Ralph's Bonds

At the end of year 0 Ralph issues a bond with a 3-year term, a $1,000 face value, and a 10% annual interest rate. Coupon payments are due at the end of years 1, 2, and 3.

Required:

1. What are the coupon payments on the bond each year?

2. How much would be raised from the issuance of the bond assuming a market interest rate of 10%?

3. In year 0 the market interest rate is 12%. How much is raised by the bond issuance? Record the journal entries in years 0-3 associated with Ralph's bond issuance. (Use the effective interest method for amortizing the bond discount.)

4. Prepare partial financial statements to reflect the bond issuance for the first period. Create a directed graph of these partial financial statements.

5. At the end of year 1 the market interest rate drops to 10% (immediately following the coupon payment). What is the market value of the bond at year 1 (after the drop in interest rate)? Record the journal entry associated with the decline in market rate.

6. At the end of year 1, Alice issues a $1,000 face value bond with a 2-year maturity and 10% annual interest rate. Coupon payments are due at the end of years 2 and 3. The market interest rate is still 10%. What amount does Alice raise from the bond issuance.

7. What is the book value of Ralph's bond at the end of year 1? What is the book value of Alice's bond at the end of year 1? If the bond values are different, why?