

BMC Answers (Bloomberg) 2020/2021, Complete solutions (A+ guide) University of Massachusetts, Lowell.

written by

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Bloomberg Answers

Economic Indicators

The Primacy of GDP (30 min.)

Knowledge Check 1

How accurately do GDP statistics portray the economy and why?

- **Inaccurately because the scope of GDP measurements can change.**

Knowledge Check 2

Consider the formula $GDP = C + I + (X - M)$. A country is undergoing a boom in consumer domestic and foreign luxury goods. In one year, the dollar growth in imports is greater than the dollar growth in domestic consumption. Assuming nothing else has changed, what happens to GDP?

- **It went down.**

Knowledge Check 3

Here is the most important economic data for Australia and Sweden. Which economy performed better year-over-year (YOY) in the fourth quarter of 2013 compared to the fourth quarter of 2012? Use the two charts to investigate.

- **Sweden performed better.**

Knowledge Check 4

In the US, why is there a strong correlation between unemployment and GDP?

- **Consumer spending accounts for two-thirds of the U.S. economy. When the unemployment rate rises, there is less consumer spending.**

SECTION QUIZ

- Here is a chart showing both nominal GDP growth and real GDP growth for the United States from 2007 to 2010. Which of the following can be a true statement at the time the chart was created?
 - The country has deflation. The bottom line is nominal growth and the top line is real growth.**
- Which of the following lines is the best leading economic factor?
 - PMI**
- The “misery index” is often cited in the media as a way to measure consumer dissatisfaction. It is defined as the inflation rate plus the unemployment rate. Review and identify the country with the highest “misery index.”
 - Argentina**
- What typically happens to nonfarm payrolls, the PMI indicator, and housing starts in the onset of a recession in the United States?
 - Nonfarm payrolls go DOWN, the PMI indicator goes DOWN, the housing starts go DOWN.**

Monitoring GDP (10 min.)

SECTION QUIZ

1. Which of the following qualities of economic indicators do investors prize the most?
 - a. Timeliness of release.
2. Why is the release of GDP statistics less interesting to investors than the release of other economic indicators?
 - a. Because GDP statistics are released well after other economic indicators.
3. Which of the following important U.S. economic indicators is only available on a quarterly basis?
 - a. GDP
4. Which economic indicator is most directly linked to unemployment?
 - a. Nonfarm payrolls.

Forecasting GDP (20 min.)

Knowledge Check 1

Here is the economic calendar for the UK for August 2013. Examine indicators like inflation, house prices, industrial production, employment, retail sales, and GDP. Based on these monthly indicators, how did the UK economy perform overall?

- Above Expectations

Knowledge Check 2

This chart was captured in mid-2014. At that point in time, which of the following trends had best described the growth in the Chinese economy predicted in this pop-out table?

- Deceleration

Knowledge Check 3

How have economic forecasts for this economy evolved?

- Minimal Change

SECTION QUIZ

1. These charts show data for four countries as of early 2016. For each country, the blue line denotes historic real GDP growth. The white line denotes the consensus analyst forecast for real GDP growth. The red line denotes the most pessimistic analyst forecast, and the green line denotes the most optimistic analyst forecast. For which country is there the most controversy among the analyst community about 2016 growth?
 - a. *RUSSIA*
2. What is the main reason that investment banks create estimates of economic indicators?
 - a. *To know when specific economic data points are a positive or negative surprise.*
3. Which of the following is the biggest pitfall of economic indicators?
 - a. *They do not consistently presage turning points.*
4. Here is a chart displaying estimates of the initial jobless claims indicator, one of the main unemployment statistics in the U.S. It measures the number of new applications for unemployment benefits each week. Which of the following best describes the trend in the data?
 - a. *The data shows a steady decline in jobless claims over the period shown.*

Currencies

Currency Market Mechanics (25 min.)

Knowledge Check 1

Which country is both the fourth biggest importer and exporter?

- JAPAN

Knowledge Check 2

In 1994, the Mexican peso declined against the U.S. dollar during the so-called "Tequila Crisis". What exacerbating factor did Mexico's "Tequila Crisis" have in common with the Asian crisis of 2002?

