Question #1 of 11

Question ID: 1574142

Every six months a bond pays coupon interest equal to 3% of its par value. This bond is a:

A) 3% semiannual coupon bond.

B) 6% annual coupon bond.

C) 6% semiannual coupon bond.

Explanation

The coupon rate on a bond is the percentage of its par value that it pays in interest each year. The coupon frequency states how often the bond will pay interest. A 6% semiannual coupon bond pays interest twice per year with each coupon equaling half of 6%, or 3%, of par value.

(Module 49.1, LOS 49.a)

Question #2 of 11

Question ID: 1574140

Assuming bond yields are greater than zero, which of the following statements about zero-coupon bonds is *least* accurate?

A) A zero coupon bond may sell at a premium to par when interest rates decline.

B) All interest is earned at maturity.

C) The lower the price, the greater the return for a given maturity.

Explanation

Zero coupon bonds always sell below their par value, or at a discount prior to maturity. The amount of the discount may change as interest rates change, but a zero coupon bond will always be priced less than par if it has a positive yield.

(Module 49.1, LOS 49.a)

Question #3 of 11

Question ID: 1574144

An analyst observes a 5-year, 10% coupon bond with semiannual payments. The face value is £1,000. How much is each coupon payment?

A) £50.

B) £25.

C) £100.

Explanation

The coupon rate is the percentage of par value paid annually. With semiannual coupons, half of the annual coupon rate is paid every six months. For a 5-year, 10% coupon bond with semiannual payments and a face value of £1,000, each coupon payment is half of 10% times £1,000, or £50.

(Module 49.1, LOS 49.a)

Question #4 of 11

Question ID: 1574150

Restrictions on asset sales and additional borrowings by a bond issuer are *best* characterized as:

A) positive covenants.

B) negative covenants.

C) affirmative covenants.

Explanation

Negative covenants are prohibitive in nature, such as restrictions on asset sales and additional borrowings.

Affirmative or positive covenants are actions a borrower is required to take and are often administrative in nature, for example to comply with relevant laws and regulations or to insure and maintain assets.

(Module 49.1, LOS 49.b)

Question #5 of 11

Question ID: 1574149

A covenant that requires the issuer not to let the insurance coverage lapse on assets pledged as collateral is an example of a(n):

A) affirmative covenant.

B) inhibiting covenant.

C) negative covenant.

Explanation

Covenants are classified as negative or affirmative. Affirmative covenants specify administrative actions a bond issuer is required to take, such as maintaining insurance coverage on assets pledged as collateral. Negative covenants are restrictions on a bond issuer's actions, such as preventing an issuer from selling any assets that have been pledged as collateral or pledging them again as collateral for additional debt.

(Module 49.1, LOS 49.b)

Question #6 of 11

Question ID: 1574143

Which of the following fixed income securities is classified as a money market security?

A) Newly issued security that will mature in one year.

B) Security issued 18 months ago that will mature in six months.

C) Security issued six months ago that will mature in one year.

Explanation

Money market securities have original maturities of one year or less. Fixed income securities originally issued with maturities longer than one year are classified as capital market securities.

(Module 49.1, LOS 49.a)

Question #7 of 11

Question ID: 1574145

Which of the following contains the overall rights of the bondholders?

A) Covenant.

B) Indenture.

C) Rights offering.

Explanation

An indenture specifies the rights of bondholders and the obligations of the issuer. Covenants are specific provisions within the indenture. A rights offering is typically associated with an equity security.

(Module 49.1, LOS 49.b)

Question #8 of 11

Question ID: 1574146

A bond's indenture *least likely* specifies the:

A) source of funds for repayment.

B) covenants that apply to the issuer.

C) identity of the lender.

Explanation

The identity of the lender (i.e., the bondholder) is not specified in a bond's indenture because a bond may be traded during its life. An indenture or trust deed is a legal contract that specifies a bond issuer's obligations and restrictions. The indenture may include covenants that require the issuer to take or refrain from taking certain actions and may specify the source of funds for repayment, such as a project to be funded or the taxing power of a government.

(Module 49.1, LOS 49.b)

Question #9 of 11

Question ID: 1574147

Features specified in a bond indenture *least likely* include the bond's:

A) coupon rate and maturity date.

B) issuer and rating.

C) par value and currency.

Explanation

Bond ratings are assigned by third-party credit rating agencies and may change during the life of a bond. Features that are specified in the indenture for a fixed income security include its issuer, maturity date, par value, coupon rate and frequency, and currency.

(Module 49.1, LOS 49.b)

Question #10 of 11

Question ID: 1574141

A bond is trading at a premium if its:

A) price is greater than its par value.

B) redemption value is greater than its face value.

C) yield is greater than its coupon rate.

Explanation

If a bond's price is greater than its par value, the bond is trading at a premium. If a bond's yield is greater than its coupon rate, its price is less than par value and the bond is trading at a discount. Face value and redemption value both refer to par value.

(Module 49.1, LOS 49.a)

Question #11 of 11

Question ID: 1574148

Which of the following bond covenants is considered negative?

A) Maintenance of collateral.

B) No additional debt.

C) Payment of taxes.

Explanation

Negative covenants set forth limitations and restrictions, whereas affirmative covenants primarily set forth administrative activities that the borrower promises to do.

(Module 49.1, LOS 49.b)