

Quiz 6 - Solution

1. Redington immunization conditions:

$$P(i_0) = 0 \quad P'(i_0) = 0 \quad \text{and} \quad P''(i_0) > 0$$

2. These conditions ensure that the NPV function has a local minimum at $i = i_0$. This means that a small deviation of i from i_0 may only help (not hurt) profitability.

3. A derivative is an agreement between two parties. What one party wins, the other party loses. The determination of who wins (loses) and by how much, is based on the future unknown value of some asset/commodity/index.