

1. Exercises 3 through 6 from page 359 of the textbook.
2. The current interest rate on a 3-month Treasury bill is 0.0634% and the current rate on a six-month bill is 0.1564%. If you assume that there is no risk or liquidity premium, you can calculate the expected return on some future Treasury bill. What are the exact characteristics of that asset (date of issue, term to maturity) and what is its expected rate of return?
3. Some stocks promise high dividend payments and others promise none.
 - a. Why do firms choose not to pay dividends?
 - b. What kind of firms are likely to make that choice?
 - c. Why are people willing to hold stocks that do not pay dividends?
 - d. Is it plausible that these stocks will never, ever pay dividends to shareholders?
4. The “price/earnings ratio” or P/E is a common metric for evaluating stocks. It is the ratio of the current share price to current annual earnings.
 - a. What economic forces that would tend to equalize P/E ratios across firms in an efficient market?
 - b. Why wouldn't you expect all P/E ratios to be exactly the same?
 - c. What kinds of firms would you expect to have high or low P/E ratios at any moment in time?
5. If you believe that interest rates are likely to rise in the future, what do you expect will happen to the prices of existing long-term bonds? Does this make bonds an attractive or unattractive investment choice? If everyone shares this opinion, will they tend to move their money into or out of bonds? How will this affect bond prices and the expected rate of return on bonds? How will this affect the prices of alternative assets such as stocks? Given this change in the value of stocks (assuming there is no change in the expected future profits of the firms), how will this affect the rate of return on stocks? How will equilibrium between the returns on stocks and bonds be restored?