Subject SP6

2021/22 CMP upgrade

CMP Upgrade

This CMP Upgrade lists all significant changes to the Core Reading and the ActEd material since last year so that you can manually amend your **2020 SP6 study material** to make it suitable for study for the **2022 SP6 exams**.

You can buy a full replacement set of up-to-date **Subject SP6 Course Notes** at a significantly reduced price if you have previously bought the full price **Subject SP6 Course Notes**. Please see our **2022 *Student Brochure*** for more details.

0 Changes to the Syllabus objectives and Core Reading

0.1 Syllabus objectives

The only change to the Syllabus objectives has been to correct the reference in objective 2.3 which now reads:

2.3 Explain how to use the futures contracts in 2.1 for hedging.

The only other changes that have been made to the Syllabus are to correct typographical errors and improve the style.

0.2 Core Reading

The Introduction to the Core Reading has been updated to include the following:

The IFoA has produced a notation sheet suggesting possible standard keyboard notation that candidates could use instead of mathematical notation when typing solutions in Word in the IFoA examinations.

The United Kingdom left the European Union on 1 January 2021 without an EU-wide arrangement for the operation and regulation of financial services. Discussions will continue during 2021 and this version of the Core Reading does not attempt to address these areas.

At the time of writing (Winter 2021), the effect of the coronavirus pandemic on both the global economy and financial markets will not be known for some time. This version of the Core Reading does not attempt to address these areas.

Unit 3 – reference at the start of the Unit to syllabus objective 2.3 includes the amended reference in the syllabus objective above.

Unit 18 – section 1.3 has been added on the use of derivatives by commercial banks, and a little more content has been added to section 1.5.

The only other changes that have been made to the Core Reading are to correct typographical errors and improve the style.

The SP6 Core Reading is given in its entirety at the end of the ActEd Course notes.

1 Changes to the ActEd Course Notes

Chapter 11

Page 4

A new section of text on Overnight index swap (OIS) rates has been added after the text about LIBOR rates but before the text on repo rates. It reads:

Overnight index swap (OIS) rates

The OIS rate is the fixed rate in an OIS swap. An OIS is a swap where a fixed rate for a period (*eg*, 1 month or 3 months) is exchanged for the geometric average of the overnight rates during the period.

OIS discounting

This is covered in Section 9.3 of Hull and was examined in Subject SP6, April 2021, Question 2. An interest rate swap can be valued by considering the present value of the differences between the fixed rate and the floating rate. The OIS rates can be used as the discount factors when these present values are calculated, thus resulting in a slightly different fixed rate on the interest rate swap. We recommend that you look at both Section 9.3 of Hull and Subject SP6, April 2021, Question 2 to see examples.

Chapter 17

Page 8

A new section, Section 1.3, on the use of derivatives by commercial banks has been added to reflect the new section of Core Reading in Unit 18, Section 1.3. It reads:

1.3 Commercial banks

Commercial banks use derivatives either to reduce the risks involved in the bank's operations or to hedge the risks inherent in products it sells to its customers. Most banks make their profits by simply charging more interest on their loans than they pay on their borrowing. The more customers the bank has, the more profits it can make. To attract more customers, the bank may offer products with special features, such as guarantees. So, the bank will not usually want to take the risk associated with these guarantees, instead it will want to use derivatives to immediately hedge the risk.

Typical derivative products used by commercial banks

- **Credit derivatives - to remove or reduce the risk of default by borrowers.**
- **Interest rate swaps**
  - **to manage the bank's own interest rate risk**
  - **to help customers who wish to manage their interest rate risk**
- **Currency forwards and futures**
  - **to reduce the bank's own foreign currency exposure**
  - **to help customers with their foreign trade or balance sheet exposure**

Example in the past exam papers

- **Subject ST6 April 2017, Question 7** is about a bank trying to manage its interest rate risk, considering bott interest rate swaps and options.

2 X assignments

The X Assignments have been changed significantly to reflect the online nature of the exams. We have not detailed all of the changes in this upgrade.

If you would like the new assignments *without* marking, then retakers can purchase an updated CMP or standalone X Assignments at a significantly reduced price. Further information on retaker discounts can be found at:

www.acted.co.uk/paper_reduced_prices.html

If you wish to submit your scripts for marking but have only an old version, then you can order the current assignments free of charge if you have purchased the same assignments in the same subject in a previous year and have purchased marking for the 2022 session. We only accept the current version of assignments for marking, *ie* those published for the sessions leading to the 2022 exams.

