

Chapter 02 Asset Classes and Financial Instruments

Multiple Choice Questions

1. Which of the following is not a money market instrument?
 - A. Treasury bill
 - B. Commercial paper
 - C. Preferred stock
 - D. Banker's acceptance

2. Thirteen week T-bill auctions are conducted _____.
 - A. daily
 - B. weekly
 - C. monthly
 - D. quarterly

3. When computing the bank discount yield you would use ____ days in the year.
 - A. 260
 - B. 360
 - C. 365
 - D. 366

4. A dollar denominated deposit at a London bank is called _____.
 - A. eurodollars
 - B. LIBOR
 - C. fed funds
 - D. banker's acceptance

5. Money market securities are sometimes referred to as "cash equivalent" because _____.
 - A. they are safe and marketable
 - B. they are not liquid
 - C. they are high risk
 - D. they are low denomination

6. The most actively traded money market security is

- A. Treasury bills
- B. Bankers' Acceptances
- C. Certificates of Deposit
- D. Common stock

7. _____ voting of common stock gives minority shareholders the most representation on the board of directors.

- A. Majority
- B. Cumulative
- C. Rights
- D. Proxy

8. An investor in a T-bill earns interest by _____.

- A. receiving interest payments every 90 days
- B. receiving dividend payments every 30 days
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- D. buying the bill at a discount from the face value received at maturity

9. _____ would not be included in the EAFE index.

- A. Australia
- B. Canada
- C. France
- D. Japan

10. _____ is considered to be an emerging market country.

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- B. Norway
- C. Brazil
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11. Which one of the following is a true statement?
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 - C. greater than the ask price of the treasury bill expressed in dollar terms
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13. The German stock market is measured by which market index?
- A. FTSE
 - B. Dow Jones 30
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 - D. Nikkei
14. Deposits of commercial banks at the Federal Reserve are called _____.
- A. bankers acceptances
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15. Which of the following is not a true statement regarding municipal bonds?
- A. A municipal bond is a debt obligation issued by state or local governments.
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 - C. The interest income from a municipal bond is exempt from federal income taxation.
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16. Which of the following is not a characteristic of a money market instrument?

- A. Liquidity
- B. Marketability
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17. An individual who goes short in a futures position

- A. commits to delivering the underlying commodity at contract maturity
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18. Which of the following is not a nickname for an agency associated with the mortgage markets?

- A. Fannie Mae
- B. Freddie Mac
- C. Sallie Mae
- D. Ginnie Mae

19. Commercial paper is a short-term security issued by _____ to raise funds.

- A. the Federal Reserve
- B. commercial banks
- C. large well-known companies
- D. the New York Stock Exchange

20. The maximum maturity on commercial paper is

- A. 270 days
- B. 180 days
- C. 90 days
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21. Which one of the following is a true statement regarding the Dow Jones Industrial Average?
- A. It is a value-weighted average of 30 large industrial stocks
 - B. It is a price-weighted average of 30 large industrial stocks
 - C. It is a price-weighted average of 100 large stocks traded on the New York Stock Exchange
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- A. I only
 - B. I and II only
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24. A bond that has no collateral is called _____.
- A. a callable bond
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 - C. a junk bond
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25. A _____ gives its holder the right to sell an asset for a specified exercise price on or before a specified expiration date.
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26. A T-bill quote sheet has 90 day T-bill quotes with a 4.92 bid and a 4.86 ask. If the bill has a \$10,000 face value an investor could buy this bill for

- A. \$10,000.00
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27. Which one of the following is a true statement regarding corporate bonds?

- A. A corporate callable bond gives its holder the right to exchange it for a specified number of the company's common shares
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- C. A corporate convertible bond gives its holder the right to exchange it for a specified number of the company's common shares
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28. The yield on tax-exempt bonds is _____.

- A. usually less than 50% of the yield on taxable bonds
- B. normally about 90% of the yield on taxable bonds
- C. greater than the yield on taxable bonds
- D. less than the yield on taxable bonds

29. _____ is not a money market instrument.

