8.05 Pricing and Valuation of Forward Contracts and for an Underlying with Varying Maturities

Question 1
An investor can *most closely* create a synthetic short position in a 30-day forward rate agreement (FRA) on 60-day LIBOR by simultaneously:
A. buying a 60-day zero-coupon bond and selling a 30-day zero-coupon bond.
B. buying a 90-day zero-coupon bond and selling a 30-day zero-coupon bond.
C. buying a 30-day zero-coupon bond and selling a 90-day zero-coupon bond.

Question 2
An analyst gathers the following data:

Selected Data	
Bond price	100
Coupon rate	6%
Risk-free rate	4%

The bond has exactly 10 years until maturity and pays coupons annually. There are no other costs or benefits while holding the bond. A 1-year forward contract created with an initial value of zero *most likely* has an agreed-on price:
A. less than 100.
B. equal to 100.
C. greater than 100.

Question 3
The seller of a forward rate agreement (FRA) is *most likely* trying to:
A. hedge a future lending rate.
B. hedge a future borrowing rate.
C. speculate on rising interest rates.

Question 4
If the benefits of holding an asset are greater than the cost of holding it, futures contracts on the asset *most likely* trade at prices:
A. below the spot price.
B. equal to the spot price.
C. above the spot price.

Question 5
A corporate borrower plans to close on a bank loan in 30 days, when the loan terms will be finalized. The interest rate on the loan is tied to 90- day LIBOR. Based on only this information, which of the following transactions *most appropriately* hedges the company's interest rate risk?

A. Long 30-day forward rate agreement (FRA) on 90-day LIBOR
B. Long 90-day forward rate agreement (FRA) on 90-day LIBOR
C. Long 120-day forward rate agreement (FRA) on 90-day LIBOR

Question 6
Buying a forward rate agreement (FRA) is *most* similar to:
A. paying a fixed interest rate and receiving a floating interest rate.
B. paying a floating interest rate and receiving a fixed interest rate.
C. paying a floating interest rate over one term and receiving a floating rate over a longer term.

Question 7
Most likely, the long party in a forward rate agreement (FRA) benefits if forward rates:
A. decrease before the FRA expires.
B. do not change before the FRA expires.
C. increase before the FRA expires.

Question 8
Which of the following positions is *most likely* equivalent to selling a 90-day forward rate agreement on a 180-day interest rate?
A. Simultaneously going long a 270-day deposit and going short a 90-day deposit
B. Simultaneously going long a 180-day deposit and going short a 90-day deposit
C. Going long a 90-day deposit and, when that deposit matures, going long a 180-day deposit