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CFA® Program Level I

Fixed Income: 71 Free Practice Questions

2027 curriculum · 19 readings · answers and full explanations

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Version v2027.3 · October 2026

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CredGuild · CFA® Program Level I · Fixed Income: 71 Free Practice Questions
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Fixed Income

Questions 1–71 · 19 readings

51 Bond Indenture

Question 1

A dealer's inventory includes the three fixed-income securities described below. Which one is classified as a money market security?

A A note issued three years ago that matures in four months.

B A bill issued today that matures in nine months.

C A bond issued ten months ago that matures in 14 months.

Question 2

Which of the following describes a bond that is trading at a premium?

A Its coupon rate is below its market yield.

B Its market price is above its par value.

C Its face value is below its redemption value.

Question 3

Government bond yields are 4.60% for 2 years, 4.10% for 7 years and 3.90% for 10 years. Ardent Rail's 7-year bond yields 5.85%. The spread on Ardent Rail's bond and the shape of the government yield curve are best described as:

A 1.25%; inverted yield curve.

B 1.75%; normal yield curve.

C 1.75%; inverted yield curve.

52 Zero Coupon Bond

Question 4

A bond with a par value of $2,000 carries a 6.8% coupon rate, paid semiannually, and is quoted at a price of 104.35. The dollar amount of each semiannual coupon is:

A $136.00.

B $70.96.

C $68.00.

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Question 5

Which statement about a sinking fund provision is *most accurate*?

A It obliges the issuer to deposit cash in a reserve that is used to repay the whole issue at maturity.

B It gives bondholders the right to sell their bonds back to the issuer at par each year.

C It obliges the issuer to retire part of the issue at scheduled dates before the final maturity.

Question 6

Priya Nair's main concern in her bond portfolio is reinvestment risk. Which of the following is she *least likely* to do?

A Choose a noncallable bond over an otherwise identical callable bond.

B Choose a low-coupon bond over a high-coupon bond of the same maturity.

C Rely on holding a coupon-paying bond to maturity to remove the risk.

Question 7

Which of the following bond issues best fits the definition of a Eurobond?

A A Mexican firm's Swiss franc bonds sold to investors in Switzerland.

B An Indian firm's Australian dollar bonds sold to investors in Singapore.

C A German firm's euro-denominated bonds sold to investors in Germany.

Question 8

Maren Holt buys a newly issued 8-year corporate bond at 106.40 per 100 of par. It pays a 6.5% annual coupon, and she plans to hold it to maturity. Her country taxes coupon interest as ordinary income and gives bonds issued at a premium the treatment that mirrors its original issue discount (OID) provision. Each year, the tax treatment of her coupons is *most likely* that:

A part of the 6.40 premium reduces the taxable portion of her coupon interest.

B the full 6.50 coupon is taxed as ordinary income, with no adjustment for the premium.

C part of the 6.40 premium is added to her taxable interest income.

53 Fixed-Income Issuance and Trading

Question 9

A bond database lets users group bonds along several dimensions: type of issuer (sector), credit quality, original maturity and currency. Which of the following groups results from sorting bonds by type of issuer?

A Bonds denominated in euros.

B Short-term money market securities.

C Bonds issued by special purpose entities.

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Question 10

An analyst compares bond market indexes with stock market indexes. Which of the following statements is *least accurate*?

A A bond index typically contains far more constituents than a stock index.

B A single company often has many bonds outstanding but only two or three share classes.

C The set of bonds in an index changes less often than the set of stocks in a stock index.

Question 11

Which of the following issuers *most likely* sells its new bonds through a public auction?

A A national government.

B A corporation.

C A municipality.

Question 12

Tamsin Hale wants to buy $2 million face value of a mid-sized corporate bond that was issued six years ago and now trades only infrequently. She is *most likely* to:

A submit a competitive bid in the issuer's next bond auction.

B buy from a dealer at its ask price, paying a relatively wide spread.

C buy on an exchange order book, paying a spread similar to an on-the-run sovereign bond.

54 Commercial Paper

Question 13

A corporate treasurer is reviewing the bank credit lines available to her company. Which of the following statements about these lines is *most accurate*?

A An uncommitted line typically carries a commitment fee on its unused portion.

B A committed line is the least reliable source of bank funding for a company.

C A revolving line often runs for years and usually comes with restrictive covenants.

Question 14

A bond dealer finances a position by entering a 60-day repurchase agreement. It delivers government bonds with a market value of $25,000,000. The lender requires an initial margin of 102% and a repo rate of 3.6%, using a 360-day year. The repurchase price the dealer will pay at the end of the term is *closest* to:

A $24,656,863.

B $24,647,000.

C $24,509,804.

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Question 15

An analyst splits the yield of each of three bonds into a benchmark rate and a credit spread. The spread accounts for 4% of Bond P's yield, 12% of Bond Q's yield and 45% of Bond R's yield. Which type of bond is Bond R *most likely* to be?

A A government bond.

B An investment-grade corporate bond.

C A high-yield corporate bond.

55 Treasury Bonds

Question 16

A bond analyst wants to group bonds according to the geography of their issuers. Which of the following labels fits that approach?

A Supranational bonds.

B Municipal bonds.

C Emerging market bonds.

Question 17

The central bank of Valdoria conducts much of its policy through a group of designated primary dealers. Which transaction is it *most likely* to carry out with them?

A Expansionary monetary policy by selling government bonds.

B Expansionary monetary policy by buying government bonds.

C Contractionary fiscal policy by cutting government spending.

Question 18

An analyst is building a government yield curve to use as the default-risk-free benchmark. The yields she uses are *most likely* taken from:

A older government bonds that have been outstanding for many years.

B the most recently issued government bonds of each maturity.

C highly rated supranational bonds.

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56 Yield to Maturity

Question 19

Five years ago, Kessler Freight Lines sold 25-year bonds with a 5.5% annual coupon, paid semiannually, to finance new rail terminals. The bonds now yield 5.2%. The price of the bonds per 100 of par is *closest* to:

A 103.70.

B 102.32.

C 96.39.

Question 20

With respect to a bond traded between coupon dates, accrued interest:

A is the interest earned from the last coupon date up to the settlement date.

B is the part of the next coupon that the seller has not earned.

C is discounted together with the other cash flows to obtain the full price.

Question 21

Holding all other features constant, which of the following statements about option-free bonds is *most accurate*?

A A long-maturity bond's price is more sensitive to yield changes than a short-maturity bond's price.

B A bond's price is more sensitive to increases in yield than to decreases in yield of the same size.

C A high-coupon bond's price is more sensitive to yield changes than a low-coupon bond's price.

Question 22

Marguerite Olsen wants to estimate the yield to maturity of a non-traded 7-year, annual-pay bond rated A. Actively traded A-rated bonds yield 4.10% at a 5-year maturity and 5.60% at a 10-year maturity. Using matrix pricing, the estimated YTM for the non-traded bond is *closest* to:

A 5.00%.

B 4.85%.

C 4.70%.

57 Credit Spread

Question 23

An analyst discounts every cash flow of a bond at one uniform rate, choosing the rate so that the total present value equals the bond's market price. This rate is the bond's:

A Yield to maturity.

B Current yield.

C Simple yield.

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Question 24

Delmont Paper's $1,000 par value bonds carry a 9% coupon rate and are quoted at a price of $962. The bonds' current yield is *closest* to:

A 8.66%.

B 9.00%.

C 9.36%.

Question 25

An analyst calculates a bond's yield to maturity using its scheduled coupon dates. Two of those dates fall on a Sunday, so the issuer will pay on the following Monday. The analyst then recalculates the yield using the dates on which the cash will actually be received. The recalculated figure is best described as:

A the true yield, slightly higher than the first figure.

B the street convention yield, slightly lower than the first figure.

C the true yield, slightly lower than the first figure.

Question 26

Which description of a callable bond's yield to worst is *most accurate*? It is the:

A yield the investor earns if the issuer defaults on its payments.

B lowest of the bond's yield to maturity and its yields to each call date.

C yield implied by the lowest price at which the bond has traded.

Question 27

A callable corporate bond has a zero-volatility spread of 160 basis points, and its embedded call option has a positive value. The bond's option-adjusted spread (OAS) is *most likely*:

A greater than 160 basis points.

B equal to 160 basis points.

C less than 160 basis points.

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58 Yield and Yield Spread Measures for Floating-Rate Instruments

Question 28

Carrow Logistics has a $5 million floating-rate note outstanding that pays an annual coupon equal to the market reference rate (MRR) plus a quoted margin of 110 basis points. Today is a reset date with exactly four years remaining to maturity. The MRR is 4.20%, and the discount margin the market currently requires on Carrow's credit is 70 basis points. Using the simplified approach that holds the MRR constant, the estimated value of the note is *closest* to:

A $5,071,084.

B $5,000,000.

C $4,929,572.

Question 29

Tenby Savings Bank issues a 91-day negotiable certificate of deposit. An investor who deposits $1,000 today receives $1,006.50 at maturity. The certificate's bond equivalent yield is *closest* to:

A 2.57%.

B 2.61%.

C 2.63%.

Question 30

A floating-rate note issued by Penhale Chemicals pays the market reference rate plus 85 basis points. Dealers now price the note at a discount margin of 55 basis points. Which of the following is the *most likely* explanation for the difference?

A The market reference rate has fallen since the note was issued.

B The issuer's credit quality has improved since the note was issued.

C The note is currently priced below its par value.

59 The Term Structure of Interest Rates: Spot, Par, and Forward Curves

Question 31

Which of the following statements about zero-coupon bonds and spot rates is *most accurate*?

A If a 4-year zero-coupon bond yields 5.2%, the 4-year spot rate is 1.3%.

B Spot rates are the same for every maturity on the term structure.

C At a positive yield, a zero-coupon bond's whole return is price appreciation.

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Question 32

Which of the following *best* describes how the arbitrage-free approach values an option-free bond?

A It discounts the cash flows at a set of spot rates that reflects the current term structure.

B It discounts the cash flows at the geometric average of the current spot rates.

C It discounts all the cash flows at a single discount rate.

Question 33

Government spot rates are 2.1% for one year, 2.9% for two years and 3.6% for three years (annual compounding). The coupon rate at which a 3-year annual-pay government bond would be priced at par (the 3-year par rate) is *closest* to:

A 2.87%.

B 3.57%.

C 3.60%.

Question 34

Current market rates (annual compounding) are as follows: the 1-year spot rate is 2.8%, the 1-year forward rate one year from now is 4.6%, and the 1-year forward rate two years from now is 6.2%. The price per 100 of par of a 3-year zero-coupon bond is *closest* to:

A 92.05.