- A. A certificate of deposit
- B. A treasury bill
- C. A treasury bond
- D. Commercial paper

30. An investor buys a T-bill at a bank discount quote of 4.80 with 150 days to maturity. The investor's actual annual rate of return on this investment was _____.

- A. 4.80%
- B. 4.97%
- C. 5.47%
- D. 5.74%

31. The U.K. stock index is the _____.

- A. DAX
- B. FTSE
- C. GSE
- D. TSE

32. A _____ gives its holder the right to buy an asset for a specified exercise price on or before a specified expiration date.

- A. call option
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33. Which one of the following provides the best example of securitization?

- A. convertible bond
- B. call option
- C. mortgage pass-through security
- D. preferred stock

34. Which of the following indices are market-value weighted?

- I. The NYSE Composite
 - II. The S&P 500
 - III. The Wilshire 5000
- A. I and II only
 - B. II and III only
 - C. I and III only
 - D. I, II and III

35. The interest rate charged by large banks in London to lend money among themselves is called _____.

- A. the prime rate
- B. the discount rate
- C. the federal funds rate
- D. LIBOR

36. A firm that has large securities holdings that wishes to raise money for a short length of time may be able to find the cheapest financing from which of the following?

- A. Reverse repurchase agreement
- B. Banker's acceptance
- C. Commercial paper
- D. Repurchase agreement

37. Currently the Dow Jones Industrial Average is computed by _____.

- A. adding the prices of 30 large "blue-chip" stocks and dividing by 30
- B. calculating the total market value of the 30 firms in the index and dividing by 30
- C. measuring the current total market value of the 30 stocks in the index relative to the total value on the previous day
- D. adding the prices of 30 large "blue-chip" stocks and dividing by a divisor adjusted for stock splits and large stock dividends

38. An investor purchases one municipal and one corporate bond that pay rates of return of 5.00% and 6.40% respectively. If the investor is in the 15% tax bracket, his after tax rates of return on the municipal and corporate bonds would be respectively

- A. 5.00% and 6.40%
- B. 5.00% and 5.44%
- C. 4.25% and 6.40%
- D. 5.75% and 5.44%

39. If a treasury note has a bid price of \$996.25, the quoted bid price in the Wall Street Journal would be _____.

- A. 99:25
- B. 99:63
- C. 99:20
- D. 99:08

40. TIPS are _____.
- A. Treasury bonds that pay a variable rate of interest
 - B. U.K. bonds that protect investors from default risk
 - C. securities that trade on the Toronto stock index
 - D. Treasury bonds that protect investors from inflation
41. The price quotations of treasury bonds in the Wall Street Journal show a bid price of 102:12 and an ask price of 102:14. If you sold the bond you expect to receive _____.
- A. \$1,024.75
 - B. \$1,024.38
 - C. \$1,023.75
 - D. \$1,022.50
42. The Dow Jones Industrial Average is _____.
- A. a price weighted average
 - B. a value weight and average
 - C. an equally weighted average
 - D. an unweighted average
43. Investors will earn higher rates of returns on TIPS than equivalent default risk standard bonds if _____.
- A. inflation is lower than anticipated over the investment period
 - B. inflation is higher than anticipated over the investment period
 - C. the U.S. dollar increases in value against the euro
 - D. the spread between commercial paper and Treasury securities remains low
44. Preferred stock is like long-term debt in that _____.
- A. it gives the holder voting power regarding the firm's management
 - B. it promises to pay to its holder a fixed stream of income each year
 - C. the preferred dividend is a tax-deductible expense for the firm
 - D. in the event of bankruptcy preferred stock has equal status with debt

45. Which of the following does not approximate the performance of a buy and hold portfolio strategy?

- A. An equally weighted index
- B. A price weighted index
- C. A value weighted index
- D. Weights are not a factor in this situation

46. In calculating the Dow Jones Industrial Average, the adjustment for a stock split occurs _____.

- A. automatically
- B. by adjusting the divisor
- C. by adjusting the numerator
- D. by adjusting the market value weights

47. If the market prices of the 30 stocks in the Dow Jones Industrial Average all change by the same dollar amount on a given day, assuming there are no stock splits which stock will have the greatest impact on the average?

