

Pricing of Discounted Securities

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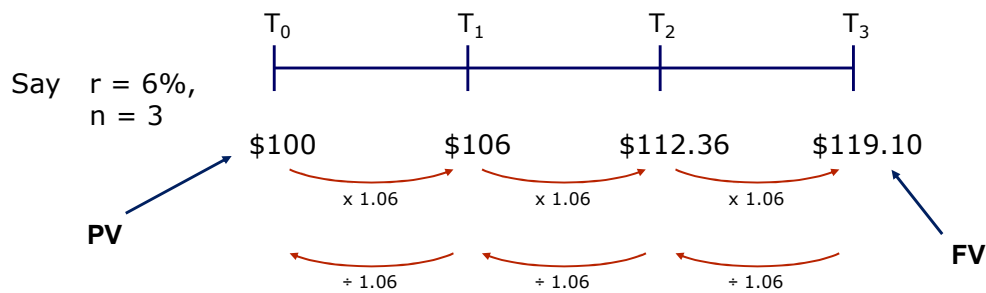
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Future and present values – compound interest

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In general:

$$FV = PV \times (1+r)^n$$

"Compounding"

$$PV = \frac{FV}{(1+r)^n}$$

"Discounting"

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Example

A 120-day banker's acceptance has a face value of HK\$100,000, with an annual interest rate of 9.00%. What is the fair price?

$$\begin{aligned} P &= \frac{100,000}{1 + \left[0.09 \times \frac{120}{365} \right]} \\ &= \frac{100,000}{1.029589} \\ &= \text{HK\$}97,126.13 \end{aligned}$$

Annotations in the original image:
- Red arrow pointing to 0.09: Annual interest rate
- Red arrow pointing to 120: Number of days to maturity
- Red arrow pointing to 365: Number of days in a year

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