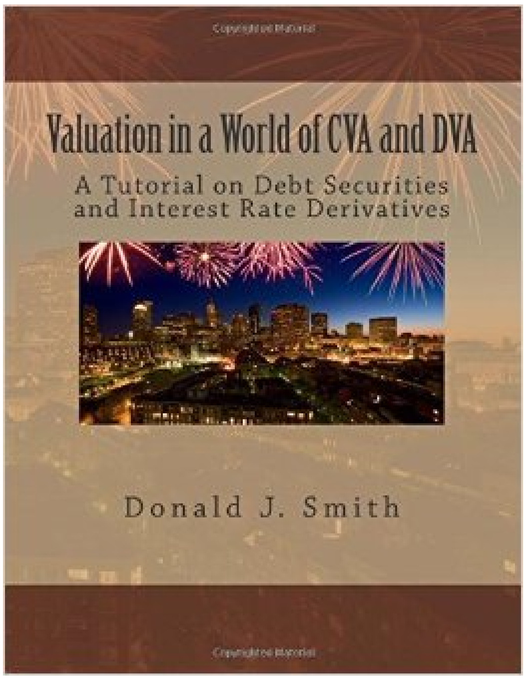
Valuation In A World Of CVA And DVA: A Tutorial On Debt Securities And Interest Rate Derivatives



Synopsis

Credit risk models invariably are mathematical, and can be dauntingly so. Nevertheless, an understanding of the impact of credit risk on the valuation of debt securities and derivatives is essential to investment analysis and risk management. The financial crisis that started in 2007 exposed the importance of counterparty credit risk; nowadays, CVA and DVAâ ”credit valuation and debit (or debt) valuation adjustments, respectivelyâ ”are part of the vocabulary of risk analysis in the â œpost-Lehmanâ • world. This tutorial introduces the key parameters that drive CVA and DVA (the expected exposure to default loss, the probability of default, and the recovery rate) and demonstrates the impact of changes in credit risk on values of various types of debt securities and interest rate derivatives in a simplified format using diagrams and tables, albeit with some mathematics.

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CVA really teach me how to build binomial tree. It is necessary to use this book to understand the inside of trading.

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