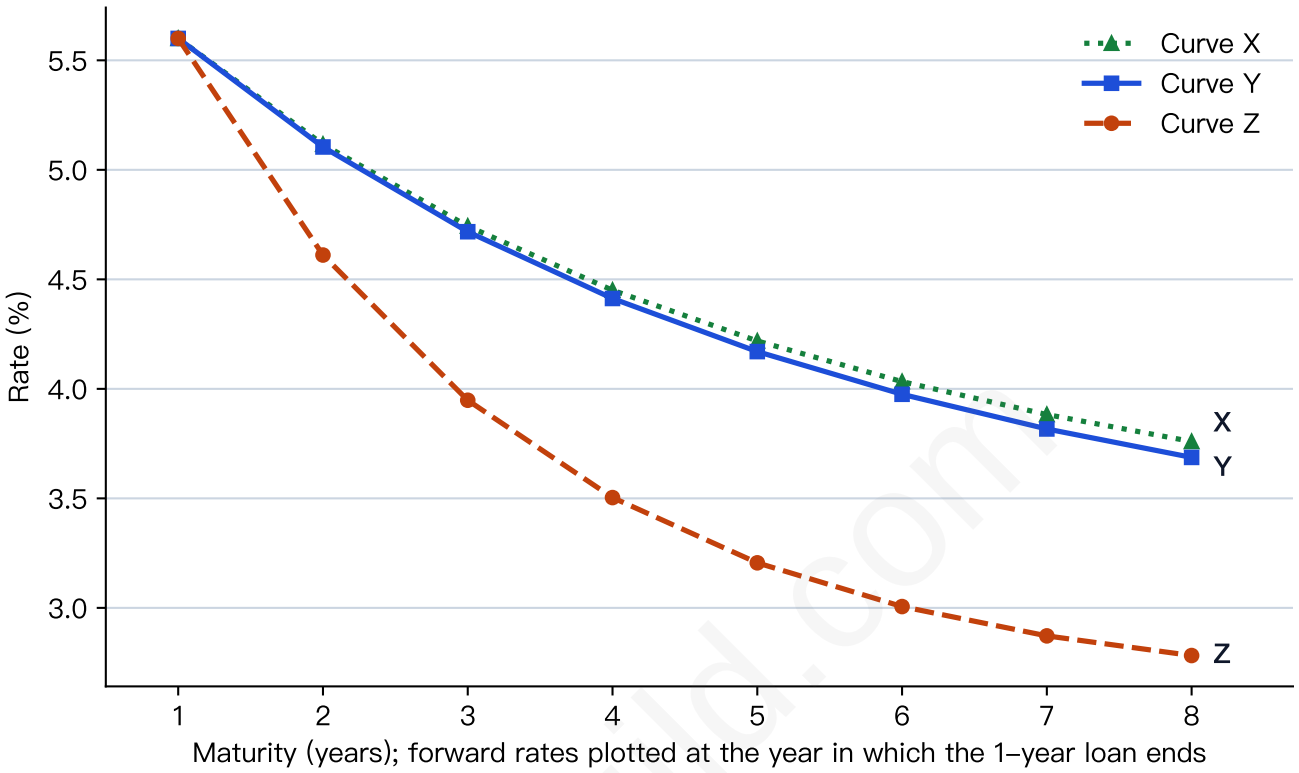
B 87.57.

C 83.49.

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Question 35

The chart below shows the spot curve, the par curve and the forward curve of 1-year rates, all derived from the same set of government bond prices (annual compounding). The curves are labeled only X, Y and Z.



Three curves derived from the same government bond prices

Curve X is *most likely* the:

A par curve.

B spot curve.

C forward curve.

60 Interest Rate Risk and Return

Question 36

A wealth manager tells a client: "When you invest in a bond for a given horizon, your return comes from the coupons you collect plus the difference between what you paid and what you receive when you sell the bond or it matures." The wealth manager's description is:

A incomplete, because it leaves out interest earned on reinvested coupons.

B complete, because it captures all sources of bond return.

C incomplete, because a bond held to maturity produces no capital gain or loss.

Question 37

Dmitri Volkov bought a 15-year, 4% semiannual-coupon bond at a yield to maturity of 5.2%. Four years later, he sells it for 92.10 per 100 of par. Per 100 of par, Volkov realizes:

A a capital gain of 2.06.

B a capital gain of 4.49.

C a capital loss of 7.90.

Question 38

A pension fund must make a single payment in eight years. The trustees want any change in the income from reinvesting coupons to be roughly offset by an opposite change in the price at which the bonds are sold at the horizon. Which measure of the bonds' duration should they set equal to eight years?

A Modified duration.

B Effective duration.

C Macaulay duration.

Question 39

Rafael Quintero calculates a Macaulay duration of 3.46 for a four-year, option-free corporate bond. The best interpretation of 3.46 is that it measures:

A the bond's price sensitivity to a change in interest rates.

B the average time until the bond's cash flows are received.

C the time the investor needs to recover his principal.

61 Macaulay Duration

Question 40

A 7-year, option-free, annual-pay bond with a 5% coupon is priced at $944.18 for each $1,000 of face value. Its Macaulay duration is 6.0444. Its modified duration is *closest* to:

A 5.868.

B 5.757.

C 5.702.

Question 41

An analyst uses modified duration alone to estimate how an option-free bond's price will respond to a 150 basis point decline in its yield. Compared with the actual price change, the estimate will *most likely*:

A understate the price increase.

B overstate the price increase.

C match the price increase closely.

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Question 42

A portfolio holds $6 million par value of an option-free bond with a full price of 98.75 per 100 of par and an annual modified duration of 5.4. If the bond's yield to maturity rises by 15 basis points, the estimated change in the value of the position, based on its money duration, is *closest* to:

A −$479,925.

B −$48,600.

C −$47,993.

Question 43

An option-free 20-year bond trades at a premium to par. If market interest rates rise, the bond's modified duration:

A increases.

B does not change.

C decreases.

Question 44

A 6-year floating-rate note resets its coupon to the market reference rate every six months. The most recent reset was two months ago. The note's Macaulay duration is *closest* to:

A 0.33 years.

B 0.50 years.

C 6.00 years.

62 Bond Convexity

Question 45

A 1.5-year option-free bond pays an 8% coupon semiannually and is priced to yield 6.00%. Using the present values of its cash flows as weights, its annualized convexity is *closest* to:

A 2.69.

B 5.37.

C 10.75.

Question 46

Three option-free bonds are priced at the same yield to maturity. Which one is *most likely* to have the highest convexity?

A A 10-year bond with a 7% coupon.

B A 25-year bond with a 2% coupon.

C A 10-year bond with a 2% coupon.

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Question 47

Which statement about an option-free bond with positive convexity is *most accurate*?

A A given fall in yield raises its price by more than the same rise in yield lowers it.

B An increase in its yield leads to an increase in its price.

C Its price rises and falls at a faster rate than its yield changes.

Question 48

A portfolio holds the three option-free bonds shown below (prices per 100 of par).

Portfolio holdings

Bond	Par value ($)	Price (per 100 of par)	Duration
Bond 1	1,000,000	112	3.1
Bond 2	1,200,000	86	10.8
Bond 3	800,000	101	6.0

Using the weighted-average method, the portfolio's duration is *closest* to:

A 6.58.

B 6.63.

C 6.95.

63 Curve-Based and Empirical Fixed-Income Risk Measures

Question 49

Effective duration is a better measure than modified duration of a bond's price sensitivity to interest rates when:

A the yield curve shifts in a nonparallel way.

B the bond has an embedded option.

C the bond has a long maturity and a low coupon rate.

Question 50

Interest rates fall by 65 basis points. Given a modified duration of 6.72 and a convexity of 55.30, the estimated percentage change in the bond's price is *closest* to:

A 4.48%.

B 4.37%.

C 4.25%.

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Question 51

A key rate duration measures the sensitivity of a bond's value to a:

A parallel shift in the benchmark yield curve.

B change in the bond's expected cash flows.

C change in the benchmark yield at one specific maturity.

Question 52

To estimate the interest rate sensitivity of a corporate bond fund, an analyst regresses the fund's past returns on past changes in benchmark government yields. The resulting measure is *best* described as:

A modified duration.

B analytical duration.

C empirical duration.

64 Credit Risk

Question 53

To judge how likely Morrow Chemicals is to default, an analyst calculates its EBIT margin, its EBIT-to-interest expense ratio, and its debt-to-EBITDA ratio. This analysis is *most likely* an evaluation of the company's:

A capacity.

B collateral.

C covenants.

Question 54

The trustees of the Linwood Teachers' Pension Plan propose to select corporate bonds using agency credit ratings alone. Which of the following is a limitation of relying solely on credit ratings?

A Agencies rate bond issuers but not individual bond issues.

B Bond prices and credit spreads can move well before a rating changes.

C Ratings let investors compare credit risk across industries and bond types.

Question 55

A portfolio manager at Corvel Asset Management expects the economy to move out of recession into a strong recovery over the coming year. Which change to her bond portfolio is *most appropriate*?

A Buy corporate bonds and sell government bonds.

B Sell corporate bonds and buy government bonds.

C Replace lower-rated corporate bonds with higher-rated ones.

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Question 56

A corporate bond has a modified duration of 6.2 and a convexity of 52. If its credit spread widens by 60 basis points while benchmark yields are unchanged, the estimated percentage change in the bond's full price is *closest* to:

A −3.63%.

B −3.72%.

C −3.81%.

65 Credit Analysis for Government Issuers

Question 57

Salvarra's central bank operates independently of the government and has a credible record of adjusting interest rates and the money supply to keep inflation low. In a sovereign credit analysis of Salvarra, this strength is best classified under which qualitative factor?

A Fiscal flexibility.

B External status.

C Monetary effectiveness.

Question 58

An analyst compares the fiscal strength of two sovereign issuers using the following data.

Selected fiscal data for two sovereign issuers (USD billions)

Item	Kestria	Varnholm
Nominal GDP	1,200	500
Government debt	780	290
Government revenue	420	145
Annual interest expense on government debt	29.4	13.05

Based on the debt burden (government debt to GDP) and debt affordability (interest expense to government revenue), which statement is *most accurate*?

A Kestria is stronger on both debt burden and debt affordability.

B Varnholm has the lighter debt burden, but Kestria has better debt affordability.

C Varnholm is stronger on both debt burden and debt affordability.

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Question 59

The regional government of Varenna sets up a transit authority to build a light-rail line. The authority issues bonds whose interest and principal are to be paid from the line's fare revenue. The national government also guarantees the bonds as a backstop. These bonds are *best* described as:

A general obligation bonds.

B revenue bonds.

C sovereign bonds.

66 Credit Analysis for Corporate Issuers

Question 60

All else equal, which of the following would indicate *higher* credit quality for a corporate issuer?

A Higher leverage

B Higher liquidity

C Lower coverage of debt service

Question 61

Tamworth Mills is being liquidated. It has three classes of debt outstanding: senior subordinated notes, first mortgage bonds and senior unsecured notes. Which list ranks them from highest to lowest priority of claims?

