EC303: Money and Banking

In-class exercise 8

Spring 2022

Exercise 1

Intel stock is currently selling for \$50 and pays yearly dividend of \$0.16 per share. Jim Cramer on CNBC predicts that Intel stock will sell for \$60 next year. Should you buy this stock? How do you decide?

Exercise 2

Kobe, Grayson, and Will are considering purchasing stock of a company. The company is expected to pay a dividend of \$2 per share next year. Since all of them love Jim Cramer, they watch CNBC and hear that this company's dividend is expected to grow at 3% per year forever.

1. Kobe is *uncertain* about both the constancy of dividends and the accuracy of the growth rate so he requires a minimum of 15% return to invest in this stock.
2. Grayson has good connections with industry insiders. She just spoke to some industry insiders and is confident about the projected cash flows. She just requires 12% return.
3. Will is dating the CEO of the company. He knows with certainty what the company will do next. He requires only 10% return.

How much will Kobe, Grayson and Will pay for this stock? Hint: apply the Gordon Growth Model.

Exercise 3

Using the Gordon Growth Model, explain how the recent monetary policy decision by the Fed affects stock prices.

Exercise 4

Using the Gordon Growth Model, analyze how the Coronavirus pandemic affected stock prices.