CCRA

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CCRA

Exam A

QUESTION 1
Case Facts as on March 31, 2012

Mark Construction Company (MCC) has bagged a contract for construction of a large dam and hydro power project on river Shiva in Madhya Pradesh (MP). The project is also of relevance from the irrigation perspective due to its location and as per the agreement MCC will have to undertake construction of web of canals, approach road to dam, power house and other ancillary units. MCC is promoted by Mr. Thomas Mark, who is a MP from the ruling party which recently formed government in MP. Historically, MCC has been engaged into construction of rural roads, small bridges and railway platforms on contract basis for the Government. MCC will have a separate special purpose vehicle (SPV) floated for this venture.

The hydro power project comes under the public private partnership scheme of the Government of MP, where in the private partner builds owns operates and transfers (BOOT) the hydro power plant. The detailed terms of the hydro power project agreement are as follows:

1. The construction of the dam, canals and hydro power plant shall be undertaken by the contractor. The Government of MP will have to acquire land which will submerge on construction of dam and shall rehabilitate the owners of land.

2. MCC shall have right to operate the hydro power project from date of commencement of commercial operations (DCCO) for a period of 20 years and shall transfer the project to Government thereafter. Further, SPV shall be tax exempt for a period of five years from DCCO i.e. FY17-FY21.

3. The power project is of 600 megawatts (MW) shall comprise 4 units of 150 MW each. The estimated cost of project is about INR3, 500 Million to be spent over a period of 4 year(s) the project is estimated to be commercially operational by April 1, 2016 with two units operational om same day and one unit each will be operational on April 1, 2017 and April 1, 2018.

4. Means of finance:

Means of Finance	INR Million
Government Aid (To be classified as Equity)	500
Equity	900
Debt	2100

Means of Finance INR Million
Government Aid (To be classified as Equity) 500Equity 900 Debt 2100
5. Amount if expenditure estimated in various years is as follows:

				Funding		
Cost of Project	INR Million		Debt	Govt Aid	Equity	Total
FY13 (April to march)	700		0	250	450	700
FY14	1200		500	250	450	1200
FY15	1200		1200	-		1200
FY15	400		400	-		400

Debt shall bear a fixed rate of interest of 10% and all interest till DCCO shall be added to the principal. The expected principal along with capitalized interest is expected to be INR2, 400 Million (i.e.INR2100 Million debt plus INR300 Million capitalized interest). The repayment of the same shall be in 12 equated annual installments starting from FY17.

Brief projections for the period of FY17 to FY21 are given below:

Particular	FY17	FY18	FY19	FY20	FY21
Revenue from Power sale	600	900	1200	1320	1452
EBITDA %	72%	68%	65%	60%	60%
Interest Cost	240.00	220.00	200.00	180.00	160.00
Depreciation	175.00	175.00	175.00	175.00	175.00
PAT	17.00	217.00	405.00	437.00	536.20

Developments as on March 31, 2015

The project manager for the SPV made following comments at a press conferee on March 31, 2015:

As you all are aware, we were running bang on schedule till we last met on December 21, 2014. From today we are just left with one more year to complete the project in time. However, the flash floods which struck our dam site on this March 15, 2015 have created havoc in the region. I shall not point out the loss of lives in the region as you all are well aware of those. Our project has also been badly hit due to the same and we have been assessing the damage over the last one week. After analyzing damage, we have made changes in project schedule. Now we will be making only one unit of 150 MW operational on April 1, 2016 and 1 unit each will be added in each of subsequent year(s).

Development as on September 30, 2015
Post the flash floods, lot of environmentalists started raising issues of changes in environment due to construction of large number of dams. A few Public Interest Litigations (PILs) have been filed in various courts.

Honorable High Court of MP on September 27, 2015, banned construction of any dams in the region and banned permissions for new dams till next hearing scheduled on November 30, 2015. MCC in its press release has indicated that they will apply to the higher court on the matter.

Based on the initial projections, do scenario analysis assuming only 75% capacity is utilized in FY17 and FY18 and thereby revenues will be proportionally reduced.
Compute DSCR under such scenario for FY17 and FY18, assuming other things remain constant?

A. FY17: 0.85; FY18: 1.26
B. FY17: 0.74; FY18: 1.09
C. FY17:1.35; FY18: 2.09
D. FY17:0.98; FY18: 1.46

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 2
Case Facts as on March 31, 2012

Mark Construction Company (MCC) has bagged a contract for construction of a large dam and hydro power project on river Shivna in Madhya Pradesh (MP). The project is also of relevance from the irrigation perspective due to its location and as per the agreement MCC will have to undertake construction of web of canals, approach road to dam, power house and other ancillary units. MCC is promoted by Mr. Thomas Mark, who is a MP from the ruling party which recently formed government in MP. Historically, MCC has been engaged into construction of rural roads, small bridges and railway platforms on contract basis for the Government. MCC will have a separate special purpose vehicle (SPV) floated for this venture.

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2. MCC shall have right to operate the hydro power project from date of commencement of commercial operations (DCCO) for a period of 20 years and shall transfer the project to Government thereafter. Further, SPV shall be tax exempt for a period of five years from DCCO i.e. FY17-FY21.

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4. Means of finance:

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Honorable High Court of MP on September 27, 2015, banned construction of any dams in the region and banned permissions for new dams till next hearing scheduled on November 30, 2015. MCC in its press release has indicated that they will apply to the higher court on the matter.