A First mortgage bonds, senior unsecured notes, senior subordinated notes.

B Senior unsecured notes, first mortgage bonds, senior subordinated notes.

C First mortgage bonds, senior subordinated notes, senior unsecured notes.

Question 62

How does an issuer credit rating *most likely* differ from an issue credit rating?

A An issuer credit rating reflects the borrower's overall creditworthiness.

B An issue credit rating is always set below the issuer credit rating.

C An issue credit rating is the one based on senior unsecured debt.

67 Fixed-Income Securitization

Question 63

Kestrel Savings Bank funds its mortgage lending mainly with customer deposits. It sells $400 million of its mortgages to a special purpose entity, which pays for them with the proceeds of an ABS issue. As a direct result of the sale, which item on Kestrel's balance sheet is *least likely* to change?

A Mortgage loans.

B Customer deposits.

C Cash.

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Question 64

Brenlow Bank sells a pool of its auto loans to a newly created trust, which issues asset-backed securities (ABS). The senior ABS receive a higher credit rating than Brenlow's own senior bonds. The *most likely* reason is that:

A ABS are always investment grade, whereas bank bonds need not be.

B the trust is a special purpose entity that is bankruptcy remote from Brenlow.

C the ABS rank senior to Brenlow's bonds if Brenlow goes bankrupt.

Question 65

An investor buys ABS backed by a pool of consumer loans originated by Farrow Bank. Which of the following risks does the investor *most likely* bear?

A The credit risk of Farrow Bank's other lending businesses.

B The credit risk of the borrowers in the collateral pool.

C The risk that Farrow Bank's creditors seize the collateral.

68 Asset-Backed Security (ABS) Instrument and Market Features

Question 66

Compared with otherwise similar asset-backed securities, covered bonds issued by Eskdale Bank *most likely* offer investors:

A recourse to the issuing bank.

B higher yields.

C lower credit quality.

Question 67

Halden Card Trust issued asset-backed securities backed by credit card receivables, and the securities are still in their lockout period. Which event would *most likely* cause the ABS holders to start receiving principal payments ahead of schedule?

A Cardholders repay a larger share of their balances each month.

B A trigger in the early (rapid) amortization provision is breached.

C The interest rate charged on the card balances reaches its cap.

Question 68

Which feature *most clearly* distinguishes a collateralized debt obligation (CDO) from most other asset-backed securities?

A It is issued through a special purpose vehicle.

B A collateral manager actively trades the securities in its collateral pool.

C It is structured with senior and subordinated tranches.

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69 Mortgage-Backed Security (MBS) Instrument and Market Features

Question 69

A sequential-pay CMO has two tranches. Class J receives all principal payments until it is fully repaid, and principal then goes to Class K. Relative to Class K, Class J has:

A less contraction risk and more extension risk.

B more contraction risk and more extension risk.

C more contraction risk and less extension risk.

Question 70

The Linwell pass-through security is backed by the three mortgages shown below. Servicing and guarantee fees total 0.50% a year.

Mortgages in the Linwell pass-through pool

Mortgage	Current balance ($ thousands)	Mortgage rate	Remaining term (years)
1	120	5.00%	22
2	80	6.50%	15
3	200	5.75%	27

The pass-through rate on the security is *closest* to:

A 5.18%.

B 5.25%.

C 5.68%.

Question 71

When comparing the loans backing different CMBS pools, which combination of credit ratios *most likely* indicates better credit quality?

A Higher DSC ratios and lower LTV ratios.

B Lower DSC ratios and higher LTV ratios.

C Higher DSC ratios and higher LTV ratios.

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FIXED INCOME

Answers and explanations

Answer key: 1. B · 2. B · 3. C · 4. C · 5. C · 6. C · 7. B · 8. A · 9. C · 10. C · 11. A · 12. B · 13. C · 14. A · 15. C · 16. C · 17. B · 18. B · 19. A · 20. A · 21. A · 22. C · 23. A · 24. C · 25. C · 26. B · 27. C · 28. A · 29. B · 30. B · 31. C · 32. A · 33. B · 34. B · 35. A · 36. A · 37. A · 38. C · 39. B · 40. C · 41. A · 42. C · 43. C · 44. A · 45. A · 46. B · 47. A · 48. A · 49. B · 50. A · 51. C · 52. C · 53. A · 54. B · 55. A · 56. A · 57. C · 58. B · 59. B · 60. B · 61. A · 62. A · 63. B · 64. B · 65. B · 66. A · 67. B · 68. B · 69. C · 70. A · 71. A

Question 1 **Answer: B**

Money market securities are those with an original maturity of one year or less. The bill issued today with nine months to maturity has an original maturity of nine months, so it is a money market security.

Why the other options are wrong

- **A.** The note had an original maturity of about three years and four months. Its short remaining maturity does not change its classification: it is a capital market security.
- **C.** The bond's original maturity is 10 + 14 = 24 months, which is longer than one year, so it is a capital market security.

Key takeaway Money market and capital market securities are classified by original maturity at issuance. The time remaining does not change the classification.

Reading 51: Fixed-Income Instrument Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-indenture/

Question 2 **Answer: B**

A bond trades at a premium when its price exceeds its par value. For a fixed-coupon bond this happens when the market yield is below the coupon rate.

Why the other options are wrong

- **A.** A coupon rate below the market yield means the bond's price is below par, so the bond trades at a discount.
- **C.** A bond's redemption value can differ from its face value under its terms, but that difference does not determine whether it trades at a premium. A premium means market price is above par.

Key takeaway A premium bond has a price above par (yield below the coupon rate). A discount bond has a price below par (yield above the coupon rate).

Reading 51: Fixed-Income Instrument Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-indenture/

Question 3 **Answer: C**

The spread is the extra yield over a government bond of the same maturity: 5.85% − 4.10% = 1.75%. Government yields fall as maturity lengthens, so the curve slopes downward, which is an inverted yield curve.

$$\text{Spread} = 5.85\% - 4.10\% = 1.75\% \ (175 \text{ bps})$$

Yields: 2-year 4.60% > 7-year 4.10% > 10-year 3.90%, so the government curve slopes downward (inverted).

Why the other options are wrong

- **A.** 1.25% measures the spread against the 2-year government yield (5.85% − 4.60%); the benchmark must have the same 7-year maturity.
- **B.** The spread is right, but a curve on which longer maturities yield less is inverted; a normal yield curve slopes upward.

Key takeaway Match maturities when measuring a spread. An upward-sloping curve is normal, and a downward-sloping curve is inverted.

Reading 51: Fixed-Income Instrument Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-indenture/

Question 4 Answer: C

Coupons are based on par value, and the market price plays no part. Half of the annual coupon is paid every six months.

$$\text{Semiannual coupon} = \frac{\text{coupon rate} \times \text{par}}{2} = \frac{0.068 \times \$2{,}000}{2} = \$68.00$$

The quoted price of 104.35 (104.35% of par) does not enter the calculation.

Why the other options are wrong

- **A.** $136.00 is the full annual coupon; it is not divided by two for semiannual payments.
- **B.** $70.96 applies the coupon rate to the market price ($2{,}000 \times 1.0435$) instead of to the par value.

Key takeaway The price quote is irrelevant to the coupon amount. Each coupon equals the coupon rate times par, divided by the number of payments per year.

Reading 52: Fixed-Income Cash Flows and Types. Notes: credguild.com/cfa/level-1/notes/fixed-income/zero-coupon-bond/

Question 5 Answer: C

A sinking fund provision requires the issuer to retire a portion of the bond issue at specified times over its life. Typically the bond trustee redeems a set amount of principal each year from holders chosen at random. Principal is therefore repaid through a series of payments rather than all at maturity.

Why the other options are wrong

- **A.** The bonds are actually retired on the schedule. The provision does not simply build up cash to repay the whole issue at maturity.
- **B.** A right to sell bonds back to the issuer at a set price is a put option, which belongs to the bondholder. A sinking fund is an obligation of the issuer, and the bonds redeemed are chosen by the trustee, not by the holders.

Key takeaway A sinking fund retires part of the issue on a schedule over its life, which reduces the principal outstanding at maturity.

Reading 52: Fixed-Income Cash Flows and Types. Notes: credguild.com/cfa/level-1/notes/fixed-income/zero-coupon-bond/

Question 6 Answer: C

Holding a coupon bond to maturity does not remove reinvestment risk, because every coupon received must still be reinvested at whatever rates then prevail. An investor focused on reinvestment risk would therefore not rely on this.

Why the other options are wrong

- **A.** A callable bond may be redeemed early, typically after rates have fallen, forcing reinvestment at lower yields. Preferring a noncallable bond reduces reinvestment risk, so she is likely to do this.
- **B.** Smaller coupons mean less cash to reinvest, so a low-coupon bond carries less reinvestment risk. She is likely to prefer it.

Key takeaway Reinvestment risk rises with coupon size and with call features; only a zero-coupon bond held to maturity avoids it.

Reading 52: Fixed-Income Cash Flows and Types. Notes: credguild.com/cfa/level-1/notes/fixed-income/zero-coupon-bond/

Question 7 **Answer: B**

A Eurobond is issued outside the jurisdiction of any one country and can be issued in any currency. An Indian firm's Australian dollar bonds sold to investors in Singapore are not issued in Australia's or India's domestic market, so they fit the Eurobond definition. The "Euro" prefix does not mean the bonds are denominated in euros, sold in Europe or issued by a European firm.

Why the other options are wrong

- **A.** A foreign issuer selling bonds in Switzerland, in Swiss francs, to Swiss investors is issuing a foreign bond.
- **C.** A German issuer selling euro bonds to investors in its home market is issuing a domestic bond; being denominated in euros does not make it a Eurobond.

Key takeaway A Eurobond is issued outside the jurisdiction of any one country and can be in any currency. The "Euro" prefix says nothing about the currency, the market of sale or the issuer's home country.

Reading 52: Fixed-Income Cash Flows and Types. Notes: credguild.com/cfa/level-1/notes/fixed-income/zero-coupon-bond/

Question 8 **Answer: A**

Under an OID provision, part of the discount on a bond issued below par is taxed each year as interest income. Some jurisdictions treat bonds issued at a premium symmetrically: part of the premium is used to reduce the taxable portion of the coupon interest. Holt paid 6.40 above par and will receive only par at maturity, so in her country part of that premium offsets her 6.50 coupon each year before tax.

Why the other options are wrong

- **B.** Taxing the full coupon with no adjustment ignores the premium treatment stated in the stem. Her country lets part of the premium reduce the taxable portion of the coupons.
- **C.** Adding part of the price difference to taxable interest each year is the OID treatment of a bond issued at a discount. For a bond issued at a premium the adjustment runs the other way and reduces taxable coupon interest.

Key takeaway With an OID provision, part of a discount is taxed each year as interest income. With the symmetric premium treatment, part of a premium reduces the taxable portion of the coupons.

