

Quiz B for 2:30 Class: 9/4/13

Name _____

Short Answer 1: Assume General Mills' current stock price is \$49.32 and that it will pay a dividend per share of \$0.35 on 10/5/13, 1/8/14, 4/8/14, and 7/8/14. Ignoring transaction costs, what price on 4/23/14 will lead to a loss for you if you short-sell General Mill's stock today and close out your position on 4/23/14?

Short Answer 2: Assume a risk-free bond pays \$150 two years from today. What is the no-arbitrage price if the risk-free rate is 1.4%?

Problem: Assume that each share of the Balanced Bond ETF holds one ST Bond and two LT bonds. Assume also that you have the following bid and ask prices, the number of bonds at each price, and the payment information for the ETF and the bonds. What is the maximum total arbitrage profit you can earn today? What trades today will set up the arbitrage? What cash flows will each of your positions generate? What transactions will be required two years from today? Show that the conditions of arbitrage are met. Notes: 1) I recommend building a table. 2) Use "+" for inflows and "-" for outflows. I will assume "+" if you do not write either one.

<u>Security</u>	<u>Bid</u>		<u>Ask</u>		<u>Payments in</u>	
	<u>Price</u>	<u>Number</u>	<u>Price</u>	<u>Number</u>	<u>Year 1</u>	<u>Year 2</u>
Balanced Bond ETF	\$859.80	500	\$860.00	300	\$400	\$500
ST Bond	\$282.80	600	\$283.20	400	\$200	\$100
LT Bond	\$277.30	700	\$277.70	900	\$100	\$200

Wall Street Journal Questions are on the back of this page.

Wall Street Journal Bonus Questions

1. How is GE planning to exit its retail lending business?
 - a. it will not allow holders of the store credit cards it has issued to make any new purchases with their cards
 - b. it will sell the unit that issues store credit cards to Warren Buffett's Berkshire Hathaway
 - c. it help each firm that has issued GE store credit cards to set up its own credit management departments
 - d. it will revoke all store credit cards it has issued and forgive any outstanding balances
 - e. it will spin off the unit that issues store credit cards through an initial public offering

2. After years of lecturing in the classroom on the dangers of pyramid schemes, Prof. William Keep has been consulted with in recent months regarding Herbalife by roughly two dozen investment firms, including Bill Ackman's Pershing Square Capital Management LP and George Soros's Soros Fund Management LLC. Professor Keep teaches in what discipline?
 - a. English
 - b. accounting
 - c. marketing
 - d. finance
 - e. economics

3. According to Jason Zweig, which of the following is the key to the investing success of Charlie Munger, Warren Buffett's business partner and vice chairman of Berkshire Hathaway?
 - a. don't be part of the herd
 - b. sit in a quiet room and think
 - c. be brave
 - d. be patient
 - e. all of the above

4. According to the Wall Street Journal, why did Verizon move to buy Vodafone's stake in Verizon wireless now?
 - a. U.S. regulators had granted a 30-day window for Verizon to buy out Vodafone's stake without requiring an anti-trust review of the acquisition
 - b. Vodafone finally agreed to an all-stock deal for its stake
 - c. Verizon wanted to gain full control of its wireless joint venture while financing is cheap
 - d. Verizon wanted to restructure its pricing of cell phone plans but Vodafone had been using its veto power to derail the plan
 - e. Vodafone had entered into discussions to sell its stake to Google

5. Standard & Poor's Ratings Services escalated its legal battle with the U.S. Justice Department, accusing it of filing its \$5 billion lawsuit against S&P in "retaliation" for the company's downgrade of
 - a. Fannie Mae debt in 2007
 - b. America's debt in 2011
 - c. Washington D.C.'s debt in 2008
 - d. mortgage-backed securities held by the Federal Reserve in 2010
 - e. Great Britain's debt in 2009