**8.4 Assume the yield curve on "plain vanilla" default-free bonds is flat at 5%, and you are thinking of buying a default-free bond. Specifically, you're thinking of buying a bond issued by Risklessco, a company considered to be default-free by all major bond rating firms.  
  
You will select one of the following three bonds, all identical except for the special features listed:**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Face Value | Maturity | Coupon Rate (Paid Annually) | Yield to Maturity | Special Features | Price |
| A | 1000 | 20 years | 5.5% | 5% | None | ? |
| B | 1000 | 20 years | 5.5% | 5% | Callable | Par |
| C | 1000 | 20 years | 5.5% | 3.5% | Callable and Convertible into Risklessco Stock | ? |

1. **Why is the yield on bonds A and B 5%? Why is the yield on bond C different?**
2. **What would be the price of Bond A?**
3. **If bond C is considered identical to bond B except for the conversion privilege, what is the value of the conversion privilege? Does the conversion privilege benefit the issuer of the bond or the purchaser? Is this consistent with the price you calculated for bond C?**
4. **Who does the callability provision benefit, the issuer or the purchaser? Is this consistent with the price you calculated for bond A?**