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Exam : **2016-FRR**

Title : Financial Risk and Regulation
(FRR) Series

Vendor : GARP

Version : DEMO

NO.1 On January 1, 2010 the TED (treasury-euro dollar) spread was 0.9%, and on January 31, 2010 the TED spread

is 0.4%. As a risk manager, how would you interpret this change?

- A.** The decrease in the TED spread indicates a decrease in credit risk on interbank loans.
- B.** Increase in credit risk on T-bills.
- C.** Increase in interest rates on both interbank loans and T-bills.
- D.** The decrease in the TED spread indicates an increase in credit risk on interbank loans.

Answer: A

NO.2 Which one of the following four statements regarding floating rate bonds is incorrect?

- A.** Floating rate bonds only have a small degree of interest rate risk.
- B.** Floating rate bonds are very sensitive to changes in interest rates.
- C.** Floating rate bonds typically have less price risk than fixed rate bonds.
- D.** Floating rate bonds have coupon payments tied to floating interest rates or floating interest rate indexes.

Answer: B

NO.3 Asset and liability management is typically concerned with all of the following activities:

- I.** Maintaining the desired liquidity structure of the bank.
- II.** Managing the factors affecting the structure and composition of a bank's balance sheet.
- III.** Effectively transferring the interest rate risk in the banking book to the investment bank at a fair transfer price.
- IV.** Focusing on the circumstances impacting the stability of income the bank generates over time.

A. I

B. I, II, IV

C. II, III

D. III, IV

Answer: B

NO.4 The pricing of credit default swaps is a function of all of the following EXCEPT:

- A.** Duration
- B.** Market spreads
- C.** Probability of default
- D.** Loss given default

Answer: A

NO.5 The main building blocks of an operational risk framework include all of the following options EXCEPT:

- A.** Scenario analysis
- B.** Loss data collection
- C.** Compliance document preparation
- D.** Risk and control self-assessment

Answer: C

NO.6 When the cost of gold is \$1,100 per bullion and the 3-month forward contract trades at \$900, a commodity trader seeks out arbitrage opportunities in this relationship. To capitalize on any arbitrage opportunities, the trader could implement which one of the following four strategies?

- A. Take long positions in both physical gold and futures contract
- B. Take a long position in physical gold and short-sell the futures contract
- C. Short-sell physical gold and take a long position in the futures contract
- D. Short-sell both physical gold and futures contract

Answer: C

NO.7 Suppose that a regulator deems all corporate debt to have the same risk level. Which of the following behavior of banks would be an example of regulatory arbitrage?

- A. Banks increase their exposure to corporate debt.
- B. Banks shift their exposure to more risky corporate debt.
- C. Banks shift their exposure to less risky corporate debt.
- D. Banks decrease their exposure to corporate debt.

Answer: B

NO.8 To estimate a partial change in option price, a risk manager will use the following formula:

- A. Partial change in option price = Delta x Gamma x (1+ Change in underlying price)
- B. Partial change in option price = Delta x Gamma x Change in underlying price
- C. Partial change in option price = Delta x Change in underlying price
- D. Partial change in option price = Delta x (1+ Change in underlying price)

Answer: C

NO.9 US-based BetaBank have accumulated Japanese yen, Japanese government bonds, options on Japanese yen, and positions in commodities that have a positive correlation with yen. Which one of the four following non-statistical risk measures could be used to evaluate the BetaBank's exposure to the Japanese economy?

- A. Position turnover
- B. Position sensitivities
- C. Position concentrations
- D. Position volatility

Answer: C

NO.10 Which one of the following areas does not typically report into a central operational risk function?

- A. Geopolitical and strategic planning

- B. Business continuity planning
- C. Embedded operational risk coordinators or specialists or managers
- D. Information security

Answer: A

NO.11 ThetaBank has extended substantial financing to two mortgage companies, which these mortgage lenders use to finance their own lending. Individually, each of the mortgage companies have an exposure at default (EAD) of \$20 million, with a loss given default (LGD) of 100%, and a probability of default of 10%. ThetaBank's risk department predicts the joint probability of default at 5%. If the default risk of these mortgage companies were modeled as independent risks, the actual probability would be underestimated by:

- A. 3%
- B. 4%
- C. 1%
- D. 2%

Answer: B

NO.12 Which one of the four following aspects of legal risk is NOT included in the Basel II Accord?

- A. Private settlements
- B. Exposure to fines
- C. Negative publicity resulting from reputational damages
- D. Punitive damages resulting from supervisory actions

Answer: C

NO.13 In the United States, Which one of the following four options represents the largest component of securitized debt?

