**Chapter 01 Test Bank - Static**

*Student: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_*

**Multiple Choice Questions**

1. The material wealth of a society is a function of

A. all financial assets.

B. all real assets.

C. all financial and real assets.

D. all physical assets.

2. \_\_\_\_\_\_\_ are real assets.

A. Land

B. Machines

C. Stocks and bonds

D. Knowledge

E. Land, machines, and knowledge

3. The means by which individuals hold their claims on real assets in a well-developed economy are

A. investment assets.

B. depository assets.

C. derivative assets.

D. financial assets.

E. exchange-driven assets.

4. \_\_\_\_\_\_\_ are financial assets.

A. Bonds

B. Machines

C. Stocks

D. Bonds and stocks

E. Bonds, machines, and stocks

5. \_\_\_\_\_\_\_\_\_ financial asset(s).

A. Buildings are

B. Land is a

C. Derivatives are

D. U.S. agency bonds are

E. Derivatives and U.S. agency bonds are

6. Financial assets

A. directly contribute to the country's productive capacity.

B. indirectly contribute to the country's productive capacity.

C. contribute to the country's productive capacity, both directly and indirectly.

D. do not contribute to the country's productive capacity, either directly or indirectly.

E. are of no value to anyone.

7. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the most significant real asset of U.S. households in terms of total value.

A. consumer durables

B. automobiles

C. real estate

D. mutual fund shares

E. bank loans

8. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the least significant financial asset of U.S. households in terms of total value.

A. real estate

B. mutual fund shares

C. debt securities

D. life insurance reserves

E. pension reserves

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A. real estate

B. mutual fund shares

C. debt securities

D. life insurance reserves

E. pension reserves

10. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the most significant asset of U.S. households in terms of total value.

A. real estate

B. mutual fund shares

C. debt securities

D. life insurance reserves

E. pension reserves

11. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ were the most significant liability of U.S. households in terms of total value.

A. credit cards

B. mortgages

C. bank loans

D. student loans

E. other forms of debt

12. In 2016, which of the following financial assets make up the greatest proportion of the financial assets held by U.S. households?