Reading 52: Fixed-Income Cash Flows and Types. Notes: credguild.com/cfa/level-1/notes/fixed-income/zero-coupon-bond/

Question 9 **Answer: C**

Classification by type of issuer (sector) separates governments (sovereign and non-sovereign), corporates, and special purpose entities issuing asset-backed securities. Bonds issued by special purpose entities are grouped by who the issuer is, so this group results from sorting by issuer. The other two groups come from the currency

and original-maturity dimensions.

Why the other options are wrong

- **A.** Bonds denominated in euros are grouped by currency, which is one of the other ways to classify bonds. Any type of issuer can sell bonds in euros.
- **B.** Money market securities are defined by original maturity (one year or less). Any type of issuer can sell them.

Key takeaway Sort the labels: type of issuer (governments, corporates, special purpose entities issuing ABSs), credit quality, original maturity (money market, intermediate, long-term), and other dimensions such as currency, issuer geography and ESG features.

Reading 53: Fixed-Income Issuance and Trading. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-issuance-and-trading/

Question 10 **Answer: C**

The bond universe is constantly changing. Bonds mature, are called or retired through sinking funds, and new issues come to market all the time. Bond indexes therefore have higher turnover than stock indexes, so the claim that their membership changes less often is inaccurate. This instability is one reason bond indexes are harder to build and track.

Why the other options are wrong

- **A.** This is accurate. Because issuers have many bonds each, bond indexes hold many more constituents than stock indexes, which is why tracker funds use sampling.
- **B.** This is accurate. It is the reason bond indexes have so many more constituents than equity indexes.

Key takeaway Bond vs. stock indexes: more constituents, higher turnover, and weights driven by issuance (large sovereign weights).

Reading 53: Fixed-Income Issuance and Trading. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-issuance-and-trading/

Question 11 **Answer: A**

Public offerings of government debt commonly take place through auctions, and sovereign (national government) issuers sell their bonds through regular public auctions. Corporations normally issue through investment banks, in underwritten or best-efforts offerings, or through private placements.

Why the other options are wrong

- **B.** Corporate bonds are usually sold through an investment bank on an underwritten or best-efforts basis, or placed privately with a small group of investors.
- **C.** A municipality is a local, non-sovereign government. Regular public auctions are the standard method for sovereign (national government) debt, so a national government is the more likely auction issuer.

Key takeaway Auctions are the standard route for government (sovereign) debt.

Reading 53: Fixed-Income Issuance and Trading. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-issuance-and-trading/

credguild.com

Question 12 **Answer: B**

A bond that was issued years ago is bought in the secondary market, where previously issued bonds trade among investors. Although some electronic platforms and exchange-based trading exist, most secondary bond trading still takes place in the dealer, or over-the-counter (OTC), market: dealers post bid (purchase) and ask (selling) prices, so a buyer pays the ask. The dealer's spread depends on liquidity, and for a smaller, older (seasoned), infrequently traded corporate issue it is typically 10 to 20 basis points or more.

Why the other options are wrong

- **A.** Auctions are a primary-market method for selling newly issued bonds, used mainly by governments. A bond issued six years ago is already outstanding, so it must be bought from another investor in the secondary market, and corporations usually issue through underwritten or best-efforts offerings rather than auctions anyway.
- **C.** Exchange trading dominates for shares, while most secondary bond trading is OTC. Spreads of a fraction of a basis point are found only on very liquid bonds, such as on-the-run developed-market sovereigns and bonds of frequent high-quality corporate issuers. A seasoned, thinly traded issue is quoted much wider.

Key takeaway Previously issued bonds trade mainly OTC through dealers, and the buyer pays the ask. The dealer's spread widens as liquidity falls, from a fraction of a basis point for on-the-run sovereigns to 10–20 bp or more for seasoned corporates.

Reading 53: Fixed-Income Issuance and Trading. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-issuance-and-trading/

Question 13 **Answer: C**

A revolving (operating) line of credit is the most reliable source of bank funding. It is typically arranged for a longer term than a committed line, sometimes several years, and because the bank is committed for that long it usually imposes restrictive covenants that oblige the borrower to take, or to avoid, specified actions, much as a bond indenture does. Its fees and rates are similar to those of a committed line.

Why the other options are wrong

- **A.** An uncommitted line is flexible and usually has no fees beyond interest on the amounts drawn, because the bank can decline to lend if conditions change. Commitment fees (about 50 bp on the full or unused amount) are charged on committed lines, and revolvers carry similar fees.
- **B.** The least reliable form is the uncommitted line, which the bank can decline to honor. A committed line binds the bank for the stated period, although the bank may decline to renew it at maturity (renewal risk).

Key takeaway Reliability rises from uncommitted to committed to revolving lines. Commitment fees apply to committed lines and revolvers, and revolvers usually add restrictive covenants over a multiyear term.

Reading 54: Fixed-Income Markets for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/commercial-paper/

Question 14 **Answer: A**

The loan (purchase price) equals the collateral's market value divided by the initial margin. The repurchase price is the loan plus interest at the repo rate, de-annualized over the 60-day term on a 360-day basis.

$$\text{purchase price} = \frac{25{,}000{,}000}{1.02} = \$24{,}509{,}804$$

$$\text{repurchase price} = 24{,}509{,}804 \times \left(1 + 0.036 \times \frac{60}{360}\right) = 24{,}509{,}804 \times 1.006 = \$24{,}656{,}863$$

Repo interest $= 24{,}656{,}863 - 24{,}509{,}804 = \$147{,}059$. Haircut $= 1 - 1/1.02 = 1.96\%$.

Why the other options are wrong

- **B.** $24,647,000 treats the 2% margin as a straight 2% deduction ($25{,}000{,}000 \times 0.98$) instead of dividing by 1.02, then adds interest. The haircut is $1 - 1/1.02 = 1.96\%$.
- **C.** $24,509,804 is the purchase price (the amount borrowed today). It omits the repo interest that must be paid on the repurchase date.

Key takeaway The loan equals the collateral value divided by the initial margin. The repurchase price equals the loan times $(1 + \text{repo rate} \times \text{days}/360)$.

Reading 54: Fixed-Income Markets for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/commercial-paper/

Question 15 **Answer: C**

For investment-grade bonds, yields are driven mostly by benchmark (sovereign) rates, so the credit spread is a small part of the yield. For high-yield bonds the credit spread is a much larger part of the yield. The bond whose spread is almost half its yield is the high-yield bond.

Why the other options are wrong

- **A.** A government bond is the benchmark itself, so its credit spread share would be close to zero, the smallest of the three.
- **B.** Investment-grade yields are largely tied to benchmark rates, so their spreads are a small share of yield, like Bond P or Bond Q.

Key takeaway The larger the credit spread's share of the yield, the lower the credit quality.

Reading 54: Fixed-Income Markets for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/commercial-paper/

Question 16 **Answer: C**

Grouping bonds as developed market or emerging market bonds classifies them by the issuer's geography. The label emerging market bonds belongs to this approach.

Why the other options are wrong

- **A.** Supranational bonds are a category of issuer: international institutions owned by several governments. The label is not geographic.
- **B.** Municipal bonds are grouped by type of issuer (local governments), and sometimes by tax status.

Key takeaway Geographic labels are developed market and emerging market. Issuer-type labels are sovereign, municipal, agency, supranational and corporate.

Reading 55: Fixed-Income Markets for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/treasury-bonds/

credguild.com

Question 17 **Answer: B**

Primary dealers act as counterparties when the central bank buys or sells government securities to carry out monetary policy. When the central bank buys securities, it pays cash into the banking system, which adds reserves and is expansionary.

Why the other options are wrong

- **A.** Selling government bonds drains reserves from the banking system. That is contractionary.
- **C.** Government spending and taxation are fiscal policy. The government sets them, and they are not executed through the central bank's primary dealers.

Key takeaway A central bank purchase of securities is expansionary, and a sale is contractionary. Primary dealers are the central bank's counterparties. Fiscal policy is not a central bank tool.

Reading 55: Fixed-Income Markets for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/treasury-bonds/

Question 18 **Answer: B**

Government bonds trade mainly in OTC dealer markets, and trading is most active, with the most informative prices, in the most recently issued (on-the-run) bond of each maturity. Their yields are therefore used as the default-risk-free benchmark yields for building yield curves.

Why the other options are wrong

- **A.** Older (seasoned) issues trade less actively, so their prices are less informative for benchmark purposes.
- **C.** Supranational bonds are high quality but are not the sovereign default-risk-free benchmark. Benchmark curves are built from the sovereign's own on-the-run issues.

Key takeaway Benchmark (risk-free) yield curves are built from on-the-run government bonds.

Reading 55: Fixed-Income Markets for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/treasury-bonds/

Question 19 **Answer: A**

Only the remaining 20 years (40 semiannual periods) of cash flows matter. Because the 5.5% coupon exceeds the 5.2% yield, the bond trades at a premium.

Remaining maturity $= 25 - 5 = 20$ years, so $N = 40$; $PMT = 5.5/2 = 2.75$; periodic yield $= 5.2\%/2 = 2.6\%$.

$$P = \sum_{t=1}^{40} \frac{2.75}{1.026^{t}} + \frac{100}{1.026^{40}} = 103.70$$

BA II Plus (P/Y = C/Y = 1, END mode; clear with `[2ND] [CLR TVM]`): `N = 40; I/Y = 2.6; PMT = 2.75; FV = 100; CPT PV = -103.70`.

Why the other options are wrong

- **B.** 102.32 uses $N = 20$, the number of remaining years, as the number of semiannual periods. It should be 40.
- **C.** 96.39 swaps the coupon and the yield (a 5.2% coupon discounted at 2.75% per half-year). This produces a discount price for what is actually a premium bond.

Key takeaway Count the remaining maturity from today and convert it to periods. The issue date does not matter.

Reading 56: Fixed-Income Bond Valuation: Prices and Yields. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-to-maturity/

Question 20 **Answer: A**

Accrued interest is the seller's share of the next coupon: the coupon times the fraction of the coupon period from the previous coupon date to the settlement date. The buyer pays it to the seller as part of the full price because the buyer will receive the whole next coupon.

$$AI = \frac{t}{T} \times PMT$$

where t = days from the last coupon to settlement and T = days in the coupon period.

Why the other options are wrong

- **B.** The part of the next coupon that the seller has not earned belongs to the buyer. Accrued interest is the part the seller has earned.
- **C.** Accrued interest is not a separate cash flow that gets discounted. The full price is the PV on the last coupon date compounded forward to settlement, and accrued interest is then subtracted from it to get the flat price.

Key takeaway Accrued interest = seller's earned share of the current coupon; full price = flat price + AI.

Reading 56: Fixed-Income Bond Valuation: Prices and Yields. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-to-maturity/

Question 21 **Answer: A**

Other things equal, a longer maturity means more of the bond's value comes from distant cash flows, so its price reacts more to a given change in yield. Low-coupon bonds are also more sensitive than high-coupon bonds.

