**Treasury Strips**

Bonds and Notes with maturity > 10 yrs. are eligible for stripping.

Stripping through the Treasury began in Feb. 1985

Reconstitution through the Treasury began in May 1987

Why strips?

1. No reinvestment risk
2. Higher duration – so greater interest rate risk.
3. Duration is always time to maturity, so less need to adjust portfolio
4. Maybe the investor doesn’t want all 60 cash flows in a 30-year bond. Instead, they just buy zeros for the CFs that they want. Customize the cash flows.

## Pricing Strips

Consider a strip maturing 11/15/20 with a BEY of 8.45%

You purchase it with a settlement date of 1/17/11

11/15/10 – 5/15/11 = 181 days in the current 6-month period

As of 1/17/11, there are 118 days left in the current period.

# So, we have 19.6519 periods till maturity because 118/181 = .6519

PV = FV = 100 . = 44.34 = Price of the strip

(1+r)t [1+(.0845/2)]19.6519

The price of strips must be monotonically decreasing as their time to maturity increases.

Given the price of a strip, you can solve for its yield the usual way.

PV = FV

(1+r)t

where PV = Price

FV = 100

t = # of semiannual periods left till maturity

r = semiannual yield

This will work on our spreadsheet: Bond Price and Yield Using Excel. Just input the Coupon Rate as 0.00%.