FIN 360: PRINCIPLES OF FINANCIAL MANAGEMENT
BOND BASICS AND DEFINITIONS
CRITICAL THINKING & CONCEPTUAL QUESTIONS

1. Why is a bond's rate of return not always the coupon rate the bond pays you?
2. What might cause a bond's price to deviate from its face value?
3. For each of the options below, which bond would generally have to pay investors a greater yield, assuming all else equal? Explain why for each.
    a. Secured vs. unsecured
    b. Callable vs. non-callable
    c. Senior vs. subordinate
    d. *With* protective covenants vs. *without* protective covenants
    e. Investment grade vs. speculative grade
    f. A highly levered firm vs. a firm with low leverage
    g. Corporate bonds vs. treasury bonds
    h. Illiquid bonds vs. liquid bonds
    i. Municipal bonds vs. treasury bonds
4. What are the similarities and differences between a sinking fund and bond callability?
5. Why is callability not desirable for a bond investor?
6. Explain when a bond is more likely to be called.
7. Describe a typical corporate bond (that we see in the real world): how frequent are the payments? Are payments at the beginning or end of the period? Are the payments fixed? Are the bonds callable? Are they debentures?
8. What is the difference between T-bills, Treasury Notes, and Treasury Bonds?
9. What's the difference between acquiring bonds on the primary market vs. the secondary market?
10. What's the difference between a bid and ask price?
11. Describe the concept of the "asked yield" in U.S. Treasury quotes. What does this number tell us?
12. On a table of U.S. Treasury quotes, why are asked yields of bonds (with very different coupons) all about the same?
13. What is an attractive feature of municipal bonds? What is an unfavorable feature?
14. Explain the significance of a yield curve inversion. Explain what causes a yield curve inversion in the first place. Is the yield curve inverted now?
15. Bond prices and yields are inversely related. Explain what this means. In particular, discuss why fixed coupon payments matter, and what the statement "bonds of similar risk and structure will trade at (about) the same YTM regardless of the coupon rate" means.