Sensitivity summary for option-free bonds:

- A longer maturity makes the price more sensitive.
- A lower coupon makes the price more sensitive.
- Because of convexity, the price gain from a yield decrease exceeds the price loss from an equal yield increase.

Why the other options are wrong

- **B.** Because the price-yield relationship is convex, prices are more sensitive to yield decreases than to equal yield increases: a bond's price sensitivity rises as yields fall.
- **C.** The relationship runs the other way. The low-coupon bond is the more sensitive one, because a larger share of its value comes from the principal paid at maturity.

Key takeaway Long maturity and low coupon = high price sensitivity; convexity favors yield decreases.

Reading 56: Fixed-Income Bond Valuation: Prices and Yields. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-to-maturity/

credguild.com

Question 22 **Answer: C**

Matrix pricing interpolates linearly between the yields of comparable traded bonds with the same rating. The 7-year maturity is two-fifths of the way from 5 to 10 years.

$$YTM_7 = 4.10\% + \frac{7-5}{10-5}(5.60\% - 4.10\%) = 4.10\% + 0.4 \times 1.50\% = 4.70\%$$

Why the other options are wrong

- **A.** 5.00% applies the two-fifths weight from the wrong end ($5.60\% - 0.4 \times 1.50\%$).
- **B.** 4.85% is the simple average of the two yields. That would be right only if 7 years were the midpoint between 5 and 10 years.

Key takeaway Interpolate in proportion to the distance from the shorter maturity.

Reading 56: Fixed-Income Bond Valuation: Prices and Yields. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-to-maturity/

Question 23 **Answer: A**

The yield to maturity is the single discount rate that sets the present value of all of a bond's cash flows equal to its price. It is the bond's internal rate of return.

Why the other options are wrong

- **B.** Current yield is the annual coupon divided by the price; it does not discount any cash flows.
- **C.** Simple yield adds straight-line amortization of a discount (or subtracts that of a premium) to the coupon and divides by the price; it is not a discount rate.

Key takeaway YTM = IRR of the bond's cash flows at the market price.

Reading 57: Yield and Yield Spread Measures for Fixed-Rate Bonds. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-spread/

Question 24 **Answer: C**

Current yield is the annual cash coupon divided by the bond's price. It considers only coupon income.

Annual coupon $= 0.09 \times 1{,}000 = 90$

$$CY = \frac{90}{962} = 9.36\%$$

Why the other options are wrong

- **A.** 8.66% multiplies the coupon by the price as a fraction of par ($90 \times 0.962/1{,}000$) instead of dividing the coupon by the price.
- **B.** 9.00% is the coupon rate, which divides the coupon by par rather than by the market price.

Key takeaway A bond priced below par has a current yield above its coupon rate.

Reading 57: Yield and Yield Spread Measures for Fixed-Rate Bonds. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-spread/

Question 25 **Answer: C**

A yield based on the scheduled coupon dates follows the street convention; a yield based on the actual payment dates, after moving payments past weekends and holidays, is the true yield. Because some cash arrives later, the true yield is usually slightly lower (by a few basis points) than the street convention yield.

Why the other options are wrong

- **A.** The label is correct, but delaying cash flows lowers the yield on a given price.
- **B.** The street convention yield is the first figure, based on scheduled dates; the figure based on actual payment dates is the true yield.

Key takeaway Street convention = scheduled dates; true yield = actual payment dates, usually a little lower.

Reading 57: Yield and Yield Spread Measures for Fixed-Rate Bonds. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-spread/

Question 26 **Answer: B**

A callable bond has a yield to call for every possible call date as well as a yield to maturity. The yield to worst is the lowest of all these yields. It is the most conservative return the investor can expect if the issuer acts in its own interest.

Why the other options are wrong

- **A.** The yield to worst is not a default measure; all the yields compared assume that every promised payment is made.
- **C.** The yield to worst is chosen among yields computed at the current price for each possible redemption date. Historical prices play no part.

Key takeaway Yield to worst = min(YTM, YTC at each call date).

Reading 57: Yield and Yield Spread Measures for Fixed-Rate Bonds. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-spread/

Question 27 **Answer: C**

For a callable bond, part of the Z-spread is extra yield that compensates the investor for the issuer's call option. The OAS removes that option component, so $\text{OAS} = \text{Z-spread} - \text{option value}$, which is below 160 bp when the option has value.

Why the other options are wrong

- **A.** An OAS above the Z-spread would require an option that benefits the investor (for example, a put). A call held by the issuer works the other way.
- **B.** The OAS equals the Z-spread only for an option-free bond or an option with zero value.

Key takeaway Callable bond: $\text{OAS} < \text{Z-spread}$; the gap is the option value.

Reading 57: Yield and Yield Spread Measures for Fixed-Rate Bonds. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-spread/

Question 28 **Answer: A**

Coupons are projected at MRR + QM and discounted at MRR + DM. The QM (110 bp) exceeds the DM (70 bp), so the note is worth more than par.

Coupon rate $= 4.20\% + 1.10\% = 5.30\%$, so the annual coupon $= 0.053 \times \$5{,}000{,}000 = \$265{,}000$.

Discount rate $= 4.20\% + 0.70\% = 4.90\%$.

$$V = \sum_{t=1}^{4} \frac{265{,}000}{1.049^{t}} + \frac{5{,}000{,}000}{1.049^{4}} = \$5{,}071{,}084$$

TI BA II Plus (P/Y = C/Y = 1, END mode): N = 4, I/Y = 4.90, PMT = 265,000, FV = 5,000,000, CPT PV = −5,071,084.

Why the other options are wrong

- **B.** $5,000,000 assumes the FRN must trade at par on a reset date. That holds only when the quoted margin equals the discount margin; here QM > DM.
- **C.** $4,929,572 swaps the two margins: coupons at 4.20% + 0.70% = 4.90% discounted at 4.20% + 1.10% = 5.30%, which produces a discount price.

Key takeaway Coupons come from the QM and the discount rate from the DM. If QM > DM the note trades at a premium; if QM < DM, at a discount.

Reading 58: Yield and Yield Spread Measures for Floating-Rate Instruments. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-and-yield-spread-measures-for-floating-rate-instruments/

Question 29 **Answer: B**

A CD is an add-on instrument: the investor deposits the full amount and receives it back with interest. The BEY annualizes the add-on return for the 91 days using a 365-day year, without compounding.

$$HPY = \frac{1{,}006.50}{1{,}000} - 1 = 0.65\%$$

$$BEY = 0.65\% \times \frac{365}{91} = 2.607\%$$

Why the other options are wrong

- **A.** 2.57% annualizes the 0.65% return on a 360-day year ($0.65\% \times 360/91$); a BEY uses 365 days.
- **C.** 2.63% compounds the period return into an effective annual yield ($1.0065^{365/91} - 1$). The BEY is a simple annualization with no compounding.

Key takeaway The BEY is a simple add-on annualization on a 365-day year, with no compounding and no 360-day year.

Reading 58: Yield and Yield Spread Measures for Floating-Rate Instruments. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-and-yield-spread-measures-for-floating-rate-instruments/

Question 30 **Answer: B**

The quoted margin (QM) is the fixed spread, set in the indenture, that is combined with the MRR to determine each coupon (it can be positive or negative). The discount (required) margin (DM) is the spread over the MRR at which the note would be priced at par on a reset date. Because the QM was fixed at issuance for the credit risk investors saw then, a DM below the QM means investors now demand less compensation, most likely because the issuer's credit quality has improved. With QM > DM, the note trades at a premium.

Why the other options are wrong

- **A.** A change in the reference rate flows into both the coupon (MRR + QM) and the required return (MRR + DM), so it does not open a gap between the two margins.
- **C.** When the discount margin is below the quoted margin, the coupon exceeds the required return and the note trades above par.

Key takeaway DM below QM points to improved credit and a premium price; DM above QM points to deteriorated credit and a discount.

Reading 58: Yield and Yield Spread Measures for Floating-Rate Instruments. Notes: credguild.com/cfa/level-1/notes/fixed-income/yield-and-yield-spread-measures-for-floating-rate-instruments/

Question 31 **Answer: C**

A zero-coupon bond pays no coupons: at a positive yield it is bought below par and pays par at maturity, so its entire return is price appreciation and there is no uncertainty about reinvesting coupons. Its yield to maturity is the spot rate for its maturity.

Why the other options are wrong

- **A.** The YTM of a zero-coupon bond *is* the spot rate for that maturity, so the 4-year spot rate is 5.2%; it is not divided by the number of years.
- **B.** Spot rates generally differ across maturities, and that variation is what the spot curve shows. Only in a flat environment are they all equal.

Key takeaway Zero-coupon bond: YTM = spot rate; at a positive yield the whole return is the price rising toward par; no reinvestment risk.

Reading 59: The Term Structure of Interest Rates: Spot, Par, and Forward Curves. Notes: credguild.com/cfa/level-1/notes/fixed-income/the-term-structure-of-interest-rates-spot-par-and-forward-curves/

Question 32 **Answer: A**

The arbitrage-free approach uses multiple discount rates: the spot rate for each cash-flow date, taken from the current term structure. Pricing this way leaves no profit from stripping the bond into zero-coupon pieces or rebuilding it from them.

Why the other options are wrong

- **B.** A geometric average of spot rates is still one rate for every cash flow; it does not apply the correct rate to each date.
- **C.** One discount rate for all cash flows is the yield-to-maturity approach, which is not how arbitrage-free values are derived.

Key takeaway Arbitrage-free valuation uses one spot rate per cash-flow date.

Reading 59: The Term Structure of Interest Rates: Spot, Par, and Forward Curves. Notes: credguild.com/cfa/level-1/notes/fixed-income/the-term-structure-of-interest-rates-spot-par-and-forward-curves/

Question 33 **Answer: B**

The par rate is the coupon that makes the spot-rate value of the bond equal to 100. It is a weighted average of the spot rates, dominated by the 3-year rate, so in an upward-sloping environment it lies just below the 3-year spot rate.

Discount factors: $d_1 = 1/1.021 = 0.97943$, $d_2 = 1/1.029^2 = 0.94443$, $d_3 = 1/1.036^3 = 0.89933$.

$$c = \frac{100\,(1 - d_3)}{d_1 + d_2 + d_3} = \frac{100 \times 0.10067}{2.82319} = 3.566\% \approx 3.57\%$$

Check with the middle choice: $3.57/1.021 + 3.57/1.029^2 + 103.57/1.036^3 = 100.01 \approx 100$.

Why the other options are wrong

- **A.** 2.87% is the simple average of the three spot rates; the par rate gives far more weight to the year-3 cash flow.
- **C.** 3.60% is the 3-year spot rate. A bond with a 3.60% coupon would price slightly above par (about 100.10), because its first two coupons are discounted at spot rates below 3.6%.