- A. The one with the highest price
- B. The one with the lowest price
- C. All 30 stocks will have the same impact
- D. The answer cannot be determined by the information given

48. A bond issued by the State of Alabama is priced to yield 6.25%. If you are in the 28% tax bracket this bond would provide you with an equivalent taxable yield of _____.

- A. 4.50%
- B. 7.25%
- C. 8.68%
- D. none of the above

49. The purchase of a futures contract gives the buyer _____.

- A. the right to buy an item at a specified price
- B. the right to sell an item at a specified price
- C. the obligation to buy an item at a specified price
- D. the obligation to sell an item at a specified price

50. Ownership of a put option entitles the owner to the _____ to _____ a specific stock, on or before a specific date, at a specific price.

- A. right, buy
- B. right, sell
- C. obligation, buy
- D. obligation, sell

51. An investor in a 28% tax bracket is trying to decide whether to invest in a municipal bond or a corporate bond. She looks up municipal bond yields (r_m) but wishes to calculate the taxable equivalent yield r . The formula she should use is given by _____.

- A. $r = r_m * (1 - 28\%)$
- B. $r = r_m / (1 - 72\%)$
- C. $r = r_m * (1 - 72\%)$
- D. $r = r_m / (1 - 28\%)$

52. June call and put options on King Books Inc are available with exercise prices of \$30, \$35 and \$40. Among the different exercise prices, the call option with the _____ exercise price and the put option with the _____ exercise price will have the greatest value.

- A. \$40; \$30
- B. \$30; \$40
- C. \$35; \$35
- D. \$40; \$40

53. Ownership of a call option entitles the owner to the _____ to _____ a specific stock, on or before a specific date, at a specific price.

- A. right, buy
- B. right, sell
- C. obligation, buy
- D. obligation, sell

54. The _____ the ratio of municipal bond yields to corporate bond yields the _____ the cutoff tax bracket where more individuals will prefer to hold municipal debt.

- A. higher; lower
- B. lower; lower
- C. lower; higher
- D. higher; higher

55. Which of the following types of bonds are excluded from most bond indices?

- A. Corporate bonds
- B. Junk bonds
- C. Municipal bonds
- D. None of the above

56. The Hang Seng index reflects market performance on which of the following major stock markets?

- A. Japan
- B. Singapore
- C. Taiwan
- D. Hong Kong

57. The Standard and Poors 500 is a(n) _____ weighted index.

- A. equally
- B. price
- C. value
- D. share

58. A firm that fails to pay dividends on its preferred stock is said to be _____.

- A. insolvent
- B. in arrears
- C. insufferable
- D. delinquent

59. Large well-known companies often issue their own short term unsecured debt notes directly to the public, rather than borrowing from banks, their notes are called _____.

- A. certificates of deposit
- B. repurchase agreements
- C. banker's acceptances
- D. commercial paper

60. Which of the following is most like a short-term collateralized loan?

- A. Certificate of deposit
- B. Repurchase agreement
- C. Banker's acceptance
- D. Commercial paper

61. Eurodollars are _____.

- A. dollar denominated deposits at any foreign bank or foreign branch of an American bank
- B. dollar denominated bonds issued by firms outside their home market
- C. currency issued by Euro Disney and traded in France
- D. dollars that wind up in banks as a result of money laundering activities

62. Which of the following is used to back international sales of goods and services?

- A. Certificate of deposit
- B. Banker's acceptance
- C. Eurodollar deposits
- D. Commercial paper

63. Treasury notes have initial maturities between _____ years.

- A. 2 and 4
- B. 5 and 10
- C. 10 and 30
- D. 1 and 10

64. Which of the following are not characteristic of common stock ownership?
- A. Residual claimant
 - B. Unlimited liability
 - C. Voting rights
 - D. Limited life of the security
65. If you thought prices of stock would be rising over the next few months you may wish to _____ on the stock.
- A. purchase a call option
 - B. purchase a put option
 - C. sell a futures contract
 - D. place a short sale order
66. A typical bond price quote includes all but which one of the following?
- A. Daily high price for the bond
 - B. Closing bond price
 - C. Yield to maturity
 - D. Dividend yield
67. What are business firms most likely to use derivative securities for?
- A. Hedging
 - B. Speculating
 - C. Doing calculus problems
 - D. Market making
68. What would you expect to have happened to the spread between yields on commercial paper and Treasury bills immediately after September 11, 2001?
- A. No change, as both yields will remain the same.
 - B. Increase, the spread usually increases in response to a crisis.
 - C. Decrease, the spread usually decreases in response to a crisis.
 - D. No change, as both yields will move in the same direction.