After the developments of March 31, 2015, assuming revenues are directly linked to the power production and the EBITDA margins remain intact for the year, as were projected, compute the revised interest coverage ratio for FY17 and FY18?

A. FY17: 0.90; FY18: 1.85
B. FY17: 1.85; FY18: 2.93
C. FY17: 0.49; FY18: 0.97
D. FY17: 1.80; FY18: 2.78

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 3
Scott is a credit analyst with one of the credit rating agencies in India. He was looking in Oil and Gas Industry companies and has presented brief financials for following 4 entities:

Particulars	A Ltd	B Ltd	C Ltd	D Ltd
Total Income	2000	2400	3000	3500
EBITDA	500	550	650	460
Interest	100	100	125	130
Total Debt	1000	1400	1000	1500

Giving equal weightage to all three ratios, determine which of the above entities should be rated highest on a relative scale.

A. C Ltd
B. A Ltd
C. D Ltd
D. B Ltd

Correct Answer: A

Section: (none)
Explanation

Explanation/Reference:

QUESTION 4
Scott is a credit analyst with one of the credit rating agencies in India. He was looking in Oil and Gas Industry companies and has presented brief financials for following 4 entities:

Particulars	A Ltd	B Ltd	C Ltd	D Ltd
Total Income	2000	2400	3000	3500
EBITDA	500	550	650	460
Interest	100	100	125	130
Total Debt	1000	1400	1000	1500

From the data given below, calculate the standard deviation of the credit portfolio assuming that facility's exposure is known with certainty, customer defaults and LGDs are independent of one another and LGDs are independent across borrower(s).

Credit Facility A – Loss Equivalent Exposure of $60m, expected Default frequency of 1.5%, loss given default of 30%, Std Deviation of LGD – 5% and Correlation to portfolio – 0.10

Credit Facility B – Loss Equivalent Exposure of $25m, expected Default frequency of 2%, loss given default of 12%, Std Deviation of LGD – 12% and Correlation to portfolio – 0.45

Credit Facility C – Loss Equivalent Exposure of $15m, expected Default frequency of 5%, loss given default of 85%, Std Deviation of LGD – 18% and Correlation to

portfolio – 0.22

A. US$6.88 million
B. US$ 1.16 million
C. US$ 1.66 million
D. US$ 0.10 million

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:
QUESTION 5
Following is information related banks:

Auckland Ltd is a public sector bank operating with about 120 branches across India. The bank has been in business since 1971 and has about 40% branches in rural areas and about 75% of all branches are in Western India. On the basis of the size, Auckland Ltd will be ranked at number 31 amongst 40 banks in India. Although top management has appointment period of 5 years, generally they retire on ach sieving age of 60 years with an average tenure of only 2 years at the top job.

Profit and Loss Account

Particulars	FY11	FY12	FY13
Interest on advances bills	124,000	182.000	283,000
Interest on investments	15,000	18,000	14,000
Interest on balances with Banking Regulator and other inter-bank funds	1, 100	1,000	1,700
Other interest income	40,000	49,000	54,000
Other Income	80,000	95,000	99,000
Total Income	260,100	345,000	451,700
Interest expenses	105,000	148,000	235,000
Operating expenses	23,000	28,000	32,000
Total expenditure	128,000	176,000	267,000
Operating Profit	155,100	197,000	216,700
Provisions	72,000	102,000	174,000
Profit before tax	83,100	95,000	42,700
Tax	16,600	19,000	8,500
Profit after Tax	66,500	76,000	34,200

Balance Sheet

Assets	March 31 2011	March 31 2012	March 31 2013
Cash and Balances with Reserve Bank of India	120,000	420,000	770,000
Balances with Banks and Money at Call and Short Notice	745,000	789,000	1194,000
Investments	598,000	689,000	1139,000
Advances	1432,000	1709,000	2485,000
Fixed Assets	223,000	234,000	245,000
Other Assets	567,000	670,000	970,000
TOTAL	3685,000	4511,000	6803,000

Liabilities	March 31 2011	March 31 2012	March 31 2013
Capital	31,000	31,000	42,000
Reserves and Surplus	294,000	370,000	1154,000
Deposits	2100,000	2120,000	2450,000
Borrowings	960,000	1590,000	2657,000
Other Liabilities and Provisions	300,000	400,000	500,000
TOTAL	3685,000	4511,000	6803,000

The rating wise break-up of assets for FY11 is as follows:

Rating	FY11
AAA	120,000
AA	530,000
A	220,000
BBB	150,000
BB and below	310,000
Unrated	102,000
Total	1432,000

Computer risk weighted assets for Auckland Ltd for FY11:

A. 10,10,000 Million
B. 13,24,500 Million

C. 11,64,500 Million
D. 11,60,000 Million

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 6
Ms. Mary Brown is a credit rating analyst. She had prepared a detailed report on one of her client, FlyHigh Airlines Ltd, a company operating chartered aircrafts in India. As she was heading for a meeting with her superior on the matter, coffee spilled over her set of prepared paper(s). As she was getting late for meeting, instead of preparing entire set she could recollect few numbers from her memory and reconstructed following partial financial table:

Period Ended	FY10	FY11	FY12
Working Results			
Total Income			
EBITDA			
Interest			
Depreciation	20.00	25.00	30.00
Effective Tax Rate	20%	24%	25%
PBT			
PAT			
Financial Position			
Net Worth	370.00	430.00	535.67
Total Debt	743.00		
Ratios			
Growth			
Growth in Total Income (%)		25%	15%
Growth in EBITDA (%)		30%	20%
Growth in PAT (%)		20%	
Profitability			
EBITDA Margins		32%	
PAT Margins			
RONW			
Solvency			
Overall Gearing Ratio		2.2	
Interest coverage ratio	3.2		3.1
Total Debt / EBITDA		4.5	5.2

An analyst comparing two competitors Comp Systems and Big Tables gathers the data below:

Cash Conversions Cycle:
Comp Systems: 18 days and Big Tables 32 days

Defense Interval Ratio:
Comp Systems: 50 and Big Tables: 20

What can the analyst conclude regarding the liquidity of these companies?

