SQ 9-9. Define and explain the use of the following: (a) long hedge; (b) short hedge; and (c) cross hedge.

SQ 9-10. Which type of hedge named above works best in an environment of rising interest rates? Of falling interest rates? Illustrate both cases using a payoff diagram.

SQ 9-11. What is the basic purpose of futures trading in securities? Where is most futures trading carried out?

P 7-1. According to the Fisher effect, if the real interest rate is 3 percent and the nominal interest rate is 8 percent, what rate of inflation is the financial marketplace expecting? Explain the reasoning behind your answer. If the nominal rate rises to 11 percent and follows the Fisher effect, what would you conclude about the expected inflation rate? The real rate?

P 7-3. An investor buys a U.S. Treasury bond whose current yield to maturity is 10 percent. The investor is subject to a 33 percent federal income tax rate on any new income received. His real after-tax return from this bond is 2 percent. What is the expected inflation rate in the financial marketplace?

SQ 11-1. Define the term *federal funds*. Why are federal funds so important to the functioning of the money market?

SQ 11-25. Why is commercial paper attractive to such money market investors as banks, insurance companies, money market funds, and industrial companies?

P 11-1. A money-centre bank is trying to decide which source of funding to rely upon to cover loans being made today. It needs to borrow $10 million in either the federal funds market or in the negotiable CD market. Funds are needed for at least a week, but the bank’s money desk manager is most concerned about the 24 hours. Federal funds are currently trading at 4.80 percent; rates on new negotiable CDs posted by leading banks have reached 4.70 percent. FDIC insurance fees are currently 27 cents per $100.

Calculate the cost to the bank for each of these funds sources. If you were a banker, which source would you prefer to use?