

PROBLEMS

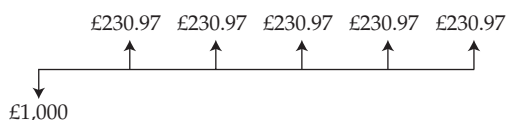
FIXED-INCOME SECURITIES: DEFINING ELEMENTS

PROBLEMS

1. A 10-year bond was issued four years ago. The bond is denominated in US dollars, offers a coupon rate of 10% with interest paid semi-annually, and is currently priced at 102% of par. The bond's:
 - A. tenor is six years.
 - B. nominal rate is 5%.
 - C. redemption value is 102% of the par value.
2. A sovereign bond has a maturity of 15 years. The bond is *best* described as a:
 - A. perpetual bond.
 - B. pure discount bond.
 - C. capital market security.
3. A company has issued a floating-rate note with a coupon rate equal to the three-month Libor + 65 basis points. Interest payments are made quarterly on 31 March, 30 June, 30 September, and 31 December. On 31 March and 30 June, the three-month Libor is 1.55% and 1.35%, respectively. The coupon rate for the interest payment made on 30 June is:
 - A. 2.00%.
 - B. 2.10%.
 - C. 2.20%.
4. The legal contract that describes the form of the bond, the obligations of the issuer, and the rights of the bondholders can be *best* described as a bond's:
 - A. covenant.
 - B. indenture.
 - C. debenture.
5. Which of the following is a type of external credit enhancement?
 - A. Covenants
 - B. A surety bond
 - C. Overcollateralization

6. An affirmative covenant is *most likely* to stipulate:
 - A. limits on the issuer's leverage ratio.
 - B. how the proceeds of the bond issue will be used.
 - C. the maximum percentage of the issuer's gross assets that can be sold.
7. Which of the following *best* describes a negative bond covenant? The issuer is:
 - A. required to pay taxes as they come due.
 - B. prohibited from investing in risky projects.
 - C. required to maintain its current lines of business.
8. A South African company issues bonds denominated in pound sterling that are sold to investors in the United Kingdom. These bonds can be *best* described as:
 - A. Eurobonds.
 - B. global bonds.
 - C. foreign bonds.
9. Relative to domestic and foreign bonds, Eurobonds are *most likely* to be:
 - A. bearer bonds.
 - B. registered bonds.
 - C. subject to greater regulation.
10. An investor in a country with an original issue discount tax provision purchases a 20-year zero-coupon bond at a deep discount to par value. The investor plans to hold the bond until the maturity date. The investor will *most likely* report:
 - A. a capital gain at maturity.
 - B. a tax deduction in the year the bond is purchased.
 - C. taxable income from the bond every year until maturity.
11. A bond that is characterized by a fixed periodic payment schedule that reduces the bond's outstanding principal amount to zero by the maturity date is *best* described as a:
 - A. bullet bond.
 - B. plain vanilla bond.
 - C. fully amortized bond.
12. If interest rates are expected to increase, the coupon payment structure *most likely* to benefit the issuer is a:
 - A. step-up coupon.
 - B. inflation-linked coupon.
 - C. cap in a floating-rate note.
13. Investors who believe that interest rates will rise *most likely* prefer to invest in:
 - A. inverse floaters.
 - B. fixed-rate bonds.
 - C. floating-rate notes.
14. A 10-year, capital-indexed bond linked to the Consumer Price Index (CPI) is issued with a coupon rate of 6% and a par value of 1,000. The bond pays interest semi-annually. During the first six months after the bond's issuance, the CPI increases by 2%. On the first coupon payment date, the bond's:
 - A. coupon rate increases to 8%.
 - B. coupon payment is equal to 40.
 - C. principal amount increases to 1,020.
15. The provision that provides bondholders the right to sell the bond back to the issuer at a predetermined price prior to the bond's maturity date is referred to as:
 - A. a put provision.
 - B. a make-whole call provision.
 - C. an original issue discount provision.

16. Which of the following provisions is a benefit to the issuer?
- A. Put provision
 - B. Call provision
 - C. Conversion provision
17. Relative to an otherwise similar option-free bond, a:
- A. puttable bond will trade at a higher price.
 - B. callable bond will trade at a higher price.
 - C. convertible bond will trade at a lower price.
18. Which type of bond *most likely* earns interest on an implied basis?
- A. Floater
 - B. Conventional bond
 - C. Pure discount bond
19. Clauses that specify the rights of the bondholders and any actions that the issuer is obligated to perform or is prohibited from performing are:
- A. covenants.
 - B. collaterals.
 - C. credit enhancements.
20. Which of the following type of debt obligation *most likely* protects bondholders when the assets serving as collateral are non-performing?
- A. Covered bonds
 - B. Collateral trust bonds
 - C. Mortgage-backed securities
21. Which of the following *best* describes a negative bond covenant? The requirement to:
- A. insure and maintain assets.
 - B. comply with all laws and regulations.
 - C. maintain a minimum interest coverage ratio.
22. Contrary to positive bond covenant, negative covenants are *most likely*:
- A. costlier.
 - B. legally enforceable.
 - C. enacted at time of issue.
23. A five-year bond has the following cash flows:



The bond can *best* be described as a:

- A. bullet bond.
 - B. fully amortized bond.
 - C. partially amortized bond.
24. Investors seeking some general protection against a poor economy are *most likely* to select a:
- A. deferred coupon bond.
 - B. credit-linked coupon bond.
 - C. payment-in-kind coupon bond.
25. The benefit to the issuer of a deferred coupon bond is *most likely* related to:
- A. tax management.
 - B. cash flow management.
 - C. original issue discount price.

26. Which of the following bond types provides the *most* benefit to a bondholder when bond prices are declining?
- A. Callable
 - B. Plain vanilla
 - C. Multiple put
27. Which type of call bond option offers the *greatest* flexibility as to when the issuer can exercise the option?
- A. A Bermuda call
 - B. A European call
 - C. An American call
28. Which of the following *best* describes a convertible bond's conversion premium?
- A. Bond price minus conversion value
 - B. Par value divided by conversion price
 - C. Current share price multiplied by conversion ratio