Key takeaway In a normal (upward-sloping) curve, par rates sit just below spot rates. Plugging in the middle answer choice is a fast exam check.

Reading 59: The Term Structure of Interest Rates: Spot, Par, and Forward Curves. Notes: credguild.com/cfa/level-1/notes/fixed-income/the-term-structure-of-interest-rates-spot-par-and-forward-curves/

Question 34 **Answer: B**

A 3-year zero-coupon bond has one cash flow at year 3, so it is discounted at the 3-year spot rate, which is the geometric mean of the 1-year spot and the two forward rates. Equivalently, divide 100 by the product of the three growth factors.

$$P = \frac{100}{(1.028)(1.046)(1.062)} = \frac{100}{1.14195} = 87.57$$

Equivalently, $S_3 = 1.14195^{1/3} - 1 = 4.524\%$; TI BA II Plus (P/Y = C/Y = 1): N = 3, I/Y = 4.524, PMT = 0, FV = 100, CPT PV = −87.57.

Why the other options are wrong

- **A.** 92.05 discounts for three years at the 1-year spot rate of 2.8%, ignoring the higher forward rates for years 2 and 3.
- **C.** 83.49 discounts for three years at the 2y1y rate of 6.2%, as if the last year's rate applied to every year.

Key takeaway To discount a year-N cash flow with forward rates, divide by the product of all one-period factors up to year N.

Reading 59: The Term Structure of Interest Rates: Spot, Par, and Forward Curves. Notes: credguild.com/cfa/level-1/notes/fixed-income/the-term-structure-of-interest-rates-spot-par-and-forward-curves/

Question 35 **Answer: A**

The chart shows a downward-sloping (inverted) environment. When forward rates decline with maturity, spot rates (geometric means of the forwards) decline more slowly, and par rates (weighted averages of spot rates) lie close to but slightly above the spot rates. The highest curve, X, is therefore the par curve; Y is the spot curve and Z the forward curve.

Why the other options are wrong

- **B.** The spot curve is Y: it lies just below the par curve in an inverted environment and above the forward curve.

- **C.** The forward curve is Z, the lowest and steepest curve: falling forward rates are what pull the spot and par curves down.

Key takeaway Normal curve: forward > spot > par. Inverted curve: forward < spot < par. Flat: all equal.

Reading 59: The Term Structure of Interest Rates: Spot, Par, and Forward Curves. Notes: credguild.com/cfa/level-1/notes/fixed-income/the-term-structure-of-interest-rates-spot-par-and-forward-curves/

Question 36 Answer: A

A fixed-rate bond has three sources of return: coupon and principal payments, reinvestment income on the coupons, and any capital gain or loss if it is sold before maturity. The manager's description covers the coupons and the price/principal difference but omits the interest earned by reinvesting coupons over the horizon.

Why the other options are wrong

- **B.** The description omits reinvestment income, which can be a large part of the return on a long-horizon, high-coupon bond.
- **C.** It is true that a bond held to maturity has no capital gain or loss, but that is not what is wrong with the description. It already allows for the bond to mature at par.

Key takeaway Three sources of bond return: coupons and principal, reinvestment income, and capital gain or loss on a sale before maturity.

Reading 60: Interest Rate Risk and Return. Notes: credguild.com/cfa/level-1/notes/fixed-income/interest-rate-risk-and-return/

Question 37 Answer: A

A capital gain or loss is measured against the carrying value, which is the price the bond would have at the sale date if its yield had stayed at the 5.2% purchase YTM. The sale price of 92.10 is above that carrying value, so Volkov has a capital gain.

Carrying value after 4 years (11 years = 22 half-years left, at the purchase YTM; P/Y = C/Y = 1, END): N = 22, I/Y = 2.6, PMT = 2, FV = 100, CPT PV = −90.043.

$$\text{Capital gain} = 92.10 - 90.043 = 2.06 \text{ per } 100 \text{ of par}$$

For reference, the purchase price was 87.608 (N = 30, I/Y = 2.6, PMT = 2, FV = 100).

Why the other options are wrong

- **B.** 4.49 compares the sale price with the purchase price ($92.10 - 87.608$). Part of that rise ($90.043 - 87.608 = 2.435$) is the normal accretion of the discount along the constant-yield path, which is interest income.
- **C.** A loss of 7.90 compares the sale price with par ($92.10 - 100$). Par is relevant only at maturity.

Key takeaway Carrying value is the PV of the remaining cash flows at the original YTM, and the capital gain is sale price minus carrying value.

Reading 60: Interest Rate Risk and Return. Notes: credguild.com/cfa/level-1/notes/fixed-income/interest-rate-risk-and-return/

Question 38 **Answer: C**

When a bond's Macaulay duration equals the investor's horizon, a change in yield moves reinvestment income and the sale price by roughly equal and opposite amounts. Setting the portfolio's Macaulay duration at eight years makes the duration gap zero, so the two risks balance.

Why the other options are wrong

- **A.** Modified duration is Macaulay duration divided by (1 + periodic yield); it measures percentage price sensitivity.
- **B.** Effective duration measures price sensitivity to shifts in a benchmark curve (used for bonds with embedded options); it is not the horizon-matching measure.

Key takeaway Match Macaulay duration to the investment horizon to balance price risk and reinvestment risk.

Reading 60: Interest Rate Risk and Return. Notes: credguild.com/cfa/level-1/notes/fixed-income/interest-rate-risk-and-return/

Question 39 **Answer: B**

Macaulay duration is the weighted average time (here 3.46 years) until the bond's cash flows are received, using the present value of each cash flow as a share of the bond's price as the weight. It is shorter than the 4-year maturity because coupons arrive before the final payment.

Why the other options are wrong

- **A.** Duration measures in general describe price sensitivity, but that is the interpretation of modified duration (percentage price change per 1% change in yield).
- **C.** The principal is repaid at maturity, in four years. The 3.46 figure is an average time across all cash flows.

Key takeaway Macaulay duration is expressed in years: the PV-weighted average time to receipt of the cash flows.

Reading 60: Interest Rate Risk and Return. Notes: credguild.com/cfa/level-1/notes/fixed-income/interest-rate-risk-and-return/

Question 40 **Answer: C**

Modified duration is Macaulay duration divided by one plus the bond's periodic yield. The YTM must first be found from the price; for an annual-pay bond the periodic yield is the YTM itself.

YTM (P/Y = C/Y = 1, END): N = 7, PV = −944.18, PMT = 50, FV = 1,000, CPT I/Y = 6.00.

$$\text{ModDur} = \frac{6.0444}{1.06} = 5.702$$

Why the other options are wrong

- **A.** 5.868 divides by $1 + 0.06/2 = 1.03$, a semiannual adjustment; this bond pays annually.
- **B.** 5.757 divides by one plus the coupon rate (1.05) instead of one plus the YTM (1.06).

Key takeaway ModDur divides by one plus the periodic yield (the coupon rate plays no part), and the periodic yield matches the payment frequency.

Reading 61: Yield-Based Bond Duration Measures and Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/macaulay-duration/

Question 41 **Answer: A**

Duration is a linear (tangent-line) approximation, but the price-yield curve of an option-free bond is convex. For a large fall in yield the actual price rises more than the straight line predicts, so a duration-only estimate understates the gain; for a large rise in yield it overstates the loss.

Why the other options are wrong

- **B.** The curve lies above the tangent line, so the actual increase is larger than the estimate.
- **C.** Duration captures only the slope of the price-yield curve. It misses the curvature (convexity). For a large 150 bp change the error is noticeable.

Key takeaway Duration alone: underestimates price increases and overestimates price decreases for large yield changes.

Reading 61: Yield-Based Bond Duration Measures and Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/macaulay-duration/

Question 42 **Answer: C**

Money duration is modified duration times the full value of the position. Multiplying it by the yield change (as a decimal) estimates the currency change in value, and a rise in yield lowers the value.

Full value $= 0.9875 \times \$6{,}000{,}000 = \$5{,}925{,}000$.

$$\text{Money duration} = 5.4 \times 5{,}925{,}000 = \$31{,}995{,}000$$

$$\Delta V \approx -31{,}995{,}000 \times 0.0015 = -\$47{,}992.50 \approx -\$47{,}993$$

Link to PVBP: $31{,}995{,}000 \times 0.0001 = \$3{,}199.50$ per basis point, and $15 \times 3{,}199.50 = \$47{,}992.50$.

Why the other options are wrong

- **A.** −$479,925 enters 15 bp as 0.015 instead of 0.0015.
- **B.** −$48,600 applies modified duration to the $6 million par value instead of the $5,925,000 full value.

Key takeaway $\Delta V \approx -\text{money duration} \times \Delta\text{YTM}$; $\text{PVBP} \approx \text{money duration} \times 0.0001$.

Reading 61: Yield-Based Bond Duration Measures and Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/macaulay-duration/

Question 43 **Answer: C**

Other things equal, a higher yield lowers duration. The price-yield curve is convex and flatter at higher yields, so the same yield change produces a smaller percentage price change. This holds whether the bond trades at a premium or a discount.

Why the other options are wrong

- **A.** Duration increases when yields fall. A rise in yields shortens it.
- **B.** Modified duration depends on the yield level through both the PV weights and the $1 + \text{YTM}$ divisor, so it changes when yields change.

Key takeaway For option-free bonds, a higher yield lowers duration and a lower yield raises it.

Reading 61: Yield-Based Bond Duration Measures and Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/macaulay-duration/

Question 44 **Answer: A**

Because the coupon is reset to the market reference rate each period, a floating-rate note's price returns to about par at each reset date. Its Macaulay duration is therefore approximately the time until the next reset rather than its maturity.

Time to next reset $= 6 - 2 = 4$ months $= 4/12 = 0.33$ years.

Why the other options are wrong

- **B.** 0.50 years is the full reset period; two of the six months have already passed.
- **C.** 6.00 years is the final maturity. The resets protect the price from rate changes, so the maturity overstates the note's duration.

Key takeaway An FRN's duration is approximately the time to the next coupon reset date.

Reading 61: Yield-Based Bond Duration Measures and Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/macaulay-duration/

Question 45 **Answer: A**

Convexity is the present-value-weighted average of each cash flow's convexity, $t(t+1)/(1+r)^2$, using the periodic yield. For a semiannual bond the result is in half-years squared and must be divided by $2^2 = 4$ to annualize.

Periodic yield $r = 3\%$; cash flows 4, 4, 104.

PVs: $4/1.03 = 3.8835$; $4/1.03^2 = 3.7704$; $104/1.03^3 = 95.1747$; price $= 102.8286$.

Weights: 0.0378, 0.0367, 0.9256. Cash-flow convexities: $1 \times 2/1.03^2 = 1.8852$; $2 \times 3/1.03^2 = 5.6556$; $3 \times 4/1.03^2 = 11.3112$.