A. Pension reserves

B. Life insurance reserves

C. Mutual fund shares

D. Debt securities

E. Personal trusts

13. In 2016, \_\_\_\_\_\_\_ of the assets of U.S. households were financial assets as opposed to tangible assets.

A. 20.4%

B. 34.2%

C. 69.4%

D. 71.7%

E. 82.5%

14. The largest component of domestic net worth in 2016 was

A. nonresidential real estate.

B. residential real estate.

C. inventories.

D. consumer durables.

E. equipment and software.

15. The smallest component of domestic net worth in 2016 was

A. nonresidential real estate.

B. residential real estate.

C. inventories.

D. consumer durables.

E. equipment and software.

16. The domestic net worth of the U.S. in 2016 was

A. $15.411 trillion.

B. $26.431 trillion.

C. $42.669 trillion.

D. $64.747 trillion.

E. $70.983 trillion.

17. A fixed-income security pays

A. a fixed level of income for the life of the owner.

B. a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

C. a variable level of income for owners on a fixed income.

D. a fixed or variable income stream at the option of the owner.

18. A debt security pays

A. a fixed level of income for the life of the owner.

B. a variable level of income for owners on a fixed income.

C. a fixed or variable income stream at the option of the owner.

D. a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

19. Money market securities

A. are short term.

B. are highly marketable.

C. are generally very low risk.

D. are highly marketable and are generally very low risk.

E. All of the options.

20. An example of a derivative security is

A. a common share of Microsoft.

B. a call option on Intel stock.

C. a commodity futures contract.

D. a call option on Intel stock and a commodity futures contract.

E. a common share of Microsoft and a call option on Intel stock.

21. The value of a derivative security

A. depends on the value of the related security.

B. is unable to be calculated.

C. is unrelated to the value of the related security.

D. has been enhanced due to the recent misuse and negative publicity regarding these instruments.

E. is worthless today.

22. Although derivatives can be used as speculative instruments, businesses most often use them to

A. attract customers.

B. appease stockholders.

C. offset debt.

D. hedge risks.

E. enhance their balance sheets.

23. Financial assets permit all of the following except

A. consumption timing.

B. allocation of risk.

C. separation of ownership and control.

D. elimination of risk.

24. The \_\_\_\_\_\_\_\_\_\_\_\_ refers to the potential conflict between management and shareholders.

A. agency problem

B. diversification problem

C. liquidity problem

D. solvency problem

E. regulatory problem

25. A disadvantage of using stock options to compensate managers is that

A. it encourages managers to undertake projects that will increase stock price.

B. it encourages managers to engage in empire building.

C. it can create an incentive for managers to manipulate information to prop up a stock price temporarily, giving them a chance to cash out before the price returns to a level reflective of the firm's true prospects.

D. All of the above.

26. Which of the following are mechanisms that have evolved to mitigate potential agency problems?

I) Using the firm's stock options for compensation

II) Hiring bickering family members as corporate spies

III) Boards of directors forcing out underperforming management

IV) Security analysts monitoring the firm closely

V) Takeover threats

A. II and V

B. I, III, and IV

C. I, III, IV, and V

D. III, IV, and V

E. I, III, and V

27. Corporate shareholders are best protected from incompetent management decisions by

A. the ability to engage in proxy fights.

B. management's control of pecuniary rewards.

C. the ability to call shareholder meetings.

D. the threat of takeover by other firms.

E. one-share/one-vote election rules.

28. Theoretically, takeovers should result in

A. improved management.

B. increased stock price.

C. increased benefits to existing management of the taken-over firm.

D. improved management and increased stock price.

E. All of the options.

29. During the period between 2000 and 2002, a large number of scandals were uncovered. Most of these scandals were related to

I) manipulation of financial data to misrepresent the actual condition of the firm.
II) misleading and overly optimistic research reports produced by analysts.
III) allocating IPOs to executives as a quid pro quo for personal favors.
IV) greenmail.

A. II, III, and IV

B. I, II, and IV

C. II and IV

D. I, III, and IV

E. I, II, and III

30. The Sarbanes-Oxley Act

A. requires corporations to have more independent directors.

B. requires the firm's CFO to personally vouch for the firm's accounting statements.

C. prohibits auditing firms from providing other services to clients.

D. requires corporations to have more independent directors and requires the firm's CFO to personally vouch for the firm's accounting statements.

E. All of the above.

31. Asset allocation refers to

A. choosing which securities to hold based on their valuation.

B. investing only in "safe" securities.

C. the allocation of assets into broad asset classes.

D. bottom-up analysis.

32. Security selection refers to

A. choosing which securities to hold based on their valuation.

B. investing only in "safe" securities.

C. the allocation of assets into broad asset classes.

D. top-down analysis.

33. Which of the following portfolio construction methods starts with security analysis?

A. Top-down

B. Bottom-up

C. Middle-out

D. Buy and hold

E. Asset allocation

34. Which of the following portfolio construction methods starts with asset allocation?

A. Top-down

B. Bottom-up

C. Middle-out

D. Buy and hold

E. Asset allocation

35. \_\_\_\_\_\_\_ are examples of financial intermediaries.

A. Commercial banks

B. Insurance companies

C. Investment companies

D. Credit unions

E. All of the options

36. Financial intermediaries exist because small investors cannot efficiently

A. diversify their portfolios.

B. assess credit risk of borrowers.

C. advertise for needed investments.

D. diversify their portfolios and assess credit risk of borrowers.

E. All of the options.

37. \_\_\_\_\_\_\_\_ specialize in helping companies raise capital by selling securities.

A. Commercial bankers

B. Investment bankers

C. Investment issuers

D. Credit raters

38. Commercial banks differ from other businesses in that both their assets and their liabilities are mostly

A. illiquid.

B. financial.

C. real.

D. owned by the government.

E. regulated.

39. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant financial asset(s) of U.S. commercial banks in terms of total value.

A. loans and leases

B. cash

C. real estate

D. deposits

E. investment securities

40. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant liability(ies) of U.S. commercial banks in terms of total value.

A. loans and leases

B. cash

C. real estate

D. deposits

E. investment securities

41. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant real asset(s) of U.S. nonfinancial businesses in terms of total value.

