

Section 6.4 Additional Problems

1. You are given the following term structure of interest rates as effective annual rates.

| 1 year | 2 year | 3 year | 4 year |
|--------|--------|--------|--------|
| .025 | .03 | .035 | .05 |

Someone offers you a 2 year forward one year rate of 5.5%. Construct a transaction in which an arbitrage gain can be obtained.