

Introduction to Finance
Quiz 4 *November 19, 2019*

1. Today is February 15, 2020, and we see the following quotes in the US Treasury market:

Security	Bid	Ask
Feb 15 2021 6% Bond	100.75	100.80
August 15 2020 STRIPS	97.65	97.75
Feb 15 2021 STRIPS	94.25	94.35

(a) **(10 points)** Is the bond trading cheap, fairly, or rich relative to the two STRIPS? *Show all work.*

(b) **(40 points)** In light of your answer to the preceding question, show how you would make arbitrage profits in this market. Show the trade, and the cash flows on all relevant dates.

2. Today is August 15, 2020, and we see the following quotes in the US Treasury market:

Security	Bid	Ask
Feb 15 2021 8.5% Bond	102.00	102.08
Feb 15 2021 2.25% Bond	99.20	99.25

(a) **(10 points)** Are these two bonds fairly priced relative to each other, or is one relatively cheap? *Show all work.*

(b) **(40 points)** In light of your answer to the preceding question, show how you would make arbitrage profits in this market. Show the trade, and the cash flows on all relevant dates.