A. equipment and software

B. inventory

C. real estate

D. trade credit

E. marketable securities

42. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant real asset(s) of U.S. nonfinancial businesses in terms of total value.

A. equipment and software

B. inventory

C. real estate

D. trade credit

E. marketable securities

43. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant liability(ies) of U.S. nonfinancial businesses in terms of total value.

A. bonds and mortgages

B. bank loans

C. inventories

D. trade debt

E. marketable securities

44. In terms of total value, the most significant liability(ies) of U.S. nonfinancial businesses in 2016 was(were)

A. bank loans.

B. bonds and mortgages.

C. trade debt.

D. other loans.

E. marketable securities.

45. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant financial asset(s) of U.S. nonfinancial businesses in terms of total value.

A. cash and deposits

B. trade credit

C. trade debt

D. inventory

E. marketable securities

46. New issues of securities are sold in the \_\_\_\_\_\_\_\_ market(s).

A. primary

B. secondary

C. over-the-counter

D. primary and secondary

47. Investors trade previously issued securities in the \_\_\_\_\_\_\_\_ market(s).

A. primary

B. secondary

C. primary and secondary

D. derivatives

48. Investment bankers perform which of the following role(s)?

A. Market new stock and bond issues for firms

B. Provide advice to the firms as to market conditions, price, etc.

C. Design securities with desirable properties

D. All of the options

E. None of the options

49. Until 1999, the \_\_\_\_\_\_\_\_ Act(s) prohibited banks in the United States from both accepting deposits and underwriting securities.

A. Sarbanes-Oxley

B. Glass-Steagall

C. SEC

D. Sarbanes-Oxley and SEC

E. None of the options

50. The spread between the LIBOR and the Treasury-bill rate is called the

A. term spread.

B. T-bill spread.

C. LIBOR spread.

D. TED spread.

51. Mortgage-backed securities were created when \_\_\_\_\_\_\_\_ began buying mortgage loans from originators and bundling them into large pools that could be traded like any other financial asset.

A. GNMA

B. FNMA

C. FHLMC

D. FNMA and FHLMC

E. GNMA and FNMA

52. The sale of a mortgage portfolio by setting up mortgage pass-through securities is an example of

A. credit enhancement.

B. credit swap.

C. unbundling.

D. derivatives.

53. Which of the following is true about mortgage-backed securities?

I) They aggregate individual home mortgages into homogeneous pools.
II) The purchaser receives monthly interest and principal payments received from payments made on the pool.
III) The banks that originated the mortgages maintain ownership of them.
IV) The banks that originated the mortgages may continue to service them.

A. II, III, and IV

B. I, II, and IV

C. II and IV

D. I, III, and IV

E. I, II, III, and IV

54. \_\_\_\_\_\_\_\_ were designed to concentrate the credit risk of a bundle of loans on one class of investor, leaving the other investors in the pool relatively protected from that risk.

A. Stocks

B. Bonds

C. Derivatives

D. Collateralized debt obligations

E. All of the options

55. \_\_\_\_\_\_\_\_ are, in essence, an insurance contract against the default of one or more borrowers.

A. Credit default swaps

B. CMOs

C. ETFs

D. Collateralized debt obligations

E. All of the options

**Chapter 01 Test Bank - Static Key**

**Multiple Choice Questions**

1. The material wealth of a society is a function of

A. all financial assets.

**B.** all real assets.

C. all financial and real assets.

D. all physical assets.

The material wealth of a society is a function of all real assets.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

2. \_\_\_\_\_\_\_ are real assets.

A. Land

B. Machines

C. Stocks and bonds

D. Knowledge

**E.** Land, machines, and knowledge

Land, machines and knowledge are real assets; stocks and bonds are financial assets.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

3. The means by which individuals hold their claims on real assets in a well-developed economy are

A. investment assets.

B. depository assets.

C. derivative assets.

**D.** financial assets.

E. exchange-driven assets.

Financial assets allocate the wealth of the economy. Example: it is easier for an individual to own shares of an auto company than to own an auto company directly.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

4. \_\_\_\_\_\_\_ are financial assets.

A. Bonds

B. Machines

C. Stocks

**D.** Bonds and stocks

E. Bonds, machines, and stocks

Machines are real assets; stocks and bonds are financial assets.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

5. \_\_\_\_\_\_\_\_\_ financial asset(s).