A. Both indicators suggest that Comp Systems is more liquid than Big Tables
B. Both indicators suggest that Big Tables manages it/s cash better than Comp Systems
C. Both indicators give contradictory results
D. While Comp Systems is more liquid as per the Cash conversion cycle, Big Tables manages its cash better as indicated by a lower, hence better Defense Ratio

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 7
Ms. Mary Brown is a credit rating analyst. She had prepared a detailed report on one of her client, FlyHigh Airlines Ltd, a company operating chartered aircrafts in India. As she was heading for a meeting with her superior on the matter, coffee spilled over her set of prepared paper(s). As she was getting late for meeting, instead of preparing entire set she could recollect few numbers from her memory and reconstructed following partial financial table:

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Total Income			
EBITDA			
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Effective Tax Rate	20%	24%	25%
PBT			
PAT			
Financial Position			
Net Worth	370.00	430.00	535.67
Total Debt	743.00		
Ratios			
Growth			
Growth in Total Income (%)		25%	15%
Growth in EBITDA (%)		30%	20%
Growth in PAT (%)		20%	
Profitability			
EBITDA Margins		32%	
PAT Margins			
RONW			
Solvency			
Overall Gearing Ratio		2.2	
Interest coverage ratio	3.2		3.1
Total Debt / EBITDA		4.5	5.2

PAT margins are highest in which of the years?

A. FY12
B. FY11
C. FY10
D. Equal in FY10 and FY12

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 8
Ms. Mary Brown is a credit rating analyst. She had prepared a detailed report on one of her client, FlyHigh Airlines Ltd, a company operating chartered aircrafts in India. As she was heading for a meeting with her superior on the matter, coffee spilled over her set of prepared paper(s). As she was getting late for meeting, instead of preparing entire set she could recollect few numbers from her memory and reconstructed following partial financial table:

Period Ended	FY10	FY11	FY12
Working Results			
Total Income			
EBITDA			
Interest			
Depreciation	20.00	25.00	30.00
Effective Tax Rate	20%	24%	25%
PBT			
PAT			
Financial Position			
Net Worth	370.00	430.00	535.67
Total Debt	743.00		
Ratios			
Growth			
Growth in Total Income (%)		25%	15%
Growth in EBITDA (%)		30%	20%
Growth in PAT (%)		20%	
Profitability			
EBITDA Margins		32%	
PAT Margins			
RONW			
Solvency			
Overall Gearing Ratio		2.2	
Interest coverage ratio	3.2		3.1
Total Debt / EBITDA		4.5	5.2

Compute Interest for FY10 and FY12?

A. Insufficient Information to compute
B. FY10: INR50.53 Million; FY12:INR81.38 Million
C. FY10: INR161.71 Million; FY12: INR252.27 Million
D. FY10: INR17.47 Million; FY12:INR782.03 Million

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 9
"Following four entities operate in the Indian IT and BPO space. They all are into same segment of providing off-shore analytical services. They all operate on the labour cost-arbitrage in India and the countries of their clients. Following information pertains for the year ended March 31, 2013.

Particular	Beautiful	Handsome	Glowing	Glamorous
Number of Employees	300	450	700	1200
Major clients based out of	UK	USA	USA	UAE
Billing currency	GBP	INR	USD	USD

Particular	Beautiful	Handsome	Glowing	Glamorous
Revenue	36	72	116	188
Employee Cost	16	22	44	88
Other Delivery Cost	2	3	4	6
Administrative and Selling Cost	2	3	3	5
Finance Cost	1	2	1	4
Depreciation	2	6	6	9
Taxes	2	8	9	12

Particular	Beautiful	Handsome	Glowing	Glamorous
Assets				
Fixed Assets	10	24	24	37
Short Term Investments	3	7	6	8
Debtors	6	18	22	48
Total	19	49	52	93
Liabilities				
Equity Share Capital	2	8	12	10
Reserves and Surplus	5	12	24	43
Term Loans	8	16	6	24
Working Capital Borrowings	4	11	9	12
Creditors	0	2	1	4
Total	19	49	52	93

The year FY13, was typically a good year for Indian IT companies. For FY14, the economic analysts have given following predictions about the IT Industry:

A) It is expected that INR will appreciate sharply against other USD.
B) Given high inflation and attrition in IT Industry in India, the wages of IT sector employees will increase more sharply than Inflation and general wage rise in country.
C) US Congress will be passing a bill which restricts the outsourcing to third world countries like India. While analyzing the four entities, you come across following findings related to Glowing:

Glowing is promoted by Mr.M R Bhutta, who has earlier promoted two other business ventures, He started with ABC Entertainment Ltd in 1996 and was promoter and MD of the company. ABC was a listed entity and its share price had sharp movements at the time of stock market scam in late 1990s. In 1999, Mr.Bhutta sold his entire stake and resigned from the post of MD. The stock price declined by about 90% in coming days and has never recovered. Later on in 2003, Mr.Bhutta again promoted a new business, Klear Publications Ltd (KCL) an in the business of magazine publication. The entity had come out with a successful IPO and raised money from public. Thereafter it ran into troubles and reported losses. In 2009, Mr.Bhutta went on to exit this business as well by selling stake to other promoter(s). There have been reports in both instances with allegations that promoters have siphoned off money from listed entities to other group entities, however, nothing has been proved in any court."