- Both countries had large dollar-denominated debts.

Knowledge Check 3

Using the given chart, how many New Zealand dollars (NZD) can you buy with 100 Australian dollars (AUD)?

- 107.89

SECTION QUIZ

- Allison lives in America and has just retired. It is early 2016. She has long had a list of places she would like to visit: cruising the fjords on the west coast of Norway, visiting Buckingham Palace in the United Kingdom, seeing the cherry blossoms in Japan, and going to the top of the Eiffel Tower in France. She last considered all four options on New Year's Day 2016. She would like to select the trip to go on based on which country's currency has subsequently weakened the most against the U.S. dollar. Where should she go for her vacation?
 - NORWAY
- Review the currency pair charts for the Barbadian dollar against the Jamaican dollar, the Czech koruna against the Polish zloty, the Nigerian naira against the Ghanaian cedi, and the Hong Kong dollar against the Macanese pataca. Which pair is pegged?
 - The Hong Kong dollar against the Macanese pataca
- Which of the following is NOT an example of a failed peg?
 - Hong Kong dollar against the U.S. dollar in 1997.
- Use the chart below to answer the question. How many Danish crowns (DKK) can you buy with 100 Japanese yen (JPY)?
 - 5.360

Currency Valuation (20 min.)

Knowledge Check 1

According to this Big Mac index screen, which of the following four countries' currencies is most undervalued?

- China

Knowledge Check 2

What generally happens when a central bank unexpectedly increases interest rates?

- The currency strengthens

Knowledge Check 3

Which driver weakened the Swiss franc?

- A surprise change in inflation expectations

SECTION QUIZ

1. What does the Big Mac index show?
 - a. *How currencies may be overvalued or undervalued*
2. Which of the following are short-term drivers of currency valuation?
 - a. *Surprise changes in interest rates, inflation, and trade*
3. By what mechanism do interest rates affect currency values?
 - a. *Global investors are attracted by higher bond yields in high interest rate countries*
4. Which of these headlines could move a currency pair?
 - a. *U.S. Stocks Rally on Fed's Surprise Reduction of the Interest Rate*

Central Banks and Currencies (15 min.)

SECTION QUIZ

1. What is the most common target inflation rate for an advanced economy?
 - a. *2%*
2. What was the primary goal of Abenomics?
 - a. *To halt the vicious cycle of deflation*
3. Here is the deflationary cycle. What steps connect the lower left gray arrow to the upper right blue arrow?
 - a. *Prices Decline*
4. Were the two oil crises in the 1970s linked to deflation or inflation?
 - a. *Inflation*

Currency Risk (15 min.)

Knowledge Check 1

On June 23, 2016, the UK voted to leave the European Union. The white line shows the UK equity index, the FTSE 100, from the start of 2016 to the date on which the UK notified the European Union of its intent to leave. The orange line shows the number of dollars it takes to buy one pound sterling. The UK is a net importer, meaning imports exceed the value of exports. What can be reasonably surmised from the large UK corporations?

- They are probably heavy exporters

Knowledge Check 2

In early 2016, the same Germany machinery company has interest from four prospective

CFO would like to choose the client which is least likely to cancel the order due to currency volatility. The invoice comes due on June 30, 2016. According to historical currency movements alone, which prospective client would be least likely to cancel the order?

- Indonesia

Knowledge Check 3

What is the median estimate for the number of Japanese yen per euro for calendar year 2018?

- 126

Knowledge Check 4

What is the different between Nomura and RBC's estimate for the Japanese yen/euro pair for the end of Q1 2018?

- 40 yen

Knowledge Check 5

Imagine you are a Dutch diamond dealer who sources diamonds from South Africa. In 2016, a new mine is being dug in South Africa and you have agreed with the mine owner to purchase one million South African rands' worth of diamond a year from today. Therefore, you will receive one million rands in cash in one year's time. The miner wants you to demonstrate your commitment by either giving him a million rands now or providing that you have an FX forward contract for the full amount. Currently, the exchange rate is 17.1 rands to the euro. You check the current forward rates on offer on the Bloomberg FRD function.