A. Buildings are

B. Land is a

C. Derivatives are

D. U.S. agency bonds are

**E.** Derivatives and U.S. agency bonds are

Buildings and land are real assets.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

6. Financial assets

A. directly contribute to the country's productive capacity.

**B.** indirectly contribute to the country's productive capacity.

C. contribute to the country's productive capacity, both directly and indirectly.

D. do not contribute to the country's productive capacity, either directly or indirectly.

E. are of no value to anyone.

Financial assets indirectly contribute to the country's productive capacity because these assets permit individuals to invest in firms and governments. This in turn allows firms and governments to increase productive capacity.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Real and financial assets*

7. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the most significant real asset of U.S. households in terms of total value.

A. consumer durables

B. automobiles

**C.** real estate

D. mutual fund shares

E. bank loans

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

8. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the least significant financial asset of U.S. households in terms of total value.

A. real estate

B. mutual fund shares

C. debt securities

**D.** life insurance reserves

E. pension reserves

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
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Difficulty: 1 Basic
Topic: Real and financial assets*

9. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was the most significant financial asset of U.S. households in terms of total value.

A. real estate

B. mutual fund shares

C. debt securities

D. life insurance reserves

**E.** pension reserves

See Table 1.1.

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Topic: Real and financial assets*

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**A.** real estate

B. mutual fund shares

C. debt securities

D. life insurance reserves

E. pension reserves

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

11. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ were the most significant liability of U.S. households in terms of total value.

A. credit cards

**B.** mortgages

C. bank loans

D. student loans

E. other forms of debt

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Debt financing*

12. In 2016, which of the following financial assets make up the greatest proportion of the financial assets held by U.S. households?

**A.** Pension reserves

B. Life insurance reserves

C. Mutual fund shares

D. Debt securities

E. Personal trusts

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

13. In 2016, \_\_\_\_\_\_\_ of the assets of U.S. households were financial assets as opposed to tangible assets.

A. 20.4%

B. 34.2%

**C.** 69.4%

D. 71.7%

E. 82.5%

See Table 1.1.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

14. The largest component of domestic net worth in 2016 was

A. nonresidential real estate.

**B.** residential real estate.

C. inventories.

D. consumer durables.

E. equipment and software.

See Table 1.2.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

15. The smallest component of domestic net worth in 2016 was

A. nonresidential real estate.

B. residential real estate.

**C.** inventories.

D. consumer durables.

E. equipment and software.

See Table 1.2.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

16. The domestic net worth of the U.S. in 2016 was

A. $15.411 trillion.

B. $26.431 trillion.

C. $42.669 trillion.

**D.** $64.747 trillion.

E. $70.983 trillion.

See Table 1.2.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

17. A fixed-income security pays

A. a fixed level of income for the life of the owner.

**B.** a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

C. a variable level of income for owners on a fixed income.

D. a fixed or variable income stream at the option of the owner.

A fixed-income security pays a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Fixed-income securities*

18. A debt security pays

A. a fixed level of income for the life of the owner.

B. a variable level of income for owners on a fixed income.

C. a fixed or variable income stream at the option of the owner.

**D.** a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

A debt security pays a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Fixed-income securities*

19. Money market securities

A. are short term.

B. are highly marketable.

C. are generally very low risk.

D. are highly marketable and are generally very low risk.

**E.** All of the options.

All answers are correct.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Money market securities*

20. An example of a derivative security is

A. a common share of Microsoft.

B. a call option on Intel stock.

C. a commodity futures contract.

**D.** a call option on Intel stock and a commodity futures contract.

E. a common share of Microsoft and a call option on Intel stock.

The values of a call option on Intel stock and a commodity futures contract are derived from that of an underlying asset; the value of a common share of Microsoft is based on the value of the firm only.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Derivatives general*

21. The value of a derivative security

**A.** depends on the value of the related security.

B. is unable to be calculated.

C. is unrelated to the value of the related security.

D. has been enhanced due to the recent misuse and negative publicity regarding these instruments.

E. is worthless today.

Of the factors cited above, only the value of the related security affects the value of the derivative and/or is a true statement.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Derivatives general*