69. A stock quote indicates a stock price of \$60 and a dividend yield of 3%. The latest quarterly dividend received by stock investors must have been _____ per share.

- A. \$0.55
- B. \$1.80
- C. \$0.45
- D. \$1.25

70. Three stocks have share prices of \$12, \$75, and \$30 with total market values of \$400 million, \$350 million and \$150 million respectively. If you were to construct a price-weighted index of the three stocks what would be the index value?

- A. 300
- B. 39
- C. 43
- D. 30

71. Which of the following is not considered a money market investment?

- A. Bankers acceptances
- B. Eurodollar
- C. Repurchase agreement
- D. Treasury note

72. The Federal Reserve Board of Governors directly controls which of the following interest rates?

- A. Bankers acceptances
- B. Brokers call
- C. Federal funds
- D. LIBOR

73. You decide to purchase an equal number of shares of stocks of firms to create a portfolio. If you wished to construct an index to track your portfolio performance your best match for your portfolio would be to construct a/an _____.

- A. value weighted index
- B. equal weighted index
- C. price weighted index
- D. bond price index

74. In a _____ index changes in the value of the stock with the greatest market value will move the index value the most everything else equal.

- A. value weighted index
- B. equal weighted index
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75. A corporation in a 34% tax bracket invests in the preferred stock of another company and earns a 6% pre-tax rate of return. An individual investor in a 15% tax bracket invests in the same preferred stock and earns the same pre-tax return. The after tax return to the corporation is _____ and the after tax return to the individual investor is _____.

- A. 3.96%; 5.1%
- B. 5.39%; 5.1%
- C. 6.00%; 6.00%
- D. 3.96%; 6.00%

76. All but which one of the following indices is value weighted?

- A. Nasdaq Composite
- B. S&P 500
- C. Wilshire 5000
- D. DJIA

77. What is the tax exempt equivalent yield on a 9% bond yield given a marginal tax rate of 28%?

- A. 6.48%
- B. 7.25%
- C. 8.02%
- D. 9.00%

78. A tax free municipal bond provides a yield of 3.2%. What is the equivalent taxable yield on the bond given a 35% tax bracket?

- A. 3.20%
- B. 3.68%
- C. 4.92%
- D. 5.00%

79. An index computed from a simple average of returns is a/an _____.

- A. equal weighted index
- B. value weighted index
- C. price weighted index
- D. share weighted index

80. A tax free municipal bond provides a yield of 2.34%. What is the equivalent taxable yield on the bond given a 28% tax bracket?

- A. 2.34%
- B. 2.68%
- C. 3.25%
- D. 4.92%

81. The Chompers Index is a price weighted stock index based on the 3 largest fast food chains. The stock prices for the three stocks are \$54, \$23, and \$44. What is the price weighted index value of the Chompers Index?

- A. 23.43
- B. 35.36
- C. 40.33
- D. 49.58

82. The Hydro Index is a price weighted stock index based on the 5 largest boat manufacturers in the nation. The stock prices for the five stocks are \$10, \$20, \$80, \$50 and \$40. The price of the last stock was just split 2 for 1 and the stock price was halved from \$40 to \$20. What is the new divisor for a price weighted index?

- A. 5.00
- B. 4.85
- C. 4.50
- D. 4.75

83. A benchmark index has three stocks priced at \$23, \$43, and \$56. The number of outstanding shares for each is 350,000 shares, 405,000 shares, and 553,000 shares, respectively. If the market value weighted index was 970 yesterday and the prices changed to \$23, \$41, and \$58, what is the new index value?

