NAME:_____

BEM 103 QUIZ 1

Present value and prices

Consider bond with 1 year maturity, a face value of 100, has a coupon of 5% (so it will pay interest only once at redemption). The annual interest rate is denoted r,

1.A Give a formula to compute the current market price of the bond given r?

X=100(1.05)/(1+r)

1.B For what values of r will the bond's price be below par (100)?

r>0.5

1.C If that bond is trading at par, what is the interest rate and what would be the value of a bond that has a coupon rate of 10% and 1 year maturity (an answer to the second decimal place is sufficient)

If the first bond is trading at par r=0.05

So X=*100(1.1)/(1.05) = 104.7*

1D. If the bonds are priced in the ways described above which one would you prefer to buy? Why?

It does not matter their returns are equal and yields are both 5%.

Π(B5%)=(-100+105/105)=0

Π(B10%)=(-104.7+110/105)=0