Which of the following risks do not exist for Indian IT industry?

A. Raw material price risk, Exchange rate Risk

B. Interest rate risk, Skilled Manpower Risk
C. Exchange Rate Risk, Interest rate risk
D. Domestic and international regulatory risk, technological risk

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 10
"Following four entities operate in the Indian IT and BPO space. They all are into same segment of providing off-shore analytical services. They all operate on the labour cost-arbitrage in India and the countries of their clients. Following information pertains for the year ended March 31, 2013.

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Finance Cost	1	2	1	4
Depreciation	2	6	6	9
Taxes	2	8	9	12

Particular	Beautiful	Handsome	Glowing	Glamorous
Assets				
Fixed Assets	10	24	24	37
Short Term Investments	3	7	6	8
Debtors	6	18	22	48
Total	19	49	52	93
Liabilities				
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Which entity is best in terms of overall gearing ratio and net gearing ratio respectively:

A. Glowing and Beautiful

B. Handsome and Handsome
C. Glamorous and Glowing
D. Glamorous and Glamorous

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 11
“Following four entities operate in the Indian IT and BPO space. They all are into same segment of providing off-shore analytical services. They all operate on the labour cost-arbitrage in India and the countries of their clients. Following information pertains for the year ended March 31, 2013.

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Billing currency	GBP	INR	USD	USD

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Employee Cost	16	22	44	88
Other Delivery Cost	2	3	4	6
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What will be impact of on the predictions A and B of the economic analysts, on companies:

A. Handsome: No Impact on sales; Margins may squeeze; Glowing: INR Sales may decline; margins may squeeze.

B. Handsome: INRSales may increase; margins may squeeze; Glowing: INRSales will increase; margins may squeeze.
C. Handsome: INR Sales may decline; margins may squeeze; Glowing: INR Sales may decline; margins may squeeze.
D. Handsome: No Impact on sales; Margins may squeeze; Glowing: No Impact on sales; Margins may squeeze.

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 12
"Following four entities operate in the Indian IT and BPO space. They all are into same segment of providing off-shore analytical services. They all operate on the labour cost-arbitrage in India and the countries of their clients. Following information pertains for the year ended March 31, 2013.

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Number of Employees	300	450	700	1200
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Billing currency	GBP	INR	USD	USD

Particular	Beautiful	Handsome	Glowing	Glamorous
Revenue	36	72	116	188
Employee Cost	16	22	44	88
Other Delivery Cost	2	3	4	6
Administrative and Selling Cost	2	3	3	5
Finance Cost	1	2	1	4
Depreciation	2	6	6	9
Taxes	2	8	9	12

Particular	Beautiful	Handsome	Glowing	Glamorous
Assets				
Fixed Assets	10	24	24	37
Short Term Investments	3	7	6	8
Debtors	6	18	22	48
Total	19	49	52	93
Liabilities				
Equity Share Capital	2	8	12	10
Reserves and Surplus	5	12	24	43
Term Loans	8	16	6	24
Working Capital Borrowings	4	11	9	12
Creditors	0	2	1	4
Total	19	49	52	93

The year FY13, was typically a good year for Indian IT companies. For FY14, the economic analysts have given following predictions about the IT Industry:

A) It is expected that INR will appreciate sharply against other USD.
B) Given high inflation and attrition in IT Industry in India, the wages of IT sector employees will increase more sharply than Inflation and general wage rise in country.
C) US Congress will be passing a bill which restricts the outsourcing to third world countries like India. While analyzing the four entities, you come across following findings related to Glowing:

Glowing is promoted by Mr.M R Bhutta, who has earlier promoted two other business ventures, He started with ABC Entertainment Ltd in 1996 and was promoter and MD of the company. ABC was a listed entity and its share price had sharp movements at the time of stock market scam in late 1990s. In 1999, Mr. Bhutta sold his entire stake and resigned from the post of MD. The stock price declined by about 90% in coming days and has never recovered. Later on in 2003, Mr. Bhutta again promoted a new business, Klear Publications Ltd (KCL) an in the business of magazine publication. The entity had come out with a successful IPO and raised money from public. Thereafter it ran into troubles and reported losses. In 2009, Mr. Bhutta went on to exit this business as well by selling stake to other promoter(s). There have been reports in both instances with allegations that promoters have siphoned off money from listed entities to other group entities, however, nothing has been proved in any court."

Based on your findings in the case of Glowing, how will you handle the same as a credit rating analyst:

A. Be more cautious and skeptical on any information received from Glowing and give negative marks in management risk and use it as an overriding factor to lower the credit ratings. B. Any of the three.

C. Deny taking up assignment for Glowing.

D. One needs to check only the corporate governance aspect of the Glowing and the past same should not have any bearing on Glowing.

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:

QUESTION 13
Satish Dhawan, a veteran fixed income trader is conducting interviews for the post of a junior fixed income trader. He interviewed four candidates Adam, Balkrishnan, Catherine and Deepak and following are the answers to his questions. **Question 1:** Tell something about Option Adjusted Spread

Adam: OAS is applicable only to bond which do not have any options attached to it. It is for the plain bonds.