- A. 960
- B. 970
- C. 975
- D. 985

84. A benchmark market value index is comprised of three stocks. Yesterday the three stocks were priced at \$12, \$20, and \$60. The number of outstanding shares for each is 600,000 shares, 500,000 shares, and 200,000 shares, respectively. If the stock prices changed to \$16, \$18, and \$62 today respectively, what is the one day rate of return on the index?

- A. 5.78%
- B. 4.35%
- C. 6.16%
- D. 7.42%

85. Which of the following mortgage scenarios will benefit the homeowner the most?

- A. Adjustable rate mortgage when interest rate increases.
- B. Fixed rate mortgage when interest rates falls.
- C. Fixed rare mortgage when interest rate rises.
- D. None of the above, as banker's interest will always be protected.

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Difficulty: Easy

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$$\$9878.50 = \$10,000 \times \left[1 - \frac{(0.0486 \times 90)}{360} \right]$$

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$$\$9800 = \$10,000 \times \left[1 - \frac{(0.0480 \times 150)}{360} \right] \quad \left(\frac{\$10,000}{9800} - 1 \right) \times \frac{365}{150} = 4.97\%$$

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- A. convertible bond
- B. call option
- C. mortgage pass-through security**
- D. preferred stock

Difficulty: Easy

34. Which of the following indices are market-value weighted?

- I. The NYSE Composite
 - II. The S&P 500
 - III. The Wilshire 5000
- A. I and II only
 - B. II and III only
 - C. I and III only
 - D. I, II and III**

Difficulty: Easy

35. The interest rate charged by large banks in London to lend money among themselves is called _____.

- A. the prime rate
- B. the discount rate
- C. the federal funds rate
- D. LIBOR**

Difficulty: Easy

36. A firm that has large securities holdings that wishes to raise money for a short length of time may be able to find the cheapest financing from which of the following?

- A. Reverse repurchase agreement
- B. Banker's acceptance
- C. Commercial paper
- D. Repurchase agreement**

Difficulty: Hard

37. Currently the Dow Jones Industrial Average is computed by _____.
- A. adding the prices of 30 large "blue-chip" stocks and dividing by 30
 - B. calculating the total market value of the 30 firms in the index and dividing by 30
 - C. measuring the current total market value of the 30 stocks in the index relative to the total value on the previous day
 - D.** adding the prices of 30 large "blue-chip" stocks and dividing by a divisor adjusted for stock splits and large stock dividends

Difficulty: Hard

38. An investor purchases one municipal and one corporate bond that pay rates of return of 5.00% and 6.40% respectively. If the investor is in the 15% tax bracket, his after tax rates of return on the municipal and corporate bonds would be respectively
- A. 5.00% and 6.40%
 - B.** 5.00% and 5.44%
 - C. 4.25% and 6.40%
 - D. 5.75% and 5.44%

After-tax return on municipal bond = .05

After-tax return on corporate bond = $.064(1 - .15) = 0.0544 = 5.44\%$

Difficulty: Medium

39. If a treasury note has a bid price of \$996.25, the quoted bid price in the Wall Street Journal would be _____.
- A. 99:25
 - B. 99:63
 - C.** 99:20
 - D. 99:08

$$\text{Quoted Price} = 996.25 \left(\frac{100}{1,000} \right) = 99.625 = 99 + \left(0.625 \times \frac{32}{32} \right) = 99 \frac{20}{32} = 99 : 20$$

Difficulty: Medium

40. TIPS are _____.

- A. Treasury bonds that pay a variable rate of interest
- B. U.K. bonds that protect investors from default risk
- C. securities that trade on the Toronto stock index
- D. Treasury bonds that protect investors from inflation**

Difficulty: Medium

41. The price quotations of treasury bonds in the Wall Street Journal show a bid price of 102:12 and an ask price of 102:14. If you sold the bond you expect to receive _____.

