

Session 6: Post Class tests

1. You have been offered a legal settlement of a lawsuit, receiving a million dollars today, a million at the end of year 3 and a million at the end of 10 years. The first two cashflows are backed up by the government, and the last one is a private commitment. If the riskfree rate is 3% and the default risk in the private commitment would lead you to add an additional 2% to the riskfree rate, what is the present value of your settlement?
 - a. \$2.477 million
 - b. \$2.529 million
 - c. \$2.608 million
 - d. \$2.659 million
 - e. \$3.000 million
2. Faced with extreme circumstances, you have borrowed money from a money lender, who will be charging you 1% a week, for the next year. What annual interest rate are you paying on the loan?
 - a. 12.68%
 - b. 52.00%
 - c. 67.77%
 - d. 167.77%
 - e. None of the above
3. You are an agent for Ron Judge, a baseball player, who has been offered a 10-year contract, \$ 8 million a year for five years and \$12 million for the following five years, with payments due at the end of each year (with the first payment due one year from now). You have come up with a discount rate of 5% as appropriate given the risk in the cash flows. What is the value of this contract?
 - a. \$73.40 million
 - b. \$75.34 million
 - c. \$79.11 million
 - d. \$86.59 million
 - e. None of the above
4. You are an independent consultant and are valuing a contract that offers you \$2 million at the end of next year, growing 10% a year for the next 9 years (with the last payment at the end of the 10th years). What is the value of this contract, if your required return (discount rate) is 8%?
 - a. \$15.36 million
 - b. \$16.76 million
 - c. \$20.14 million
 - d. \$21.75 million
 - e. None of the above
5. In the perpetual growth model, which of the following is the most reasonable cap on the growth rate forever?
 - a. It should not be higher than the discount rate
 - b. It should not be higher than the nominal growth rate of the economy
 - c. It should not be higher than the real growth rate of the economy

- d. It should not be higher than the inflation rate
- e. It should not be higher than zero