INTEREST RATE QUOTATIONS AND MARKET TERMINOLOGY

TI &RM Chapter 6

Q: 1 What is the meaning of a "fixed rate of interest"?

a) An interest rate that changes periodically based on market conditions

b) An interest rate that remains constant throughout the tenure of the instrument

c) An interest rate that is linked to a benchmark rate

d) An interest rate that is applicable only to short-term loans

Q: 2 What happens to the market price of a fixed-rate bond when market interest rates rise above the coupon rate?

a) It increases significantly

b) It remains unchanged

c) It decreases

d) It fluctuates randomly

Q: 3 Which of the following is NOT a key feature of a floating rate instrument?

a) The interest rate is variable and linked to a benchmark rate
b) The coupon rate resets periodically based on market interest rates
c) The return to the investor remains fixed throughout the tenure
d) Price volatility is generally lower compared to fixed rate instruments

Q: 4 Why is price volatility lower in floating rate instruments compared to fixed rate instruments of the same tenure?

a) They are risk-free instruments
b) They have shorter tenures
c) The coupon rate adjusts with market rates
d) They are not traded in the secondary market

Q: 5 In a floating-rate instrument, if the benchmark rate decreases, what happens to the coupon payment?

a) It increases
b) It decreases
c) It remains unchanged
d) It becomes zero

Q: 6 Which of the following statements about Simple Interest is true?

a) Simple interest is calculated only on the principal

b) Simple interest is charged only once in entire loan Period.

c) Simple interest is easier to calculate than compound interest

d) All of the above

Q: 7 Simple interest is calculated only on the principal amount over a fixed period of time and charged only once in entire loan Period. What is the formula for calculating simple interest?

a) Principal × Rate × Time

b) Principal × (1 + Rate)^Time

c) Principal × Rate / Time

d) Principal + (Rate × Time)

Q: 8 A person purchases a car by obtaining a loan on simple interest. The car costs Rs 1,50,000 and the interest rate on the loan is 10 percent per annum (simple). If the loan is to be paid back after two years, calculate simple interest.

a) Rs 25,000

b) Rs 30,000

c) Rs 15,000

d) Rs 20,000

Q: 9 Which of the following statements about Compound Interest are correct?

I. Compound interest is an interest calculated on the principal and the existing interest together .
II. Compound interest includes interest on both the principal and previously earned interest.
III. The accumulated interest is added to the principal to form a new principal for the next period.
IV. Compound interest remains the same every year, regardless of the period.

a) Only statements 1 and 4 are correct
b) Only statements 2 and 3 are correct
c) Statements 1, 2, and 3 are correct
d) All statements are correct

Q: 10 If the compounding frequency increases, what happens to the total interest earned?

a) It decreases
b) It remains the same
c) It increases
d) It becomes zero

Q: 11 What is the formula for calculating Compound Interest?

a) A=p(1+r/n)^nt
b) A=a(1+r/n)^nt
c) A=p(1+r)^nt
d) A=p(1+r/n)^t

$$.A = p(1 + r/n)^{nt}$$

P = Principal (Initial amount you borrowed or deposited)

r= Annual rate of interest (per cent)

n = Number of compounding period for the year

A = Amount of money accumulated (Interest + principal)

Q: 12 A principal amount of Rs 10,0000 is invested at an annual compound interest rate of 6%. If the interest is compounded annually, what will be the total amount after 10 years?

a) 150000
b) 155000
c) 179084
d) 191000
Solution

$$.A = p(1 + r/n)^{nt}$$

Q: 13 X invested Rs.100000 in a bank FDR at 6% p.a. for 4 year. If interest is compounded on half-yearly basis, the amount payable shall be?

a) 120675
b) 126677.
c) 128525
d) 130251
Solution

$$. .A = p(1 + r/n)^{nt}$$

Q: 14 _____ refers to the return on investment or income generated from an investment, typically expressed as a percentage of the investment's cost, face value, or market price.

a) Dividend
b) Yield
c) Capital Gain
d) Net Worth

Q: 15 What is the definition of "nominal yield"?

a) The yield calculated based on the current market price of the security
b) The annual interest rate specified on the security, irrespective of its actual price
c) The total return earned if the security is held until maturity
d) The yield adjusted for inflation

Q: 16 Annual income (such as interest or dividends) earned from an investment, expressed as a percentage of the investment's current market price, is known as ____.

a) Face Value

b) Capital Gain
c) Current Yield
d) Net Asset Value

Q: 17 How is the "current yield" calculated?

a) (Coupon Payment / Face Value) × 100
b) (Coupon Payment / Current Market Price) × 100
c) (Face Value / Current Market Price) × 100
d) (Total Interest Earned / Purchase Price) × 100

Q: 18 A bond has a face value of Rs 1,000 and pays an annual interest (coupon) of Rs 80. If the current market price of the bond is Rs 1,200, what is the current yield?

a) 6.67%
b) 8.00%
c) 10.00%
d) 12.50%

Q: 19 What does "Yield to Maturity (YTM)" represent?

a) The annual interest rate specified on the bond
b) The yield based on the current market price of the bond

c) The yield adjusted for inflation

d) It is rate of return earned by the investor who purchases a bond and holds it till maturity.

Q: 20 A bond is said to be trading at a premium when_____

a) Its price is lower than the face value

b) Its price is higher than the face value

c) Coupon rate is lower than market interest rates

d) Yield to maturity is higher than coupon rate

Q: 21 Why do investors pay a premium for a bond?

a) Because its coupon payments are lower than market rates

b) Because its coupon payments are higher than market rates

c) Because the bond has no coupon payments

d) Because the bond is about to mature

Q: 22 Why does paying a premium for a bond reduce the bondholder's overall return?

a) Because the bondholder receives more than the purchase price at maturity
b) Because the bondholder receives the par value, which is lower than the purchase price, causing a capital loss
c) Because the coupon payments are lower than market rates
d) Because the bondholder pays less than the face value

Q: 23 Which of the following statements about a discount bond are correct?

a) A bond is at a discount when its market price is less than its par value.
b) A discount bond usually has a coupon rate lower than the prevailing market interest rates.
c) When you buy a discount bond, you pay less than par value but receive full par value at maturity, creating a capital gain.
d) All of the above

Q: 24 If yield is quoted on a front-ended basis for a discounted instrument, how does it compare to the YTM?

a) Front-end yield is higher than YTM
b) Front-end yield is the same as YTM
c) Front-end yield is lower than YTM
d) Front-end yield equals the coupon rate

Q: 25 In the A/360 day count convention, how is the year assumed?

a) 365 days
b) 360 days
c) 364 days
d) None of the above

Q: 26 In the A/A (Actual by Actual) day count convention, what happens if the period includes February 29 in a leap year?

a) The year is assumed to have 360 days
b) The denominator is 365 days
c) The denominator is 366 days
d) The denominator depends on the coupon rate

Q: 27 What is the key difference between front-end yield and rear-end yield?

a) Front-end yield is higher than rear-end yield
b) Front-end yield is the same as YTM, while rear-end yield is lower

c) Front-end yield is lower than YTM, while rear-end yield is the same as YTM

d) Front-end yield and rear-end yield are always equal