

On CDO^2 pricing using conditional moment matching.

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Abstract

We consider an semi-analytical method of approximate pricing of CDO^2 within a factor copula framework using conditional moment matching. While Monte-Carlo methodologies can be made fast and can be adapted for quick internal sensitivity calculation, the method presented here provides an even faster alternative for both. We show that the biggest challenge is actually finding an adequate proxy distribution, as for CDO^2 the boundedness of the loss is essential, as are atomic survival and full loss probabilities. Examples of the method's performance for a typical deal are provided.

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