

FIN 533 Homework
Due Thursday, October 15

You have a one-year investment horizon and are trying to choose among three bonds. All have the same degree of default risk and mature in 10 years. The first is a zero-coupon bond that pays \$1,000 at maturity. The second has an 8% coupon rate. The third has a 10% coupon rate.

- a. If all three bonds are priced to yield 8% to maturity, what are their prices?
- b. If you expect their yields to maturity to be 8% at the beginning of next year, what will be their prices then? What is your before-tax **holding-period return** on each bond?
- c. Recalculate your answer to b. under the assumption that you expect the yields to maturity on each bond to be 7% at the beginning of next year.