22. Although derivatives can be used as speculative instruments, businesses most often use them to

A. attract customers.

B. appease stockholders.

C. offset debt.

**D.** hedge risks.

E. enhance their balance sheets.

Firms may use forward contracts and futures to protect against currency fluctuations or changes in commodity prices. Interest-rate options help companies control financing costs.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Derivatives general*

23. Financial assets permit all of the following except

A. consumption timing.

B. allocation of risk.

C. separation of ownership and control.

**D.** elimination of risk.

Financial assets do not allow risk to be eliminated. However, they do permit allocation of risk, consumption timing, and separation of ownership and control.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Real and financial assets*

24. The \_\_\_\_\_\_\_\_\_\_\_\_ refers to the potential conflict between management and shareholders.

**A.** agency problem

B. diversification problem

C. liquidity problem

D. solvency problem

E. regulatory problem

The agency problem describes potential conflict between management and shareholders. The other problems are those of firm management only.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Agency problems and issues*

25. A disadvantage of using stock options to compensate managers is that

A. it encourages managers to undertake projects that will increase stock price.

B. it encourages managers to engage in empire building.

**C.** it can create an incentive for managers to manipulate information to prop up a stock price temporarily, giving them a chance to cash out before the price returns to a level reflective of the firm's true prospects.

D. All of the above.

Encouraging managers to undertake projects that will increase stock price is a desired characteristic. Encouraging managers to engage in empire building is not necessarily a good or bad thing in and of itself. Creating an incentive for managers to manipulate information to prop up a stock price temporarily creates an agency problem.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Employee stock options*

26. Which of the following are mechanisms that have evolved to mitigate potential agency problems?

I) Using the firm's stock options for compensation

II) Hiring bickering family members as corporate spies

III) Boards of directors forcing out underperforming management

IV) Security analysts monitoring the firm closely

V) Takeover threats

A. II and V

B. I, III, and IV

**C.** I, III, IV, and V

D. III, IV, and V

E. I, III, and V

All the options except hiring bickering family members as corporate spies have been used to try to limit agency problems.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 2 Intermediate
Topic: Agency problems and issues*

27. Corporate shareholders are best protected from incompetent management decisions by

A. the ability to engage in proxy fights.

B. management's control of pecuniary rewards.

C. the ability to call shareholder meetings.

**D.** the threat of takeover by other firms.

E. one-share/one-vote election rules.

Proxy fights are expensive and seldom successful, and management may often control the board or own significant shares. It is the threat of takeover of underperforming firms that has the strongest ability to keep management on their toes.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 2 Intermediate
Topic: Agency problems and issues*

28. Theoretically, takeovers should result in

A. improved management.

B. increased stock price.

C. increased benefits to existing management of the taken-over firm.

**D.** improved management and increased stock price.

E. All of the options.

Theoretically, when firms are taken over, better managers come in and thus increase the price of the stock; existing management often must either leave the firm, be demoted, or suffer a loss of existing benefits.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Agency problems and issues*

29. During the period between 2000 and 2002, a large number of scandals were uncovered. Most of these scandals were related to

I) manipulation of financial data to misrepresent the actual condition of the firm.
II) misleading and overly optimistic research reports produced by analysts.
III) allocating IPOs to executives as a quid pro quo for personal favors.
IV) greenmail.

A. II, III, and IV

B. I, II, and IV

C. II and IV

D. I, III, and IV

**E.** I, II, and III

I, II, and III are all mentioned as causes of recent scandals.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 2 Intermediate
Topic: Ethics and corporate governance*

30. The Sarbanes-Oxley Act

A. requires corporations to have more independent directors.

B. requires the firm's CFO to personally vouch for the firm's accounting statements.

C. prohibits auditing firms from providing other services to clients.

D. requires corporations to have more independent directors and requires the firm's CFO to personally vouch for the firm's accounting statements.