Balkishna: In bonds with embedded options, AS reflects not only the credit risk but also reflects prepayment risk over and above the benchmark.

Catherine: Sincespreads are calculated to know the level of credit risk in the bound, OAS is difference between in the Z spread and price of a call option for a callable bond.

Deepark: For callable bond OAS will be lower than Z Spread.

Question 2: This is a spread that must be added to the benchmark zero rate curve in a parallel shift so that the sum of the risky bond's discounted cash flows equals its current market price. Which Spread I am talking about?

Adam: Z Spread

Balkrishna: Nominal Spread
Catherine: Option Adjusted Spread
Deepark: Asset Swap Spread

Question 3: What do you know about Interpolated spread and yield spread?

Adam: Yield spread is the difference between the YTM of a risky bond and the YTM of an on-the-run treasury benchmark bond whose maturity is closest, but not identical to that of risky bond. Interpolated spread is the spread between the YTM of risky bond and the YTM of same maturity treasury benchmark, which is interpolated from the two nearest on-the-run treasury securities.

Balkrishna: Interpolated spread is preferred to yield spread because the latter has the maturity mismatch, which leads to error if the yield curve is not flat and the benchmark security changes over time, leading to inconsistency.

Catherine: Interpolated spread takes account the shape of the benchmark yield curve and therefore better than yield spread.

Deepak: Both Interpolated Spread and Yield Spread rely on YTM which suffers from drawbacks and inconsistencies such as the assumption of flat yield curve and reinvestment at YTM itself.

Then Satish gave following information related to the benchmark YTMs:

Maturity(yrs)	1	2	3	4	5
YTM	8.22	8.52	8.88	8.98	9.02

There is a 10.25% risky bond with a maturity of 4.75 year(s). Its current price is INR105.31, which corresponds to YTM of 9.22%. Compute Interpolated Spread from the information provided in the vignette:

A. 0.20%
B. 0.21%
C. 0.24%
D. 0.22%

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 14

Satish Dhawan, a veteran fixed income trader is conducting interviews for the post of a junior fixed income trader. He interviewed four candidates Adam, Balkrishnan, Catherine and Deepak and following are the answers to his questions. **Question 1:** Tell something about Option Adjusted Spread

Adam: OAS is applicable only to bond which do not have any options attached to it. It is for the plain bonds.

Balkishna: In bonds with embedded options, AS reflects not only the credit risk but also reflects prepayment risk over and above the benchmark.

Catherine: Sincespreads are calculated to know the level of credit risk in the bound, OAS is difference between in the Z spread and price of a call option for a callable bond.

Deepark: For callable bond OAS will be lower than Z Spread.

Question 2: This is a spread that must be added to the benchmark zero rate curve in a parallel shift so that the sum of the risky bond's discounted cash flows equals its current market price. Which Spread I am talking about?

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Catherine: Option Adjusted Spread
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Question 3: What do you know about Interpolated spread and yield spread?

Adam: Yield spread is the difference between the YTM of a risky bond and the YTM of an on-the-run treasury benchmark bond whose maturity is closest, but not identical to that of risky bond. Interpolated spread is the spread between the YTM of risky bond and the YTM of same maturity treasury benchmark, which is interpolated from the two nearest on-the-run treasury securities.

Balkrishna: Interpolated spread is preferred to yield spread because the latter has the maturity mismatch, which leads to error if the yield curve is not flat and the benchmark security changes over time, leading to inconsistency.

Catherine: Interpolated spread takes account the shape of the benchmark yield curve and therefore better than yield spread.

Deepak: Both Interpolated Spread and Yield Spread rely on YTM which suffers from drawbacks and inconsistencies such as the assumption of flat yield curve and reinvestment at YTM itself.

Then Satish gave following information related to the benchmark YTMs:

Maturity(yrs)	1	2	3	4	5
YTM	8.22	8.52	8.88	8.98	9.02

An investor decides to invest in the bond futures and has an outlook that the term structure curve would steepen. What should be his trading strategy?

A. Sell futures on short-maturity underlying, Buy futures on long-maturity underlying
B. Buy futures on short-maturity underlying, Buy futures on long-maturity underlying and Sell futures on middle-maturity underlying
C. Buy futures on short-maturity underlying, Sell futures on long-maturity underlying.
D. Sell futures on short-maturity underlying, Sell futures on long-maturity underlying and Buy futures on middle-maturity underlying.

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 15
The following information pertains to bonds:

Bond	Initial Maturity	Spread from G-Sec (bps)		
		January 2013	April 2013	July 2013
Bond A	10 Years	94	97	89
Bond B	10 Years	102	103	93
Bond C	10 Years	370	530	560
Bond D	10 Years	115	130	110
Bond E	10 Years	10	15	7

Further following information is available about a particular bond 'Bond F'

There is a 10.25% risky bond with a maturity of 2.25% year(s) its current price is INR105.31, which corresponds to YTM of 9.22%. The following are the benchmark YTMs.

