

**HOMEWORK # 4 (for due date see web page)**

You have been hired by a firm as a consultant for three consecutive years, starting from next year (a year from now). The firm is offering alternative compensation options:

- (1) You are paid the same salary of \$12,000 in each of the three years.
- (2) You will be paid only once in the amount of  $B$  in the third year.
- (3) You will be paid only once in the amount of  $C$  in the second year.
- (4) You will be paid only once in the amount of  $D$  in the first year.
- (5) You will be paid only once, today, in the amount of  $E$ .

You decide to evaluate each option in terms of its present value.

- (a) Suppose that the annual interest rate is 5%. What value of  $B$  would make you indifferent between options 1 and 2?
- (b) Suppose that the annual interest rate is 5%. What value of  $C$  would make you indifferent between options 1 and 3?
- (c) Suppose that the annual interest rate is 5%. What value of  $D$  would make you indifferent between options 1 and 4?
- (d) Suppose that the annual interest rate is 5%. What value of  $E$  would make you indifferent between options 1 and 5?
- (e) Suppose that the annual interest rate is 5%. What will you choose if  $B = 37,500$ ,  $C = 36,050$ ,  $D = 34,200$  and  $E = 32,678$ ?