- A. Credit card loans
- B. Real estate loans
- C. Education loans
- D. Lines of credit

Answer: B

NO.14 Which one of the four following statements about technology systems for managing operational risk event data is incorrect?

- A. Operational risk event databases are independent elements of the operational risk management framework.
- B. Operational risk event databases are always integrated with the other components of the operational risk management program.

C. The implementation of a new operational risk event loss database has to incorporate an analysis of the advantages and disadvantages of external systems.

D. Operational risk loss event data collection software can be internally developed.

Answer: B

NO.15 Which one of the following four statements correctly defines credit risk?

A. Credit risk is the risk arising from execution of a company's strategy.

B. Credit risk is a form of performance risk in contractual relationship.

C. Credit risk is the risk that summarizes the exposures a company or firm assumes when it attempts to operate within a given field or industry.

D. Credit risk is the risk that complements market and liquidity risks.

Answer: B

NO.16 Short-selling is typically associated with the following risks:

I. Potential for extreme losses

II. Risk associated with the availability of shares to borrow

III. Market behavior risk

IV. Liquidity risk

A. I, II

B. II, IV

C. I, II, III, IV

D. I, III

Answer: C

NO.17 Mega Bank holds a \$250 million mortgage loan portfolio, which reprices every 5 years at LIBOR + 10%. The

bank also has \$150 million in deposits that reprices every month at LIBOR + 3%. What is the amount of Mega

Bank's rate sensitive assets?

A. \$250 million

B. \$200 million

C. \$150 million

D. \$100 million

Answer: A

NO.18 Which of the following statements is a key difference between customer loans and interbank loans?

A. Customer loans are easier to sell than interbank loans

B. Customers are less credit-worthy than banks on average and hence yields are higher on average for customer loans as compared to interbank loans

C. Customer loans are of shorter duration than interbank loans

D. Interbank loans are more customized than commercial loans

Answer: B

NO.19 What is the role of market risk management function within a bank?

- I. Control and minimize the risks the bank should take.
- II. Establish a comprehensive market risk policy framework.
- III. Define, approve and monitor risk limits.
- IV. Perform stress tests and other qualitative risk assessments.

A. II, III, and IV

B. I, II and III

C. I and III

D. II and IV

Answer: A

NO.20 Which of the following statements presents an advantage of using risk and control self-assessments (RCSA) in the operational risk framework?

- I. RCSA provides very accurate scoring of risks and controls due to its subjective nature.
- II. RCSA program provides insight into risks that exist in a firm, but that may or may not have occurred before.
- III. RCSA program can produce biased but transparent operational risk reporting.
- IV. RCSA program allows each department to take ownership of its own risks and controls.

A. I and III

B. I, II and III

C. II, III, and IV

D. II and IV

Answer: D

NO.21 Which of the following attributes of duration gap model typically cause criticism?

- I. Basis risk
- II. Errors in the linear model
- III. Costs of immunization
- IV. Constant nature of calculation

A. I, III, IV

B. I, II

C. II, III, IV

D. I, II, III

Answer: D

NO.22 According to Basel II what constitutes Tier 1 capital?

- A.** Profits to reserves and innovative Tier 1 capital
- B.** Equity capital and accrued profits to reserves
- C.** Core capital and innovative Tier 1 capital.

D. Equity capital and core capital

Answer: C

NO.23 What is a difference between currency swaps and interest rate swaps?

- A.** Currency swaps generate foreign exchange rate risk in addition to interest rate risk.
- B.** Currency swaps do not require the exchange of notional principal on maturity.
- C.** Currency swaps allow banks and customers to obtain the risk/reward profile of long-term interest rates without having to use long-term funding.
- D.** Currency swaps are OTC derivative contracts.

Answer: A

NO.24 Which one of the following four statements about the "market-maker" trading strategy is INCORRECT?

- A.** This risk in this strategy is that traders have to take positions that may quickly incur a loss.
- B.** This strategy is independent of market liquidity and number of other market makers.
- C.** A market maker can benefit from the market information she gets from the trades she is asked to execute.
- D.** A market maker that attracts buy and sell orders can make a profit from the spread quoted between the buy and sell price.

Answer: B

NO.25 Alpha Bank, a small bank, has a long position with larger BetaBank and has an identical short position with another larger bank GammaBank. Each large bank requires a 20% initial collateral to support the trade. As prices fluctuate in either direction, one large bank will require additional collateral from the small bank, while the risk of loss to the other large bank will increase. By running the trades through a clearinghouse, the small bank can achieve all of the following objectives EXCEPT:

- A.** Mitigating option hedging risks and altering margin requirement
- B.** Protecting against the risk of the failure of one of the large banks
- C.** Eliminating the collateral requirement
- D.** Protecting itself against increases in future collateral demands

Answer: A