Maturity(yrs)	1	2	3	4	5
YTM	8.22	8.52	8.88	8.98	9.02

Compute interpolated spread for Bond F based on the information provided in the vignette:

A. 1.64%
B. 0.43%
C. 0.61%
D. 1.46%

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 16
The following information pertains to bonds:

Bond	Initial Maturity	Spread from G-Sec (bps)		
		January 2013	April 2013	July 2013
Bond A	10 Years	94	97	89
Bond B	10 Years	102	103	93
Bond C	10 Years	370	530	560
Bond D	10 Years	115	130	110
Bond E	10 Years	10	15	7

Further following information is available about a particular bond 'Bond F'

There is a 10.25% risky bond with a maturity of 2.25% year(s) its current price is INR105.31, which corresponds to YTM of 9.22%. The following are the benchmark YTMs.

Maturity(yrs)	1	2	3	4	5
YTM	8.22	8.52	8.88	8.98	9.02

Following are the relevance of Industry Analysis:
Statement 1: Evaluating Industry risk is the first and foremost step for top down approach of analysis.

Statement 2: Industry Analysis is relevant for analyzing the industry life cycle, which is highly important from the perspective of an investor or lender.

State which is/are correct?

A. Both are incorrect
B. Both are correct
C. Only Statement 2 is correct
D. Only Statement 1 is correct

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 17

The following information pertains to bonds:

Bond	Initial Maturity	Spread from G-Sec (bps)		
		January 2013	April 2013	July 2013
Bond A	10 Years	94	97	89
Bond B	10 Years	102	103	93
Bond C	10 Years	370	530	560
Bond D	10 Years	115	130	110
Bond E	10 Years	10	15	7

Further following information is available about a particular bond 'Bond F'

There is a 10.25% risky bond with a maturity of 2.25% year(s) its current price is INR105.31, which corresponds to YTM of 9.22%. The following are the benchmark YTMs.

Maturity(yrs)	1	2	3	4	5
YTM	8.22	8.52	8.88	8.98	9.02

Assuming the G-Sec has not changed from the time January 2013 to April 2013, what can you predict about the changes bond price and change in issues borrowing rates:

A. Decrease and Increase
B. Increase and Increase
C. Decrease and Decrease
D. Increase and Decrease

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:

QUESTION 18
Two economies HardLand and SincereLand have provided following information with respect to their economies in USD Billion:

Particulars (USD bn)	Hard Land	Sincere Land
Current Account Reciepts	400	700
Current Account Payments	480	810
GDP	1800	2200
External Debt	650	850
Forex Reserve	200	240
Principal amount of debt Repyable in one year	120	140
Interest Payable	60	75

Based on the above information which entity is better in terms of current account deficit %?

A. Sincereland by 583 bps
B. Hardland by 56 bps
C. Sincereland by 56 bps
D. Hardland by 583 bps

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 19
The longer the term to maturity of bond:

A. term to maturity and price of a bond are not related
B. The lesser is the risk associated with price of a bond
C. The higher is the return from the bond

D. The more risk in the price of a bond

Correct Answer: D
Section: (none)
Explanation
Explanation/Reference:
Reference: https://www.investopedia.com/university/advancedbond/advancedbond5.asp

QUESTION 20
In Steepening short term rates ______relative to long term rate

A. falls
B. rises
C. is independent of each other
D. remains constant

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:
Reference: https://www.analystforum.com/forums/cfa-forums/cfa-level-ii-forum/91348766

QUESTION 21
If you yield curve is humped and the medium rates drop, what will happen to the yield curve?

A. It will move from negative to positive
B. It will shift up in a uniform fashion
C. It will become steeper
D. It will flatten

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 22
Which of the following statement is false?

A. DEF Ltd. has received a speculative grade rating as its outstanding rating is B+

B. Non-Convertible debenture of PQR Ltd. has a speculative rating since its outstanding rating is C
C. ABC Ltd. short term is BBB- for its commercial paper
D. XYZ has an investment grade rating as his outstanding rating is A1

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 23
Which of the following is not one of the C in the 5 C Model?

A. Capacity
B. Capital
C. Covenants
D. Conditions

Correct Answer: C

Section: (none)

Explanation

Explanation/Reference:
Reference: https://www.investopedia.com/terms/f/five-c-credit.asp

QUESTION 24
In an industry there are only 20 firms and each of them has equal share. Compute Herfindahl Hirschman Index and state the level of concentration in the industry.

A. HHI = 500; High Concentration
B. HHI = 8000; low Concentration
C. HHI = 8000; High Concentration
D. HHI = 500; Low Concentration

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:
Reference: https://www.investopedia.com/terms/h/hhi.asp

QUESTION 25
Z spreads in Callable bonds include:

A. Does not include premium for credit risk and call option price for prepayment risk.
B. Premium for credit risk and call option price for prepayment risk in included.
C. Premium for credit risk is only included.
D. Premium for call option price for prepayment risk os only included.

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:
Reference: https://books.google.com.pk/books?id=WTvNAgAAQBAJ&pg=PA224&lpg=PA224&dq=credit+Z+spreads+in+Callable+bonds+include+Premium+for+credit+risk+and+call+option+price+for+prepayment+risk+in+included&source=bl&ots=cdWVJiWQSC&sig=d9Y2vg5dyIZIrlBT7tmKRihUg2M&hl=en&sa=X&ved=2ahUKEwiUqN2I_93eAhXMA8AKHSb1B7gQ6AEwCXoECAcQAQ#v=onepage&q=credit%20Z%20spreads%20in%20Callable%20bonds%20include%20Premium%20for%20credit%20risk%20and%20call%20option%20price%20for%20prepayment%20risk%20in%20included&f=false

QUESTION 26
Which of the following is a factor considered while evaluating resources profile for rating of bank?

