(s): B

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18. Fill in the blank in the following sentence:

A. Covariance

B. Correlation

C. Volatility

D. Positive semi-definite

Answer(s): D

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19. The returns for a stock have a monthly volatilty of 5%. Calculate the volatility of the stock over a two month period, assuming returns between months have an autocorrelation of 0.3.

A. 8.062%

B. 7.071%

C. 5%

D. 10%

Answer(s): A

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20. An error by a third party service provider results in a loss to a client that the bank has to make up. Such as loss would be categorized per Basel II operational risk categories as:

A. Execution delivery and process management

B. Outsourcing loss

C. Business disruption and process failure

D. Abnormal loss

Answer(s): A