You have two options. Exchange euros today at today's exchange rate to pay him one million rands now, or lock in a forward agreement to convert euros to one million rands in one year's time and share the forward agreement with him. If you were to do the forward agreement, exchanging euros for rands today, approximately how much more or less would you have in a year?

- EUR 4,717 more

SECTION QUIZ

1. Why would Jack Welch suggest putting all company plants on barges?
 - a. *To respond quickly to changes in the currency markets*
2. Samsung is based in South Korea and reports in South Korean won. Samsung's revenue comes from products around the world and the geographic breakdown of its 2015 revenue is shown in the first chart. The other charts show how some major world currencies moved relative to the South Korean won through the course of 2015. Of the currencies shown, which currency's movement boosted Samsung's revenue growth the most?
 - a. *DOLLAR*
3. Legendary investor Warren Buffet said, "Gold gets dug out of the ground... it's melted, melt it down, dig another hole, bury it again, and pay people to stand around it. It has no utility. Anyone watching from Mars would be scratching their head." Based on this quotation, what quality of gold is he referring to?
 - a. *Its storage costs*
4. Which of the following options is the best way for investors to manage currency risk?

Fixed Income

The Roots of the Bond Market (25 min.)

Knowledge Check 1

What do the green bars at the bottom signify?

- Surplus

Knowledge Check 2

According to the table, who owns approximately 1.3% of actively traded US debt?

- Taiwan

Knowledge Check 3

What quality of US government bonds causes investors to buy them when market values rise?

- U.S. Government Bonds are considered low risk

Knowledge Check 4

Why is fixed income called fixed income?

- Because the repayment amounts and timings are fixed for ordinary bonds

SECTION QUIZ

1. Why does the United States have a strong reputation for creditworthiness?
a. Because it has the right to tax the wealthiest population on earth.
2. What is one reason why foreign governments lend to the U.S. government?
a. To build liquid FX reserves.
3. What does one yellow bar depict in this debt distribution diagram?
a. Coupon repayment
4. Which one of the following actors benefits when interest rates go up?
a. An investor who is about to buy bonds.

Bond Valuation (50 min.)

Knowledge Check 1

When investors doubt the creditworthiness of a borrower, how do they alter their calculation of the bond yield to take into account these doubts?

- Investors do not alter the calculation.

Knowledge Check 2

As a general rule, what percentage of debt to GDP will make a government bond yield rise?

- There is no general rule.

Knowledge Check 3

What is true of both the UK and the US?

- Both countries are highly creditworthy.

Knowledge Check 4

Which would you prefer?

Knowledge Check 2

Why did the corporate spread significantly widen during the 2008 market crash?

- Corporate bond issuers go bankrupt more frequently than governments, as they do not have a tax base to fall back on in hard times.

SECTION QUIZ

1. What impact will a tightening of the corporate spread most likely have on a company?
a. A tendency to expand the borrowing capacity of the company.
2. What are the three main transmission mechanisms by which the yield curve affects the economy?
a. Corporate impact, global impact, consumer impact.
3. What is the 10-year to 3-month term premium of the following yield curve?
a. 2.398%
4. The purchase of which of the following products is most affected by interest rate changes?
a. A house.

Movements in the Yield Curve (20 min.)

SECTION QUIZ

1. What is the primary driver of the left-hand end of the yield curve?
a. Central bank interest rates.
2. Which yield curve is most likely linked to a booming economy?
a. B
3. The two yield curves in the chart are from September 10, 2001 and from October 1, 2001. What do you think the Federal Reserve did with interest rates in the months following the attacks of September 11, 2001?
a. Cut interest rates.
4. Why does the yield curve tend to invert shortly before a recession?
a. An inverted yield curve means that bond traders are predicting interest rate cuts and interest rate cuts happen in response to a recession.

EQUITIES

Introducing the Stock Market (25 min.)

Knowledge Check 1

Why do companies do IPOs?

- IPOs incentivize entrepreneurs to innovate as IPOs provide a way for entrepreneurs to monetize their work.