Periodic convexity $= 0.0378(1.8852) + 0.0367(5.6556) + 0.9256(11.3112) \approx 10.748$; annualized $= 10.748/4 \approx 2.69$.

Why the other options are wrong

- **B.** 5.37 divides by the periodicity (2) instead of the periodicity squared (4).
- **C.** 10.75 is the convexity in semiannual periods, before annualizing.

Key takeaway Annualize convexity by dividing by periodicity squared (4 for semiannual).

Reading 62: Yield-Based Bond Convexity and Portfolio Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-convexity/

Question 46 **Answer: B**

Convexity is increased by the same features that increase duration: a longer maturity and a lower coupon rate (and a lower yield, which is equal here). The 25-year, 2% coupon bond combines the longest maturity with the lowest coupon, so it has the most convexity.

Why the other options are wrong

- **A.** This bond has both the shorter maturity and the higher coupon, so it has the least convexity of the three.

- **C.** The low coupon raises convexity relative to the 7% bond, but with a 10-year maturity it is less convex than the 25-year bond with the same coupon.

Key takeaway A longer maturity, a lower coupon and a lower yield all raise convexity. For equal duration, more dispersed cash flows give more convexity.

Reading 62: Yield-Based Bond Convexity and Portfolio Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-convexity/

Question 47 **Answer: A**

With positive convexity the price-yield curve is steeper at lower yields, so an equal-sized decline in yield produces a larger price gain than the price loss produced by an equal-sized rise in yield.

Why the other options are wrong

- **B.** Bond prices and yields move in opposite directions; convexity does not change that.
- **C.** Convexity describes the asymmetry between price gains and losses. It does not compare the rate of price change with the rate of yield change.

Key takeaway Positive convexity means bigger gains than losses for equal yield moves.

Reading 62: Yield-Based Bond Convexity and Portfolio Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-convexity/

Question 48 **Answer: A**

Portfolio duration is the average of the bonds' durations weighted by each bond's market value (price per 100 of par times par, divided by 100) as a proportion of the portfolio's total market value.

Market values: $1{,}000{,}000 \times 1.12 = 1{,}120{,}000$; $1{,}200{,}000 \times 0.86 = 1{,}032{,}000$; $800{,}000 \times 1.01 = 808{,}000$. Total $= 2{,}960{,}000$.

$$D_p = \frac{1{,}120{,}000(3.1) + 1{,}032{,}000(10.8) + 808{,}000(6.0)}{2{,}960{,}000} = \frac{19{,}465{,}600}{2{,}960{,}000} \approx 6.58$$

Why the other options are wrong

- **B.** 6.63 is the simple (equal-weighted) average $(3.1 + 10.8 + 6.0)/3$, which ignores the bonds' different market values.
- **C.** 6.95 weights the durations by par value ($1.0, 1.2, 0.8$ out of 3.0 million) instead of market value; the discount bond is overweighted.

Key takeaway Weight each bond by its market value. Par-value and equal weights give the wrong answer.

Reading 62: Yield-Based Bond Convexity and Portfolio Properties. Notes: credguild.com/cfa/level-1/notes/fixed-income/bond-convexity/

Question 49 **Answer: B**

Effective duration uses model values that reflect how an embedded option changes expected cash flows as rates move; modified duration ignores that effect. For option-free bonds the two measures are similar. Both, however, assume a parallel shift in the curve.

Why the other options are wrong

- **A.** Neither effective nor modified duration handles nonparallel shifts; key rate durations do.
- **C.** A long maturity and low coupon raise duration and convexity, but for an option-free bond modified duration is still appropriate.

Key takeaway Effective duration matters when cash flows depend on rates (embedded options).

Reading 63: Curve-Based and Empirical Fixed-Income Risk Measures. Notes: credguild.com/cfa/level-1/notes/fixed-income/curve-based-and-empirical-fixed-income-risk-measures/

Question 50 **Answer: A**

The estimated change is the duration effect plus the convexity effect.

$$\%\Delta P \approx -6.72(-0.0065) + \tfrac{1}{2}(55.30)(-0.0065)^2 = 0.043680 + 0.001168 = 0.044848 \approx 4.48\%$$

Why the other options are wrong

- **B.** 4.37% is the duration effect alone.
- **C.** 4.25% subtracts the convexity effect.

Key takeaway Square the decimal yield change: $(0.0065)^2 = 0.00004225$.

Reading 63: Curve-Based and Empirical Fixed-Income Risk Measures. Notes: credguild.com/cfa/level-1/notes/fixed-income/curve-based-and-empirical-fixed-income-risk-measures/

Question 51 **Answer: C**

A key rate (partial) duration tells how much the value of a bond or portfolio moves when the benchmark rate at just one maturity changes and every other rate stays put. Summed across maturities, key rate durations equal the effective duration.

Why the other options are wrong

- **A.** Sensitivity to a parallel shift of the whole curve is measured by effective duration.
- **B.** Key rate duration is a rate sensitivity. It does not measure changes in a bond's cash flows.

Key takeaway Key rate duration covers one point on the curve; effective duration covers the whole curve moving in parallel.

Reading 63: Curve-Based and Empirical Fixed-Income Risk Measures. Notes: credguild.com/cfa/level-1/notes/fixed-income/curve-based-and-empirical-fixed-income-risk-measures/

Question 52 **Answer: C**

Empirical duration is a statistical estimate: it measures how bond prices have actually moved in the past when benchmark yields changed. It is useful for credit-risky portfolios, whose spreads may move with benchmark yields.

Why the other options are wrong

- **A.** Modified duration is calculated mathematically from the bond's cash flows and yield. It does not use historical data.
- **B.** Analytical durations (Macaulay, modified, effective) come from mathematical analysis of cash flows rather than from historical price data.

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Key takeaway A duration estimated from historical data (for example, by regression) is empirical; a formula-based duration is analytical.

Reading 63: Curve-Based and Empirical Fixed-Income Risk Measures. Notes: credguild.com/cfa/level-1/notes/fixed-income/curve-based-and-empirical-fixed-income-risk-measures/

Question 53 Answer: A

Capacity is the borrower's ability to make its debt payments on time. It is assessed with quantitative measures of profitability, coverage and leverage. A high EBIT margin, high interest coverage and low debt/EBITDA indicate strong capacity and a low probability of default.

Why the other options are wrong

- **B.** Collateral analysis looks at the value of the specific assets pledged as security rather than at the issuer's income and leverage ratios.
- **C.** Covenant analysis reviews the legal terms and conditions of the bond agreement.

Key takeaway Ratio analysis of profits, coverage and leverage assesses capacity; pledged assets are collateral; legal terms are covenants.

Reading 64: Credit Risk. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-risk/

Question 54 Answer: B

Credit ratings lag market pricing. Spreads and prices react to new information quickly, while agencies revise ratings more slowly, so an investor who waits for a rating change often trades after the price has already moved. Two further limitations are that some risks, such as litigation, natural disasters, acquisitions or debt-financed share buybacks, are hard to capture in a rating, and that agencies make mistakes. Investors should therefore do their own credit analysis as well.

Why the other options are wrong

- **A.** The statement is false. Agencies assign issuer credit ratings and issue credit ratings, and an issue can be notched above or below its issuer's rating.
- **C.** Comparing credit risk across issuers, industries and bond types is a use of credit ratings. It does not describe a limitation.

Key takeaway Uses of ratings: comparing credit risk, tracking credit migration risk and meeting regulatory or contractual rules. Limitations: ratings lag market prices, some risks are hard to rate, and agencies can be wrong.

Reading 64: Credit Risk. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-risk/

Question 55 Answer: A

In an economic expansion, profits rise and the probability of default falls, so corporate yield spreads narrow. Narrowing spreads mean corporate bond prices rise relative to government bond prices, so the manager should overweight corporates versus government bonds.

Why the other options are wrong

- **B.** This positioning profits when spreads widen, which is what happens when the economy weakens.
- **C.** Upgrading credit quality is a defensive move suited to an expected contraction; in a recovery the lower-rated bonds' spreads tend to narrow the most.

Key takeaway In an expansion spreads narrow, which favors credit (and lower quality); in a contraction spreads widen, which favors government and higher-quality bonds.

Reading 64: Credit Risk. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-risk/

Question 56 Answer: A

Duration and convexity estimate the price effect of a spread change exactly as they do for a yield change, with the spread change replacing the yield change. The convexity adjustment is positive, so it makes the price decline slightly smaller than the duration-only estimate.

$$\%\Delta P \approx -\text{ModDur} \times \Delta\text{Spread} + \tfrac{1}{2}\,\text{Convexity} \times (\Delta\text{Spread})^2$$

$$= -6.2(0.0060) + 0.5(52)(0.0060)^2 = -0.03720 + 0.000936 = -0.03626 \approx -3.63\%$$

Why the other options are wrong

- **B.** −3.72% is the duration-only estimate; it omits the positive convexity adjustment.
- **C.** −3.81% subtracts the convexity adjustment instead of adding it.

Key takeaway The convexity term $\frac{1}{2}\,\text{Convexity}\,(\Delta\text{Spread})^2$ is always added for an option-free bond.

Reading 64: Credit Risk. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-risk/

Question 57 Answer: C

Monetary effectiveness concerns the central bank's ability to vary the money supply and interest rates credibly to support stable growth. An independent central bank is less likely to print money to service government debt, which reduces the risk of high inflation and currency weakness.

Why the other options are wrong

- **A.** Fiscal flexibility is the government's ability to raise taxes or cut spending to keep up debt payments. That is a budget issue rather than a central bank issue.
- **B.** External status concerns the international standing of the currency (e.g., reserve currency status) and geopolitical risk.

Key takeaway Central bank credibility and independence belong to monetary effectiveness, room to tax or cut spending to fiscal flexibility, and reserve currency status to external status.

Reading 65: Credit Analysis for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-government-issuers/

Question 58 Answer: B

Fiscal strength is measured by a low debt burden (debt/GDP) and good debt affordability (low interest/revenue). Varnholm's debt is a smaller share of its GDP, but its interest bill absorbs a larger share of its revenue, so the two measures point in different directions.

$$\text{Debt burden: Kestria} = \frac{780}{1{,}200} = 65.0\%, \qquad \text{Varnholm} = \frac{290}{500} = 58.0\%$$

$$\text{Debt affordability: Kestria} = \frac{29.4}{420} = 7.0\%, \qquad \text{Varnholm} = \frac{13.05}{145} = 9.0\%$$

Varnholm has the lower debt burden; Kestria has the lower (better) interest-to-revenue ratio.

Why the other options are wrong

- **A.** Kestria's debt/GDP (65%) is higher than Varnholm's (58%), so Kestria does not have the lighter debt burden.
- **C.** Varnholm's interest/revenue (9.0%) is higher than Kestria's (7.0%), so its debt affordability is worse.

