8.02 Forward Commitment and Contingent Claim Features and Instruments

Question 1
Which of the following forward commitments is *least likely* to expose investors to default?
A. Swaps
B. Futures
C. Forwards

Question 2
If the credit protection buyer of a credit default swap (CDS) chooses a cash settlement after a credit event, the required payment from the credit protection seller is *most likely*:
A. established by an auction after the credit event.
B. negotiated between the counterparties after the credit event.
C. a preset amount of money established at the creation of the CDS.

Question 3
An investor sells a European call for GBP 3 with a strike price of GBP 50. Based only on this information, which of the following *best* describes the investor's loss potential?
A. Unlimited loss
B. Loss of GBP 3
C. Loss of GBP 47

Question 4
Which of the following factors *least likely* contributes to the liquidity of futures contracts?
A. Daily price limits
B. Contract standardization
C. Exchange clearinghouse

Question 5
A trader takes a long stock futures position and deposits the initial margin requirement in cash under the following circumstances:

Selected Data (in €)	
Futures price	150
Initial margin	15
Maintenance margin	6

If the next futures settlement price is €140, the amount of the margin call issued to the trader is *closest* to:
A. €1
B. €9
C. €10

Question 6
A call option with an exercise price of €60 is purchased for €4. At expiration, if the price of the underlying is €70, then the call buyer's profit (in €) is *closest* to:
A. −4
B. 6
C. 10

Question 7
A European call option with an exercise price of €45 is sold for €3. If the price of the underlying is €52 at expiration, the call seller's profit (in €) is *closest* to:
A. −7
B. −4
C. 4

Question 8
A European put option with an exercise price of €85 is selling for €5. At expiration, if the put seller's profit for the short position is €2, then the underlying spot price is *closest* to:
A. €78
B. €82
C. €88

Question 9
On the day of expiration, a European call option with an exercise price of USD 50 has an underlying asset with a value of USD 57. If USD 2 was paid to purchase the option, the call buyer's profit is *closest* to:
A. USD −7
B. USD 5
C. USD 7

Question 10
Daily price limits are *most likely* a feature of:
A. swaps.
B. futures.
C. forwards.

Question 11
A European put option with an exercise price of $120 is selling for $10. If the price of the underlying is $112 at expiration, then a put buyer's profit at expiration (in $) is *closest* to:
A. −10
B. −2
C. 8

Question 12
The credit protection buyer in a credit default swap *most likely* pays:

A. a series of payments in return for a promise of compensation if a credit event occurs.
B. a one-time premium for the right to benefit from an increase in a bond's credit spread.
C. the interest, principal, and appreciation on a specific bond in return for a fixed or variable rate.

Question 13
The named third party of a credit default swap suffers a credit event that results in payment to the credit protection buyer. The event is *least likely* to be which of the following?
A. A reduction in credit rating
B. A failure to make a scheduled payment
C. An involuntary restructuring of a debt contract

Question 14
A trader fails to meet a margin call on a long futures position, and before the position can be liquidated fast markets result in additional losses greater than the account balance. The amount the trader owes the clearinghouse is *most likely*:
A. the full value of the futures contract.
B. the losses in excess of previous margin deposits.
C. zero, since losses are limited to the initial margin.

Question 15
An investor sells a European call option for €7 with a strike price of €150 on a stock trading at €140 with 3 months to expiration. Based on only this information, if the stock is trading at €145 at expiration, the seller's profit (in €) is *closest* to:
A. 2
B. 5
C. 7

Question 16
Which of the following is *least likely* to be a feature of futures contracts? Buyers and sellers:
A. must meet initial margin requirements.
B. negotiate the quantity of the underlying asset.
C. use a clearinghouse as their legal counterparty.

Question 17
On the day of expiration, a European put option's underlying asset has a price of GBP 83. The option's exercise price is GBP 76, and the put buyer paid GBP 3 to purchase the option. The payoff to the put buyer is *closest* to:
A. GBP −3
B. GBP 0
C. GBP 7

Question 18
If a put option holder exercises the option, the original put option seller:

A. is obligated to sell the underlying asset.
B. is obligated to buy the underlying asset.
C. has the right to buy the underlying asset.

Question 19
Which of the following derivatives is *most likely* to require periodic payments equal to the net difference between its two payment streams?
A. Interest rate swap
B. Credit default swap
C. Forward rate agreement

Question 20
An investor sells a European put with a strike price of EUR 100 for EUR 5. At expiration, the underlying stock is trading at EUR 90. Based only on this information, the investor's profit (in EUR) is *closest* to:
A. −5.
B. 5.
C. 15.

Question 21
Payments of gains and losses on futures contracts are *most likely* made:
A. daily.
B. only at expiration.
C. as negotiated by the counterparties.

Question 22
Which of the following *best* describes the maximum potential gains and losses on a short put at expiration?
A. Limited gains and limited losses
B. Limited gains and unlimited losses
C. Unlimited gains and unlimited losses

Question 23
The margin deposits required to hold futures contracts are *best* described as:
A. down payments.
B. contract premiums.
C. performance bonds.

Question 24
Options are *most likely* considered contingent claims due to:
A. sellers paying a premium that depends on future actions.
B. buyers having a right, but no obligation, to trade the underlying asset.
C. uncertainty regarding the counterparty's ability to meet contractual obligations.

Question 25
For a trader with no positions in the underlying asset or related options, the maximum gain on a short call is *best* described as:
A. unlimited.
B. the premium received.
C. the strike price less the premium received.

Question 26
Which of the following *best* describes the effect of daily price limits in futures trading? Price limits:
A. reduce risk by capping the leverage on futures positions.
B. facilitate arbitrage pricing of futures by stabilizing futures prices.
C. define the trading range around the previous day's settlement price.

Question 27
Which of the following is *most likely* a feature of contingent claims but not forward commitments?
A. Symmetric payoffs
B. A nonzero initial value
C. An exchange of obligations by the counterparties

Question 28
Which of the following is *least likely* to contribute to minimizing the default risk of futures contracts?
A. Daily price limits
B. Contract standardization
C. Exchange clearinghouses

Question 29
For a trader with no position in the underlying asset or related options, the maximum loss on a short put is *best* described as:
A. unlimited.
B. the strike price.
C. the strike price minus the premium.

Question 30
A company has a floating-rate loan with a bank but would prefer to pay a fixed rate instead. The company should *most appropriately* enter into a:
A. total return swap.
B. plain vanilla swap.
C. credit default swap.

Question 31
An investor purchases a call option on a stock with a strike price of 120 for a premium of 6 when the stock is trading at 118. If the stock is trading at 124 at the option's exercise, the investor's profit is *closest* to:
A. −2
B. 0
C. 4

Question 32
When a call option is exercised, the short call position *most likely* has:
A. a right to sell.
B. an obligation to sell.
C. an obligation to buy.

Question 33
The counterparty credit risk exposure of fixed-for-floating interest rate swaps is *most likely* the:
A. notional principal of the swap.
B. value of the fixed rate payment stream.
C. difference between the two payment streams.

Question 34
When losses on a long futures position result in a margin call, the amount due is *most likely* the money required to:
A. buy the underlying asset.
B. return the account balance to the initial margin.
C. return the account balance to the maintenance margin.