Question #1 of 4

Question ID: 1469218

A corporation that employs hedge accounting and uses an interest rate swap to offset changes in the value of fixed rate bond liability is said to be employing a:

A) cash flow hedge.

B) net investment hedge.

C) fair value hedge.

Explanation

Using an interest rate swap to hedge changes in the value of a balance sheet liability is considered a fair value hedge. If the interest rate swap is used to convert the fixed-rate payments on a bond liability to floating-rate payments, it would be considered a cash flow hedge.

(Module 50.1, LOS 50.b)

Question #2 of 4

Question ID: 1469219

Hedge accounting with a net investment hedge *most likely* refers to a company that is using derivatives to reduce the volatility of:

A) a balance sheet liability.

B) its net working capital.

C) the value of a foreign subsidiary.

Explanation

A hedge using foreign currency derivatives to hedge the reported value (in domestic currency) of the equity of a foreign subsidiary is termed a net investment hedge.

(Module 50.1, LOS 50.b)

Question #3 of 4

Question ID: 1469217

A corporation that employs hedge accounting and uses derivatives to reduce the volatility of the value of its inventory is *most likely* using a:

A) net investment hedge.

B) fair value hedge.

C) cash flow hedge.

Explanation

Using derivatives to hedge the changes in value of inventory is considered a fair value hedge.

(Module 50.1, LOS 50.b)

Question #4 of 4

Question ID: 1469220

A bond portfolio manager who wants to decrease the duration of her portfolio would *most appropriately*:

A) enter an interest rate swap as the floating rate payer.

B) enter an interest rate swap as the fixed rate payer.

C) take a long position in government bond futures.

Explanation

The pay fixed side of an interest rate swap is equivalent to issuing a floating rate bond and purchasing a fixed rate bond, which will reduce the portfolio duration, effectively substituting a floating rate bond for a fixed rate portfolio bond. A long position in government bond futures will have gains when yields go down and losses when yields go up, increasing the portfolio duration.

(Module 50.1, LOS 50.b)