Key takeaway Lower ratios are better for both fiscal strength measures, and the two can disagree, so compute both.

Reading 65: Credit Analysis for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-government-issuers/

Question 59 **Answer: B**

Revenue bonds finance a specific project and are serviced from that project's revenues. The fare revenue of the light-rail line is the primary source of repayment. The national guarantee is extra credit support; it does not make the national government the issuer.

Why the other options are wrong

- **A.** General obligation bonds are backed by the full faith and credit, that is, the taxing power, of the issuing government. These bonds rely on the project's revenue instead.
- **C.** Sovereign bonds are issued by the national government itself and serviced mainly from its tax revenue. Here the issuer is a regional entity, and the national government only guarantees the debt.

Key takeaway Classify regional government debt by its primary source of repayment: tax base (GO bonds) or a single project's revenue (revenue bonds). A guarantee adds support but does not change the classification.

Reading 65: Credit Analysis for Government Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-government-issuers/

Question 60 **Answer: B**

Other things equal, companies have higher credit quality when they have strong operating profits and recurring revenues, low leverage, high coverage of debt service by income, and high liquidity to meet short-term debt payments. Higher liquidity means more cash and liquid assets to meet obligations that fall due soon.

Why the other options are wrong

- **A.** Higher leverage means greater reliance on debt in the capital structure, which points to lower credit quality.
- **C.** Lower coverage means income covers interest and principal payments less comfortably, which points to lower credit quality.

Key takeaway Signs of stronger corporate credit: strong, recurring profits; low leverage; high coverage; high liquidity.

Reading 66: Credit Analysis for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-corporate-issuers/

Question 61 **Answer: A**

Secured debt ranks ahead of unsecured debt, and a first mortgage, which pledges a specific property, sits at the top of the secured classes. Senior unsecured debt is the highest class of unsecured debt. Senior subordinated debt ranks below it, because all subordinated classes rank behind other unsecured debt. Recovery rates fall with each step down this ranking.

Why the other options are wrong

- **B.** This places unsecured debt ahead of secured debt. First mortgage bondholders have a claim on the pledged property and rank first.
- **C.** The word "senior" in senior subordinated notes gives them priority only over other subordinated classes. They still rank behind senior unsecured notes.

Key takeaway General ranking: first lien or first mortgage, senior secured (second lien), junior secured, senior unsecured, senior subordinated, subordinated, junior subordinated.

Reading 66: Credit Analysis for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-corporate-issuers/

Question 62 **Answer: A**

The issuer credit rating (the corporate family rating) reflects the borrower's overall creditworthiness and is typically based on its senior unsecured debt. Issue credit ratings apply to specific bonds and may be notched above or below the issuer rating depending on seniority and covenants.

Why the other options are wrong

- **B.** Notching can go either way: a secured issue with strong covenants may be rated above the issuer, a subordinated issue below it.
- **C.** The issuer rating (CFR) is the one typically based on senior unsecured debt. An issue rating reflects the seniority and covenants of one specific bond.

Key takeaway The CFR rates the issuer and is anchored on senior unsecured debt; an issue credit rating rates one specific bond and can be notched up or down.

Reading 66: Credit Analysis for Corporate Issuers. Notes: credguild.com/cfa/level-1/notes/fixed-income/credit-analysis-for-corporate-issuers/

Question 63 **Answer: B**

Securitization sells financial assets, not liabilities. Kestrel gives up $400 million of mortgage loans and receives $400 million of cash, so both of these asset lines change. The deposits that funded the loans stay on the balance sheet, because the SPE buys the loans and takes on none of the bank's obligations to its depositors. The bank benefits from the cash it can re-lend and from the lower capital it must hold once the loans are sold; removing deposits or other liabilities is not a benefit of securitization.

Effect of the sale on Kestrel's balance sheet:

- Mortgage loans: $-\$400$ million (sold to the SPE).
- Cash: $+\$400$ million (sale proceeds).
- Customer deposits and other liabilities: no change.

Why the other options are wrong

- **A.** The mortgages are the assets sold to the SPE, so this line falls by $400 million.
- **C.** The SPE pays $400 million for the mortgages, so cash rises by that amount until the bank re-lends it.

Key takeaway In a securitization the originator swaps loans for cash on the asset side; its deposits and other liabilities are not transferred.

Reading 67: Fixed-Income Securitization. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-securitization/

Question 64 Answer: B

The trust is a special purpose entity, legally separate from Brenlow. Because it is bankruptcy remote, Brenlow's creditors have no claim on the loan pool, and a decline in Brenlow's finances does not affect ABS holders' claim on the collateral. The ABS can therefore be rated on the pool (plus any credit enhancement) rather than on Brenlow's overall credit.

Why the other options are wrong

- **A.** ABS are not automatically investment grade; subordinated tranches can be rated well below investment grade.
- **C.** ABS holders have no claim in Brenlow's bankruptcy at all. Their claim is on the SPE's collateral only, so they are not ranked against Brenlow's bonds.

Key takeaway Bankruptcy remoteness of the SPE (plus credit tranching) can allow senior ABS to be rated above the originator.

Reading 67: Fixed-Income Securitization. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-securitization/

Question 65 Answer: B

In a securitization the credit risk of the collateral passes through to ABS investors: if borrowers in the pool default, investors bear the losses (after any credit enhancement). ABS investors also face uncertainty about the timing of cash flows, for example from prepayments.

Why the other options are wrong

- **A.** The SPE holds only the securitized pool, so the investor is not exposed to the bank's other loans.
- **C.** The SPE is bankruptcy remote, so the bank's creditors have no claim on the securitized collateral.

Key takeaway ABS investors swap exposure to the originator for exposure to the collateral pool itself.

Reading 67: Fixed-Income Securitization. Notes: credguild.com/cfa/level-1/notes/fixed-income/fixed-income-securitization/

Question 66 Answer: A

Covered bondholders have dual recourse: a claim on the cover pool and a claim on the issuing bank's other unencumbered assets. Ordinary ABS investors can look only to the collateral held by the SPE. The extra recourse, together with overcollateralization and loan-to-value limits, gives covered bonds higher credit quality and lower yields than comparable ABS.

Why the other options are wrong

- **B.** Because covered bonds are safer, investors accept lower yields than on comparable ABS.
- **C.** Dual recourse and a dynamic, overcollateralized cover pool give covered bonds higher credit quality than comparable ABS.

Key takeaway A covered bond has dual recourse, no SPE and a dynamic cover pool, which give it higher credit quality and a lower yield than comparable ABS.

Reading 68: Asset-Backed Security (ABS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/asset-backed-security-abs-instrument-and-market-features/

Question 67 **Answer: B**

During the lockout (revolving) period, ABS holders receive only interest and fees, and principal repaid by cardholders is used to buy new receivables so that the pool stays about the same size. An early (rapid) amortization provision ends this reinvestment and passes principal to investors sooner when that is needed to protect the credit quality of the securities, much like the acceleration of a loan when credit conditions worsen.

Why the other options are wrong

- **A.** Principal that cardholders repay during the lockout period is reinvested in new receivables, so faster repayment does not reach the ABS holders as principal. For the same reason, investors bear no prepayment risk during this period.
- **C.** A cap on the card rate limits the interest earned on the receivables. It can affect the interest available to investors, but it does not change when principal is repaid.

Key takeaway Credit card ABS: in the lockout (revolving) period investors get interest and fees only and principal is recycled into new receivables; in the amortization period principal is passed through; an early (rapid) amortization provision brings principal forward to protect credit quality.

Reading 68: Asset-Backed Security (ABS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/asset-backed-security-abs-instrument-and-market-features/

Question 68 **Answer: B**

Ordinary ABS rely on the cash flows from a static collateral pool. In a CDO, a collateral manager actively trades the pool's holdings to raise the cash required for the payments promised to CDO investors.

Why the other options are wrong

- **A.** Most ABS are also issued through a special purpose vehicle (SPV), so this does not distinguish a CDO.
- **C.** Senior/subordinated tranching is common to many ABS structures as well as CDOs.

Key takeaway The collateral manager is the defining feature of a CDO.

Reading 68: Asset-Backed Security (ABS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/asset-backed-security-abs-instrument-and-market-features/

Question 69 **Answer: C**

In a sequential-pay structure the first tranche receives all scheduled principal and prepayments first. If prepayments speed up, it is repaid sooner (more contraction risk); if they slow, it is still first in line, so it is well protected against extension, which falls mainly on the later tranche.

Why the other options are wrong

- **A.** This is the profile of the later tranche (Class K), which waits longest for principal.
- **B.** Time tranching reallocates prepayment risk: the short tranche gains extension protection in exchange for bearing more contraction risk, so it cannot have more of both.

Key takeaway First-pay tranche: contraction risk. Last-pay tranche: extension risk.

Reading 69: Mortgage-Backed Security (MBS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/mortgage-backed-security-mbs-instrument-and-market-features/

Question 70 **Answer: A**

The pool's weighted average coupon (WAC) weights each mortgage rate by its share of the pool's outstanding balance. Investors receive the pool's interest net of servicing and guarantee fees, so the pass-through rate is the WAC minus the fees.

Total balance $= 120 + 80 + 200 = 400$.

$$\text{WAC} = \frac{120(5.00\%) + 80(6.50\%) + 200(5.75\%)}{400} = \frac{600 + 520 + 1{,}150}{400}\% = 5.675\%$$

$$\text{Pass-through rate} = 5.675\% - 0.50\% = 5.175\% \approx 5.18\%$$

The remaining terms are not needed here. They would be used for the WAM, $= (120 \times 22 + 80 \times 15 + 200 \times 27)/400 = 23.1$ years.

Why the other options are wrong

- **B.** 5.25% subtracts the fees from a simple average of the three rates (5.75%) instead of the balance-weighted WAC.
- **C.** 5.68% is the WAC itself; it omits the 0.50% of fees deducted before investors are paid.

Key takeaway Weight by current balance, then deduct fees. The pass-through rate is always below the WAC when fees are charged.

Reading 69: Mortgage-Backed Security (MBS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/mortgage-backed-security-mbs-instrument-and-market-features/

Question 71 **Answer: A**

A higher debt service coverage ratio means the property's net operating income covers the required interest and principal by a wider margin. A lower loan-to-value ratio means the loan is smaller relative to the property's value, so the borrower has more equity and the lender recovers more in a default. Both indicate better credit quality.

Why the other options are wrong

- **B.** Both ratios point to weaker credit: thinner income coverage and more leverage.
- **C.** The higher DSC ratio is favorable, but a higher LTV ratio signals more leverage and higher default risk.

Key takeaway A higher DSCR and a lower LTV indicate stronger CMBS credit.

Reading 69: Mortgage-Backed Security (MBS) Instrument and Market Features. Notes: credguild.com/cfa/level-1/notes/fixed-income/mortgage-backed-security-mbs-instrument-and-market-features/

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