

**1. Correct Answer: C.**

The maximum loss to the long is the premium. The payoffs of contingent claims are not linearly related to the underlying, and only one party, the short, can default.

**2. Correct Answer: A.**

A is correct. Derivative markets are not necessarily more or less volatile than spot markets. Derivative markets reveal prices and volatilities of the underlying assets and facilitate risk management.

B is incorrect. One of the main purposes of derivative markets is risk management

C is incorrect. One of the main purposes of derivative markets is price discovery.

**3. Correct Answer: B.**

Forward rate agreements are used to hedge interest rate exposure present in the money market.

**4. Correct Answer: A.**

Clearing houses arrange for financial settlement of trades. In futures markets, they guarantee contract performance.

**5. Correct Answer: A.**

Buying a put is most similar to a short position in the underlying asset because the put increase the value if the underlying asset value decreases. The writer of a put and the holder of call have a long exposure to the underlying asset because their positions increase in value if the underlying asset value increase.