SECTION QUIZ

1. Why do company manager-owners smile when they ring the stock exchange bell on the day of an IPO?
 - a. *An IPO crystallizes the value of the manager-owners' stake*
2. The Dow Jones Industrial Average Index has an unusual weighting method. Unlike the S & P 500, it is weighted by share price. Here are 22 of the 30 members of the Dow Jones as of mid-June 2015. If all the shares went up by 5%, which share on the list shown would have the biggest contribution to an upward movement in the index?
 - a. *Goldman Sachs*
3. In 1999, James Glassman and Kevin Hassett published a book called "Dow Jones: The Story of the Dow Jones Industrial Average Index". At the time, the Dow Jones Industrial Average Index was just under 12,000. Which of the following is a potential substitute for the book title?
 - a. *"The Sum of the Share Prices of All 30 Dow Jones Members Will Triple"*
4. Here is a chart of the index value for the S&P 500 and the United Kingdom's index, the FTSE 100, from the end of 2008 to early 2015. The labels have been removed. One index has clearly outperformed the other. Over this period, there was a housing boom and an oil crash. Here are pie charts showing the early 2015 index composition by industry for both the S&P 500 and the FTSE 100. Which index outperformed the other?
 - a. *The S&P 500 Index.*

The Nature of Equities (35 min.)

Knowledge Check 1

What is the prime reason that Jenny's discretionary income is more volatile than her total income?

- Her mortgage payments and necessities are fixed.

Knowledge Check 2

A wedding planning company has a high fixed-cost base and a lot of debt. Who would be most likely to start such a company rather than be an employee?

- A shareholder in a booming economy

Knowledge Check 3

The S&P 500 stood at 1848 at the end of 2013. According to the chart, what would the approximate return be on the S&P 500 from the trough of March of 2009 to the end of 2013, ignoring dividends?

- 170%

Knowledge Check 4

Assume that an investor in the S&P 500 reinvests his dividends. According to the chart, what approximate return would this investor have reaped from the early 2009 through the endpoint of the chart?

- 200%

SECTION QUIZ

1. Why are equities volatile?
 - a. *Due to the residual nature of earnings.*
2. Which of the following statements is true?
 - a. *When you buy an equity, the most you can lose is 100% and your potential gain is unlimited.*
3. In the example highlighting the differences between bond holders and shareholders, we equated surgeon Jenny to a shareholder. Which row of the budget planning table represents the amount to which she as a shareholder would be entitled?
 - a. *D.*
4. You buy the stock of four consumer goods companies at the end of 2004 and hold it until August 2010. Here are the TRA (Total Return) charts from Bloomberg for these stocks. The "Buy Price" in the top left-hand corner is the price you paid for the stock. The price of the stock in August 2010 is noted in the chart's legend. The legend also shows the Dividend Adjusted Value in 2010, which is the value of the stock including dividends over the holding period. For which stock did the bulk of the total return come from dividends?
 - a. *Procter & Gamble.*

Equity Research (45 min.)

Knowledge Check 1

What does the release of earnings announcements have in common with the release of economic indicators?

- Both are estimated in advance by analysts.

Knowledge Check 2

The number at the bottom right of each supplier's box shows the portion of Boeing's capital expenditure last year that went to that supplier. The number at the bottom right of each customer's box shows the portion of the customer's capital expenditure (money spent in high value purchases) in the last year that went to Boeing. For which company shown was Boeing the largest supplier in the last year?

- United Continental

Knowledge Check 3

Which company is most exposed to the ups and downs of the aircraft engine industry?

- MTU Aero Engines

Knowledge Check 4

research note to help a portfolio manager decide between investing in Rolls-Royce or Boeing Technologies?

- A comparison of the commercial prospect of new aircraft models.

Knowledge Check 5

You are building a financial model of a bifocal lens manufacturer. Which of the following would be the best driver to use?

- Median age of society

Knowledge Check 6

Here is a table from the Bloomberg Intelligence aluminum dashboard which shows the end-uses of aluminum in China. Which of the following Bloomberg headlines would be of most interest to an aluminum trader in China?

