# Session 1
# Questions

**Question 1**
A zero coupon bond is best described as a bond that:
**a.** Pays a zero rate of return.
**b.** Can have a price that is above par.
**c.** Does not pay coupon interest every 6 months.

**Question 2**
Reinvestment risk tends to be highest for:
**a.** Zero coupon bonds
**b.** High-coupon amortizing securities
**c.** High-coupon straight bonds

**Question 3**
The following data is available

| Dealer | Bid | Ask |
|---|---|---|
| 1 | 100 1/32 | 100 5/32 |
| 2 | 100 4/32 | 100 6/32 |
| 3 | 100 2/32 | 100 5/32 |

The bid-asked spread for the bond is *closest* to:
**a.** 0.03125
**b.** 0.06250
**c.** 0.12500

**Question 4**
The interest rate sensitivity of a bond increases when the maturity is:
**a.** Long term and the coupon is low.
**b.** Short term and the coupon is low.
**c.** Long term and the coupon is high.

**Question 5**
Assuming all fixed-income securities are trading at the same yield, interest rate risk is highest for which of the following bonds?
**a.** A 30-year, 6% bond.
**b.** A 10-year, 8% bond.
**c.** A 20-year, 6% bond.

**Question 6**
Currency risk in a bond refers to the risk that:
**a.** interest rates in a foreign country will change.
**b.** The domestic inflation rate will change.
**c.** The foreign currency exchange rate will change.

**Question 7**
Considering credit quality only, which of the following is the safest investment?
**a.** AA municipal bond with call features.
**b.** A-rated municipal bond.
**c.** B-rated corporate bond.

**Question 8**
High downgrade risk in a bond refers to the probability:
**a.** A rating agency will lower the bond's credit rating.
**b.** The credit spread will decrease.
**c.** The bond will not default.

**Question 9**
Which of the following is a type of credit risk associated with bonds?
**a.** Default risk.
**b.** Call risk.
**c.** Liquidity risk.

**Question 10**
To reconstitute a bond, a dealer would buy the:
**a.** Bond and sell each coupon payment and the principal as zero coupon bonds
**b.** Individual coupons and principal zeros to put them back together and resell the whole bond.
**c.** Bond and a put on the bond while selling a call on the bond.

**Question 11**
An investor purchases a 5 year, 6% coupon bond at a yield-to-maturity of 7% for a price of 95.84. One year later the yield-to-maturity of the bond is 6.5%. The price of the bond will be:
**a.** Less than 95.84
**b.** 95.84
**c.** More than 95.84

**Question 12**
An arbitrage trader observes that the piece of a coupon-bearing treasury bond is less than the value of zero-coupon treasury securities that could be created from it. The trader could profit from this by:
**a.** Buying and selling the bond in a repurchase agreement transaction.
**b.** Buying the bond, stripping it, and selling the pieces.
**c.** Selling the bond because it is overvalued.

**Question 13**

An analyst gathers the following U.S. Treasury spot rates

| Maturity | Spot Rate |
|---|---|
| 0.5 years | 3.0% |
| 1.0 year | 3.3% |
| 1.5 years | 3.7% |
| 2.0 years | 4.0% |
| 2.5 years | 4.2% |
| 3.0 years | 4.4% |

The arbitrage-free value of a 4% coupon, 3-year Treasury note is *closest* to:

**a.** $989.64
**b.** $972.22
**c.** $877.35

**Question 14**

A bond's yield-to-maturity and current yield are equal when the bond priced at:

**a.** A discount
b. Par
**c.** A premium

**Question 15**

All other things being equal, which one of the following bonds will have the greatest volatility?

**a.** 15-year, 15% coupon bond.
**b.** 5-year, 10% coupon bond.
**c.** 15-year, 10% coupon bond.
**d.** 5-year, 15% coupon bond.