**Question 1: (Interest Rates)**

a. Assume the following conditions prevail in the economy at this time:

Real rate of interest…………………..2%

Expected inflation rate……………….3%

Default risk premium………………...1%

Maturity risk premium……………….1%

Liquidity risk premium………………1%

Contractural provision risk premium...1%

Exchange rate risk premium………….1%

Tax risk premium…………………….1%

Market risk premium…………………1%

Given these conditions, what would you expect the yield on 3-Month U.S. Treasury Bills to be at this time?

b. What is a “yield curve?”

**Question 2: (Bonds)**

Recentlydealers were offering the US government’s 8.875% 2019 Treasury Bond for “147.23.” Answer the following questions about the bond:

a. What is the price in dollars of the bond?

b. What is the amount of the coupon interest payment you would receive each year if you bought the bond? (assume annual payments)

c. How many payments would you receive if you bought the bond and held it to maturity? (In other words, how many years does the bond have to go before it matures?)

d. What is the bond’s *Yield to Maturity*, or YTM, assuming you purchased it for the current offering price?

**Question 3: (Bonds)**

Hewitt Packing Company has an issue of $1,000 par value bonds with a 14 percent coupon interest rate outstanding. The issue pays interest semiannually and has 10 years remaining to its maturity date. Bonds of similar risk are currently selling to yield a 12 percent rate of return. What is the value of these Hewitt Packing Company bonds?

**Question 4 (Stocks)**

You are considering buying a stock with an expected dividend next year of $2, and a long-term growth rate of 10%. If your required rate of return is 14%, what price are you willing to pay for the stock?

**Question 5: (Capital Budgeting--NPV)**

Your firm is looking at a new investment opportunity, Project Alpha, with net cash flows as follows:

 ---- Net Cash Flows ----

 Project Alpha

 Initial Cost at T-0 (Now) ($10,000)

cash inflow at the end of year 1 6,000

cash inflow at the end of year 2 4,000

cash inflow at the end of year 3 2,000

a. Calculate the project's Net Present Value (NPV), assuming your required rate of return

 is 10%

b. On the basis of your analysis in part a, should the project be accepted or rejected?

**Question 6: (Capital Budgeting--NPV)**

What is the NPV of an project with an initial investment of $1,000 that provides after-tax operating cash flows of $300 per year for four years? Assume the firm's cost of capital is 15 percent.

**Question 7: (Capital Budgeting--IRR)**

What is the IRR for a project if its initial after tax cost is $5,000,000 and it is expected to provide after-tax operating cash inflows of $1,800,000 in year 1, $1,900,000 in year 2, $1,700,000 in year 3 and $1,300,000 in year 4?

**Question 8: (Working Capital and Current Assets)**

DP Dolls’ inventory has an average age of 80 days and its customers pay off their accounts receivable in 40 days. The company pays its suppliers after 30 days. Given these conditions, what is the length of the company’s Cash Conversion Cycle?

**Question 9: (Working Capital and Current Assets)**

DP Dolls is using the EOQ model to determine the optimum amount of toys to order. Every time DP orders, there is a fixed charge of $75. The total amount of product needed monthly is 10,000 units. The carrying cost per unit per year is $5.00.

a. What is DP’s optimal ordering quantity? (EOQ)

b. What are the total inventory costs per year for DP Dolls, assuming the number of units in each order (Q) is the EOQ quantity from part a?