**E.** All of the above.

The Sarbanes-Oxley Act does all of the above.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Financial market regulation and protections*

31. Asset allocation refers to

A. choosing which securities to hold based on their valuation.

B. investing only in "safe" securities.

**C.** the allocation of assets into broad asset classes.

D. bottom-up analysis.

Asset allocation refers to the allocation of assets into broad asset classes.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Asset allocation and security selection*

32. Security selection refers to

**A.** choosing which securities to hold based on their valuation.

B. investing only in "safe" securities.

C. the allocation of assets into broad asset classes.

D. top-down analysis.

Security selection refers to choosing which securities to hold based on their valuation.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Asset allocation and security selection*

33. Which of the following portfolio construction methods starts with security analysis?

A. Top-down

**B.** Bottom-up

C. Middle-out

D. Buy and hold

E. Asset allocation

Bottom-up refers to using security analysis to find securities that are attractively priced. Top-down refers to using asset allocation as a starting point.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Portfolio construction*

34. Which of the following portfolio construction methods starts with asset allocation?

**A.** Top-down

B. Bottom-up

C. Middle-out

D. Buy and hold

E. Asset allocation

Bottom-up refers to using security analysis to find securities that are attractively priced.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 2 Intermediate
Topic: Portfolio construction*

35. \_\_\_\_\_\_\_ are examples of financial intermediaries.

A. Commercial banks

B. Insurance companies

C. Investment companies

D. Credit unions

**E.** All of the options

All are institutions that bring borrowers and lenders together.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

36. Financial intermediaries exist because small investors cannot efficiently

A. diversify their portfolios.

B. assess credit risk of borrowers.

C. advertise for needed investments.

D. diversify their portfolios and assess credit risk of borrowers.

**E.** All of the options.

The individual investor cannot efficiently and effectively perform any of the tasks above without more time and knowledge than that available to most individual investors.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

37. \_\_\_\_\_\_\_\_ specialize in helping companies raise capital by selling securities.

A. Commercial bankers

**B.** Investment bankers

C. Investment issuers

D. Credit raters

An important role of investment banking is to act as middlemen in helping firms place new issues in the market.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

38. Commercial banks differ from other businesses in that both their assets and their liabilities are mostly

A. illiquid.

**B.** financial.

C. real.

D. owned by the government.

E. regulated.

See Table 1.3.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

39. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant financial asset(s) of U.S. commercial banks in terms of total value.

**A.** loans and leases

B. cash

C. real estate

D. deposits

E. investment securities

See Table 1.3.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

40. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant liability(ies) of U.S. commercial banks in terms of total value.

A. loans and leases

B. cash

C. real estate

**D.** deposits

E. investment securities

See Table 1.3.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

41. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the most significant real asset(s) of U.S. nonfinancial businesses in terms of total value.

A. equipment and software

B. inventory

**C.** real estate

D. trade credit

E. marketable securities

See Table 1.4.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

42. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant real asset(s) of U.S. nonfinancial businesses in terms of total value.

A. equipment and software

**B.** inventory

C. real estate

D. trade credit

E. marketable securities

See Table 1.4.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

43. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant liability(ies) of U.S. nonfinancial businesses in terms of total value.

A. bonds and mortgages

**B.** bank loans

C. inventories

D. trade debt

E. marketable securities

See Table 1.4.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Debt financing*

44. In terms of total value, the most significant liability(ies) of U.S. nonfinancial businesses in 2016 was(were)

A. bank loans.

**B.** bonds and mortgages.

C. trade debt.

D. other loans.

E. marketable securities.

See Table 1.4.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Debt financing*

45. In 2016, \_\_\_\_\_\_\_\_\_\_\_\_ was(were) the least significant financial asset(s) of U.S. nonfinancial businesses in terms of total value.

A. cash and deposits

B. trade credit

C. trade debt

D. inventory

**E.** marketable securities

See Table 1.4.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Real and financial assets*

46. New issues of securities are sold in the \_\_\_\_\_\_\_\_ market(s).

**A.** primary

B. secondary

C. over-the-counter

D. primary and secondary

New issues of securities are sold in the primary market.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Primary and secondary markets*

47. Investors trade previously issued securities in the \_\_\_\_\_\_\_\_ market(s).

A. primary

**B.** secondary

C. primary and secondary

D. derivatives

Investors trade previously issued securities in the secondary market.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Primary and secondary markets*

48. Investment bankers perform which of the following role(s)?

A. Market new stock and bond issues for firms

B. Provide advice to the firms as to market conditions, price, etc.

C. Design securities with desirable properties

**D.** All of the options

E. None of the options

Investment bankers perform all of the roles described above for their clients.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Financial intermediaries and market participants*

49. Until 1999, the \_\_\_\_\_\_\_\_ Act(s) prohibited banks in the United States from both accepting deposits and underwriting securities.