- A. \$1,024.75
- B. \$1,024.38
- C. \$1,023.75**
- D. \$1,022.50

$$P = \left(102 + \frac{12}{32} \right) \times \left(\frac{1,000}{100} \right) = 1,023.75$$

Difficulty: Medium

42. The Dow Jones Industrial Average is _____.

- A. a price weighted average**
- B. a value weight and average
- C. an equally weighted average
- D. an unweighted average

Difficulty: Easy

43. Investors will earn higher rates of returns on TIPS than equivalent default risk standard bonds if _____.

- A. inflation is lower than anticipated over the investment period
- B.** inflation is higher than anticipated over the investment period
- C. the U.S. dollar increases in value against the euro
- D. the spread between commercial paper and Treasury securities remains low

Difficulty: Medium

44. Preferred stock is like long-term debt in that _____.

- A. it gives the holder voting power regarding the firm's management
- B.** it promises to pay to its holder a fixed stream of income each year
- C. the preferred dividend is a tax-deductible expense for the firm
- D. in the event of bankruptcy preferred stock has equal status with debt

Difficulty: Medium

45. Which of the following does not approximate the performance of a buy and hold portfolio strategy?

- A. An equally weighted index
- B. A price weighted index
- C.** A value weighted index
- D. Weights are not a factor in this situation

Difficulty: Medium

46. In calculating the Dow Jones Industrial Average, the adjustment for a stock split occurs _____.

- A. automatically
- B.** by adjusting the divisor
- C. by adjusting the numerator
- D. by adjusting the market value weights

Difficulty: Medium

47. If the market prices of the 30 stocks in the Dow Jones Industrial Average all change by the same dollar amount on a given day, assuming there are no stock splits which stock will have the greatest impact on the average?

- A. The one with the highest price
- B. The one with the lowest price
- C.** All 30 stocks will have the same impact
- D. The answer cannot be determined by the information given

Difficulty: Medium

48. A bond issued by the State of Alabama is priced to yield 6.25%. If you are in the 28% tax bracket this bond would provide you with an equivalent taxable yield of _____.

- A. 4.50%
- B. 7.25%
- C.** 8.68%
- D. none of the above

Difficulty: Medium Feedback: $8.68\% = 6.25\% / (1 - 0.28)$

49. The purchase of a futures contract gives the buyer _____.

- A. the right to buy an item at a specified price
- B. the right to sell an item at a specified price
- C.** the obligation to buy an item at a specified price
- D. the obligation to sell an item at a specified price

Difficulty: Easy

50. Ownership of a put option entitles the owner to the _____ to _____ a specific stock, on or before a specific date, at a specific price.

- A. right, buy
- B.** right, sell
- C. obligation, buy
- D. obligation, sell

Difficulty: Easy

51. An investor in a 28% tax bracket is trying to decide whether to invest in a municipal bond or a corporate bond. She looks up municipal bond yields (r_m) but wishes to calculate the taxable equivalent yield r . The formula she should use is given by _____.

- A. $r = r_m * (1 - 28\%)$
- B. $r = r_m / (1 - 72\%)$
- C. $r = r_m * (1 - 72\%)$
- D.** $r = r_m / (1 - 28\%)$

Difficulty: Hard

52. June call and put options on King Books Inc are available with exercise prices of \$30, \$35 and \$40. Among the different exercise prices, the call option with the _____ exercise price and the put option with the _____ exercise price will have the greatest value.

- A. \$40; \$30
- B.** \$30; \$40
- C. \$35; \$35
- D. \$40; \$40

Difficulty: Medium

53. Ownership of a call option entitles the owner to the _____ to _____ a specific stock, on or before a specific date, at a specific price.

- A.** right, buy
- B. right, sell
- C. obligation, buy
- D. obligation, sell

Difficulty: Easy

54. The _____ the ratio of municipal bond yields to corporate bond yields the _____ the cutoff tax bracket where more individuals will prefer to hold municipal debt.