A. Size and growth of deposits
B. All of the three
C. Deposit composition & stickiness
D. Geographic distribution of deposits

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 27
Mr. A shares details of two bonds as follows:

Particulars	Bond X	Bond Y
Yeild to Maturity	7%	9%
Maturity	2.25 Years	4.75 years
Number of coupons in the year	1	1

Term Structure:

1 Year	6.8%
2 Year	7.2%
3 Year	7.8%
4 Year	8.6%
5 Year	9.2%
6 Year	9.9%

Determine the interpolated spread for Bond X and Bond Y?

A. Bond X: 80 bps
   Bond Y: Negative
B. Bond X: 35 bps
   Bond Y: 5 bps
C. Bond X: 65 bpsBond Y: Nil
D. Bond X: 20 bps
   Bond Y: 20 bps

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 28
A coupon bond is trading at 110% of the USD 1000 par value. If the last interest payment was made one month ago and the coupon rate is 12%, the accrued interest on this bond is_______

A. 110
B. 100
C. 120
D. 10

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:
Reference: http://www.faculty.umassd.edu/xtras/catls/resources/binarydoc/2288.pdf

QUESTION 29
Basket Default swaps could be

A. reference sectors could be from the same economy
B. reference sectors could be the entire global space
C. reference securities are from the same sector

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 30
Attributes of healthy cultural values exclude:
A. Experienced management.
B. Diversified sources of revenue.
C. Brand.
D. Healthy relationship with employees

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 31
An increase in the salaries of the bank employees due to new bank employee pay commission implemented by the Central Government will lead to deterioration of which of the following ratios:

A: Cost to Income Ratio
B: Net Interest Margin
C: Core Spread

A. Only A
B. A B and C
C. Only B
D. Only C

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 32
Project 1: Company X has a sugar mill at Philadelphia and is replicating same at Toronto.
Project 2: Company Y has a sugar mill at Philadelphia and is increasing capacity from 100000 MT to 140000 MT per annum.

What type of projects are Project 1 and Project 2?

A. Project 1: Diversification; Project 2: Forward Integration
B. Project 1: Expansion; Project 2: Forward Integration
C. Project 1: Diversification; Project 2: Expansion
D. Project 1: Expansion; Project 2: Expansion

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 33

Which of the following may lead to the deterioration in credit profile of a bank?

Statement 1. Bank's Capital adequacy falling below regulatory requirement.
Statement 2. Rise in Slippage ratio

A. None of the statement is correct
B. Both statement 1 and 2 are correct
C. Statement 1 is correct
D. Statement 2 is correct

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:
Reference: https://economictimes.indiatimes.com/industry/banking/finance/pnbs-capital-adequacy-falls-below-regulatory-requirement-due-to-nirav-scam/articleshow/64573303.cms

QUESTION 34
During FY13, Small Bazar, a leading retail company has sold three of its prime properties for a sum of USD 24 Million. The same had a carrying value of USD 30 Million.

Analyst had considered the same as operating income and considered it to be part of operating expenses. However, she realized her mistake and recorded the loss as non-operating loss. Which of the following ratio will not change despite the correction?

A) EBITDA Margins
B) Interest Coverage
C) PAT Margins
D) Gross Profit Margin

A. B, C & D
B. A, B & C
C. B, C
D. All Ratios will change

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 35
Which of the following statements concerning having a CEO serve as chairman of the board is most accurate? Having a CEO also serve as chairman is considered:

A. poor corporate governance practice as having the CEO server as chairman is an inherent conflict when determining management compensation.
B. good corporate governance practice as the CEO is the best person to provide the board with information about the company's strategy and operations.
C. cannot be determined
D. poor corporate governance practice as having the CEO and chairman serve as separate positions ensures a properly-functioning board.

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:

QUESTION 36
The most important metric for a bank is the Net Interest Income (NII) which is the difference between____income and____expense.

A. Interest; Total
B. Interest; Fee
C. Interest; Interest
D. Total; Total

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:
Reference: https://economictimes.indiatimes.com/definition/net-interest-income-nii

QUESTION 37
Based on the common size statement analysis which of the following statement regarding employee cost is correct?

Particulars (USD Million)	YE FY14	YE FY15
SALES	2800	3800
Employee Cost	1200	1400
Power and Establishment Cost	160	180
Depreciation	26	31
Interest	25	37
Taxes	200	240

A. The employee cost is expected to contribute 8% to decrease in PAT in FY15
B. The employee cost is expected to contribute 7% to decrease in PAT in FY15
C. The employee cost is expected to contribute 6% to decrease in PAT in FY15
D. The employee cost is expected to contribute 5% to decrease in PAT in FY15

Correct Answer: C
Section: (none)
Explanation

Explanation/Reference:

QUESTION 38
Butterfly strategy is a combination of

A. Ladder and Barbell on the same market sides
B. Barbell and Bullet on the opposite market sides
C. Barbell and Bullet on the same market sides
D. Ladder and barbell on the opposite market sides

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:
Reference:
https://books.google.com.pk/books?id=WTvNAgAAQBAJ&pg=PA213&lpg=PA213&dq=Butterfly+strategy+is+a+combination+of+Barbell+and+Bullet+on+the+opposite+market+sides&source=bl&ots=cdWVJkVMRG&sig=XIB-

7YqySq5YDEUmEWusH5JCsjY&hl=en&sa=X&ved=2ahUKEwj3_pCrxN7eAhVkK8AKHYuDCwUQ6AEwBnoECAUQAQ#v=onepage&q=Butterfly%20strategy%20is
%20a%20combination%20of%20Barbell%20and%20Bullet%20on%20the%20opposite%20market%20sides&f=false

QUESTION 39
Based on the Moody's KMV model which of the following is not correct?