A. Sarbanes-Oxley

**B.** Glass-Steagall

C. SEC

D. Sarbanes-Oxley and SEC

E. None of the options

Until 1999, the Glass-Steagall Act prohibited banks in the United States from both accepting deposits and underwriting securities.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Financial market regulation and protections*

50. The spread between the LIBOR and the Treasury-bill rate is called the

A. term spread.

B. T-bill spread.

C. LIBOR spread.

**D.** TED spread.

The spread between the LIBOR and the Treasury-bill rate is called the TED spread.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Interest rates*

51. Mortgage-backed securities were created when \_\_\_\_\_\_\_\_ began buying mortgage loans from originators and bundling them into large pools that could be traded like any other financial asset.

A. GNMA

B. FNMA

C. FHLMC

**D.** FNMA and FHLMC

E. GNMA and FNMA

Mortgage-backed securities were created when FNMA and FHLMC began buying mortgage loans from originators and bundling them into large pools that could be traded like any other financial asset.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: 1 Basic
Topic: Mortgage securities and issues*

52. The sale of a mortgage portfolio by setting up mortgage pass-through securities is an example of

A. credit enhancement.

**B.** credit swap.

C. unbundling.

D. derivatives.

The financial asset is secured by the mortgages backing the instrument.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Mortgage securities and issues*

53. Which of the following is true about mortgage-backed securities?

I) They aggregate individual home mortgages into homogeneous pools.
II) The purchaser receives monthly interest and principal payments received from payments made on the pool.
III) The banks that originated the mortgages maintain ownership of them.
IV) The banks that originated the mortgages may continue to service them.

A. II, III, and IV

**B.** I, II, and IV

C. II and IV

D. I, III, and IV

E. I, II, III, and IV

III is not correct because the bank no longer owns the mortgage investments.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 2 Intermediate
Topic: Mortgage securities and issues*

54. \_\_\_\_\_\_\_\_ were designed to concentrate the credit risk of a bundle of loans on one class of investor, leaving the other investors in the pool relatively protected from that risk.

A. Stocks

B. Bonds

C. Derivatives

**D.** Collateralized debt obligations

E. All of the options

Collateralized debt obligations were designed to concentrate the credit risk of a bundle of loans on one class of investor, leaving the other investors in the pool relatively protected from that risk.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Collateralized mortgage obligations*

55. \_\_\_\_\_\_\_\_ are, in essence, an insurance contract against the default of one or more borrowers.

**A.** Credit default swaps

B. CMOs

C. ETFs

D. Collateralized debt obligations

E. All of the options

Credit default swaps are in essence an insurance contract against the default of one or more borrowers.

*AACSB: Reflective Thinking
Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: 1 Basic
Topic: Swaps*

**Chapter 01 Test Bank - Static Summary**

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| --- | --- |
| *Category* | *# of Questions* |
| AACSB: Reflective Thinking | 55 |
| Accessibility: Keyboard Navigation | 55 |
| Blooms: Remember | 43 |
| Blooms: Understand | 12 |
| Difficulty: 1 Basic | 40 |
| Difficulty: 2 Intermediate | 15 |
| Topic: Agency problems and issues | 4 |
| Topic: Asset allocation and security selection | 2 |
| Topic: Collateralized mortgage obligations | 1 |
| Topic: Debt financing | 3 |
| Topic: Derivatives - general | 3 |
| Topic: Employee stock options | 1 |
| Topic: Ethics and corporate governance | 1 |
| Topic: Financial intermediaries and market participants | 7 |
| Topic: Financial market regulation and protections | 2 |
| Topic: Fixed-income securities | 2 |
| Topic: Interest rates | 1 |
| Topic: Money market securities | 1 |
| Topic: Mortgage securities and issues | 3 |
| Topic: Portfolio construction | 2 |
| Topic: Primary and secondary markets | 2 |
| Topic: Real and financial assets | 19 |
| Topic: Swaps | 1 |