Interest Rate Derivatives

Introduction

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Callable Bond

The bond has an embedded short call that reduces the value of the bond and increases the coupon. An issuer can call back the bond if bond prices rice in order to refinance at a lower coupon rate

Puttable Bond

The bond has an embedded long put that increases the value of the bond and decreases the coupon rate. If bond prices go down the holder can put the bond back and invest the proceeds at a higher coupon rate.

Bond Forward Level

$$\frac{B_0 - I}{df}$$

Where I is the net present value of the coupons paid over the lifetime of the bond and df is the price of zero coupon bond that pays 1$ on the forward date

Interest Rate Futures