Department of Banking and Finance
FINA 522-622
Project Finance and Risk Management
Final Exam Questions

1. What is limited recourse project financing? Give two examples of such financing.
2. Why do we need project financing?
3. Why do we have to do prerequisites for project financing?
4. What do you mean managing the financial risk? Explain.
5. Please explain about the post-completion risks.
6. What are the main characteristics of project finance?
7. What is the purpose of an interest rate swap? How does it work? Explain with a numerical example.
8. What's the difference between an interest-rate swap and a currency swap? How do their purposes differ?
9. How can a project benefit from trading in currency swaps?
10. A commercial bank has $200 million of floating rate loans yielding the T-bill rate (5%) plus 2 percent. These loans are financed by $200 million of fixed-rate deposits costing 9 percent. A savings bank has $200 million of mortgage with a fixed rate of 13 percent. They are financed by $200 million in CDs with a variable rate of T-bill rate plus 3 percent. Show that this swap would be acceptable to both parties.
11. Bank 1 can issue five-year CDs at an annual rate of 11 percent fixed or at a variable rate of LIBOR (7%) plus 2 percent. Bank 2 can issue five-year CDs at an annual rate of 13 percent fixed or at a variable rate of LIBOR plus 3 percent. Is a mutually beneficial swap possible between the two banks?
12. Consider the following currency swap of coupon interest on the following assets:
    5 percent (annual coupon) fixed-rate U.S. $ 1 million bond
    5 percent (annual coupon) fixed-rate bond denominated in deutsche marks (DM)
    Spot exchange rates: DM 1.5/$
    a. What are the cash flows if spot exchange rates fall to DM 0.50/$? What are the net cash flows on the swap?
    b. What are the cash flows if spot exchange rates rise to DM 2.25/$? What are the net cash flows on the swap?

13. A savings and loan whose credit ratings has just slipped and half of whose assets are long-term mortgages offers to swap interest payments with a money center bank in a $100 million deal. The bank can borrow short term at LIBOR (8 percent) and long term at 10 percent. The company must pay LIBOR plus 1.5 percent on short–term debt and 10.75 percent on long-term debt. Show, how these parties could put together a swap deal that benefits both of them about equally.
14. A bank plans to borrow $55 million in the money market for 3 years at a current interest rate of 8.5 percent with an interest-rate cap on this borrowing of 10 percent. Suppose money market interest rates climb to 11.5 percent as soon as the borrowing occurs. How much total interest will the bank owe?
15. What are the expectations of forward and future contracts?
16. What are the other risks? Explain each of them.
17. What are the contractual agreements? Explain two of them.
18. What is a testing contract?
19. What are the advantages and disadvantages of project financing?
20. Why do projects need contracts?
21. What is a clawback agreement?
22. What are three different ownership structures that you might have as the legal entity of a project that is being financed on a project financing basis? Indicate how each of the ones you choose affect: A. the legal liability of their owners. B. the ownership of Assets and Liabilities. C. the tax treatment of the project.
23. What are the fundamental set of contracts needed for a typical project financed investment? What are the issues that need to be considered when designing these contracts?
24. Outline three reasons why it could be attractive to use project financing to undertake an investment. Explain each of the reasons you suggest in one or two sentences.
25. Outline three types of <u>post- completion </u>risks that a project might face. Indicate how these risks might be reduced or managed. Explain how the risk management techniques you suggest would reduce or manage the risk.
26. Explain how the following contracts operate. How do they reduce the risks of a project? How are they different in their impact on the reduction of the risks of a project?

a. Take-if- Offered Contract.
b. Take-or-Pay Contract.
c. Cost-of- service Contract.

27. Suppose you are a commercial banker who is being asked to finance a private electric generation plant in North Cyprus on a project finance basis. What types of contracts or agreements do you think would be necessary for the project to have in place before you would be willing to make a long term loan to the project? (You should outline at least 3 types). Explain briefly the reason for having each type of contract or agreement.

28. What are three different ownership structures that you might have as the legal entity of a project that is being financed on a project financing basis? Indicate how each of the ones you choose affect: A. the legal liability of their owners. B. the ownership of Assets and Liabilities. C. the tax treatment of the project.

29. Name three typical sources of finance that could be used in the future to finance projects in Cyprus under project finance arrangements? What are the advantages and disadvantages of each of the sources of finance you suggest?

30. What do we mean by Security Arrangements? Name four types of such arrangements and explain how they are designed and how they work to reduce the risk facing the financial institutions lending to the project?