A: Growth variables are important for default analysis. rapid growth will lead to lower probability of default and rapid decline will lead to higher probability of default.
B: Activity ratios are relevant for default analysis. A large stock of inventories relative to sales will lead to a higher probability of default.

A. Only Statement A is correct
B. Both the statements are correct
C. None of the statements is correct
D. Only Statement B is correct

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:
Reference: https://books.google.com.pk/books?id=g8XgCwAAQBAJ&pg=PA67&lpg=PA67&dq=Activity+ratios+are+relevant+for+default+analysis.+A+large+stock+of+inventories+relative+to+sales+will+lead+to+a+higher+probability+of+default&source=bl&ots=Q-6qbboNbl&sig=iKGUJsn0wKNSv-F7pZ5B_GElw5E&hl=en&sa=X&ved=2ahUKEwjsruKZwd7eAhUqB8AKHQFGAtAQ6AEwC3oECAsQAQ#v=onepage&q=Activity%20ratios%20are%20relevant%20for%20default%20analysis.%20A%20large%20stock%20of%20inventories%20relative%20to%20sales%20will%20lead%20to%20a%20higher%20probability%20of%20default&f=false

QUESTION 40
Bank A has an imaginary portfolio of USD 1000 Million distributed towards following four entities:

Company W	USD 200 Million,	Rated AA
Company X	USD 300 Million,	Rated A
Company Y	USD 300 Million,	Rated AA
Company Z	USD 200 Million,	Rated BBB

Bank A is stipulated to maintain a capital adequacy ratio of 11% on its risk weighted assets. It is being stipulated that the ratings for all the four entities is expected to be downgraded by 1 notch each. Estimate the amount of new capital required for Bank A?

A. USD 93.5 Million
B. USD 38.5 Million
C. USD 55 Million
D. USD 850 Million

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:

QUESTION 41
Stand by letter of credits are typically taken as credit enhancement for___________

A. Commercial Paper
B. Long term Bond issues
C. Long term debenture issues
D. Bank debt

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:
Reference: https://www.investopedia.com/terms/s/standbyletterofcredit.asp

QUESTION 42
Which of the following is NOT a conceptual definition of credit risk on which credit models are based?

A. Default Mode Paradigm
B. Value-at-Risk paradigm
C. Mark-to-Market Paradigm

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:
Reference: http://www.bulentsenver.com/yeditepe/pdf/Credit%20Risk%20Modelling%20BIS49.pdf (page 9)

QUESTION 43

Which of the following is false in case of credit enhancements?

A. It reduces the default risk of the borrowing entity for the lender, thereby deteriorating the overall credit worthiness of the borrower
B. Credit enhancement could be implicit or explicit
C. Credit enhancement is a mechanism whereby external cash flows is extended by an entity which has a stringer credit profile, so that it benefits the fund raising entity

Correct Answer: A
Section: (none)
Explanation

Explanation/Reference:

QUESTION 44
Step up upon feature will lead to

A. no change as step is not linked to issuers rating
B. positive basis because the bond holder is compensated
C. negative basis given that the bondholder is not compensated
D. Will lead to a change only if there is a linkage to the issuer's rating

Correct Answer: B
Section: (none)
Explanation

Explanation/Reference:
Reference: https://books.google.com.pk/books?id=WTvNAgAAQBAJ&pg=PA242&lpg=PA242&dq=credit+research+Step+up+upon+positive+basis+because+the+bond+holder+is+compensated&source=bl&ots=cdWVJkYMRF&sig=t3wUd2qxS8OTjzUl8EfSzkmf7Eg&hl=en&sa=X&ved=2ahUKEwi8w4rBz97eAhUPgVwKHRAfAMgQ6AEwAHoE CAkQAQ#v=onepage&q=credit%20research%20Step%20up%20upon%20positive%20basis%20because%20the%20bond%20holder%20is%20compensated&f=false

QUESTION 45
__________Strategy consists of buying a bond with maturity longer than the investment horizon (for investor) or buying a long-maturity bond with short-term funding through repo (for speculator).

A. Barbell, Ladder and Butterfly
B. Yield Spread Anticipation
C. Rate Anticipation with Maturity Mismatch
D. Riding the yield curve

Correct Answer: D
Section: (none)
Explanation

Explanation/Reference:
Reference: https://books.google.com.pk/books?id=WTvNAgAAQBAJ&pg=PA276&lpg=PA276&dq=Strategy+consists+of+buying+a+bond+with+maturity+longer
+than+the+investment+horizon+(for+investor)+or+buying+a+long-maturity+bond+with+short-term+funding+through
+repo&source=bl&ots=cdWVJkURVE&sig=zdiI1Gm3sNJnB6zDJ82OkMAAtk&hl=en&sa=X&ved=2ahUKEwiYoNDOwt7eAhUFDsAKHWG8BvcQ6AEwAHoECAkQ
AQ#v=onepage&q=Strategy%20consists%20of%20buying%20a%
20bond%20with%20maturity%20longer%20than%20the%20investment%20horizon%20(for%20investor)%20or%20buying%20a%20long-
maturity%20bond%20with %20short-term%20funding%20through%20repo&f=false