- China's Aluminum Demand Weathers Real-Estate Slowdown So Far

SECTION QUIZ

1. When an analyst is looking at a company for the first time, which of the following activities does he do first?
 - a. *Defines the industry or industries in which the company operates.*
2. Here is a table from the Bloomberg Intelligence copper dashboard which shows the different end-users of the "red metal." Which of the following Bloomberg headlines would likely be of most interest to a copper trader?
 - a. *China's Construction Slowdown Dents Copper Consumption, Prices*
3. Here is a breakdown of post-it note inventor 3M's revenue by industry. Which of the following industry drivers should be of most interest to a prospective investor?
 - a. *The change in postal volumes.*
4. Company X was expected to have earnings per share of \$0.52 for the upcoming quarter. On the day of the results, the company reported earnings per share of \$0.80. What happened to the share price when the stock market opened?
 - a. *There is not enough information to tell.*

Absolute Valuation (50 min.)

Knowledge Check 1

Which company is worth more, Coca-Cola or Pepsi?

- Coca-Cola because it has a higher market capitalization

Knowledge Check 2

Widget Co has a market capitalization of \$ 100M. It does a 10-for-1 stock split. It then does a 5-for-1 stock split. Finally, it does a 35-for-1 stock split. Nothing else changes. What is the new market cap?

- \$100M

Knowledge Check 3

What input do both absolute valuation and relative valuation typically require?

- Short-term forecasts

Knowledge Check 4

Which if the following is most likely to be the most challenging part of this step of the valuation process?

- Making the assumptions upon which to project future performance.

Knowledge Check 5

What is a reason one discounts future cash flow as part of the absolute valuation process?

- Future profits are uncertain

Knowledge Check 6

What role does beta play in absolute valuation?

- It determines how risky a stock is in comparison to the overall stock market

Knowledge Check 7

Here is the capital structure of Microsoft. What part of the \$42.03 share price (to the dollar) is represented by cash?

- \$11

Knowledge Check 8

How is enterprise value calculated?

- Enterprise Value = Market Cap – Cash + Debt

SECTION QUIZ

1. Which of the following stocks is most sensitive to the movement of the market?
a. Amazon
2. Which of the following assigns the same relative weightings to short-term and long-term outcomes as the absolute variation process?
a. A fishery exceeding fishing quotas.
3. Here is the WACC function for U.S. drug company Pfizer. The WACC calculation is hidden. What is the WACC?
a. 8.2%
4. A rise in which of the following inputs will increase an absolute variation?
a. Earnings Estimates

Relative Valuation (45 min.)

Knowledge Check 1

How do earnings yields differ from bond yields?

- The cash flow from equities can continue indefinitely while the cash flow from bonds comes to an end.

Knowledge Check 2

At its peak at the end of 1999, Microsoft had a market cap of \$600B. PC sales were growing rapidly and most PCs ran on Microsoft software. Revenue was growing 30% per year. The market peaked at nearly 80.0X in 1999. Looking at this chart, what happened in the subsequent years?

Knowledge Check 3

What is one possible weakness of this peer approach to valuation?

- The estimated growth can be dramatically wrong.

Knowledge Check 4

What may be a problem of comparing the P/E of a stock to the P/E of the overall market?

- A stock's P/E ratio can remain above or below market average for extended periods.

SECTION QUIZ

1. Here is a chart of the NASDAQ Composite, the world's main technology index, in the dotcom bubble on March 10, 2000. The P/E ratio later peaked above 30. In hindsight, this is widely agreed to have been a bubble. In March 2015, the index for the first time since then surpassed the peak. Why might some investors have argued "this time it's different"?
 - a. *Earnings grew substantially, meaning that the P/E ratio in early 2015 was around 30.3x.*
2. The World Equity Index function shown contains two valuation metrics for the Nike stock. The Nike description contains the same two valuation metrics. How does Nike's valuation compare to that of the S&P 500?
 - a. *Nike is more expensive than the S&P 500 on both a P/E and dividend yield basis.*
3. If the earnings per share of a company is \$1 and the earnings yield is 2%, what is the price per share?
 - a. *\$50.00*
4. This chart shows a scatterplot with the x-axis being the estimated sales growth rate and the y-axis being the estimated P/E multiple. Given this data alone, which of the companies may warrant further analysis by a portfolio manager looking to buy an insurance company for her portfolio?
 - a. *Chubb.*