

The one-month and two-month interest rates are 3.8% and 4.0%, respectively. Our model of the term structure says that one month from now the one-month interest rate will be either 3.3% or 4.3%. Compute the price of an interest rate derivative that pays \$1 in one month if the one-month interest rate is 4.3% and \$0.5 if the one-month interest rate is 3.3%. (**NOTE:** the interest rates quoted are the spot rates that have been annualized using compounding.)