- A.** higher; lower
- B. lower; lower
- C. lower; higher
- D. higher; higher

Difficulty: Hard

55. Which of the following types of bonds are excluded from most bond indices?

- A. Corporate bonds
- B.** Junk bonds
- C. Municipal bonds
- D. None of the above

Difficulty: Medium

56. The Hang Seng index reflects market performance on which of the following major stock markets?

- A. Japan
- B. Singapore
- C. Taiwan
- D.** Hong Kong

Difficulty: Medium

57. The Standard and Poors 500 is a(n) _____ weighted index.

- A. equally
- B. price
- C.** value
- D. share

Difficulty: Easy

58. A firm that fails to pay dividends on its preferred stock is said to be _____.
- A. insolvent
 - B. in arrears**
 - C. insufferable
 - D. delinquent

Difficulty: Medium

59. Large well-known companies often issue their own short term unsecured debt notes directly to the public, rather than borrowing from banks, their notes are called _____.
- A. certificates of deposit
 - B. repurchase agreements
 - C. banker's acceptances
 - D. commercial paper**

Difficulty: Easy

60. Which of the following is most like a short-term collateralized loan?
- A. Certificate of deposit
 - B. Repurchase agreement**
 - C. Banker's acceptance
 - D. Commercial paper

Difficulty: Medium

61. Eurodollars are _____.
- A. dollar denominated deposits at any foreign bank or foreign branch of an American bank**
 - B. dollar denominated bonds issued by firms outside their home market
 - C. currency issued by Euro Disney and traded in France
 - D. dollars that wind up in banks as a result of money laundering activities

Difficulty: Easy

62. Which of the following is used to back international sales of goods and services?

- A. Certificate of deposit
- B. Banker's acceptance**
- C. Eurodollar deposits
- D. Commercial paper

Difficulty: Medium

63. Treasury notes have initial maturities between _____ years.

- A. 2 and 4
- B. 5 and 10
- C. 10 and 30
- D. 1 and 10**

Difficulty: Easy

64. Which of the following are not characteristic of common stock ownership?

- A. Residual claimant
- B. Unlimited liability**
- C. Voting rights
- D. Limited life of the security

Difficulty: Easy

65. If you thought prices of stock would be rising over the next few months you may wish to _____ on the stock.

- A. purchase a call option**
- B. purchase a put option
- C. sell a futures contract
- D. place a short sale order

Difficulty: Medium

66. A typical bond price quote includes all but which one of the following?

- A. Daily high price for the bond
- B. Closing bond price
- C. Yield to maturity
- D. Dividend yield**

Difficulty: Easy

67. What are business firms most likely to use derivative securities for?

- A. Hedging**
- B. Speculating
- C. Doing calculus problems
- D. Market making

Difficulty: Medium

68. What would you expect to have happened to the spread between yields on commercial paper and Treasury bills immediately after September 11, 2001?

- A. No change, as both yields will remain the same.
- B. Increase, the spread usually increases in response to a crisis.**
- C. Decrease, the spread usually decreases in response to a crisis.
- D. No change, as both yields will move in the same direction.

Difficulty: Hard

69. A stock quote indicates a stock price of \$60 and a dividend yield of 3%. The latest quarterly dividend received by stock investors must have been _____ per share.

- A. \$0.55
- B. \$1.80
- C. \$0.45**
- D. \$1.25

$$\frac{\$60 \times 0.030}{4} = \$0.45$$

Difficulty: Medium

70. Three stocks have share prices of \$12, \$75, and \$30 with total market values of \$400 million, \$350 million and \$150 million respectively. If you were to construct a price-weighted index of the three stocks what would be the index value?

- A. 300
- B. 39**
- C. 43
- D. 30

$$Index = (12 + 75 + 30)/3 = 39$$

Difficulty: Medium

71. Which of the following is not considered a money market investment?

- A. Bankers acceptances
- B. Eurodollar
- C. Repurchase agreement
- D. Treasury note**

Difficulty: Easy

72. The Federal Reserve Board of Governors directly controls which of the following interest rates?

- A. Bankers acceptances
- B. Brokers call
- C. Federal funds**
- D. LIBOR

Difficulty: Easy

73. You decide to purchase an equal number of shares of stocks of firms to create a portfolio. If you wished to construct an index to track your portfolio performance your best match for your portfolio would be to construct a/an _____.

- A. value weighted index
- B. equal weighted index
- C. price weighted index**
- D. bond price index

Difficulty: Hard

74. In a _____ index changes in the value of the stock with the greatest market value will move the index value the most everything else equal.

- A. value weighted index**
- B. equal weighted index
- C. price weighted index
- D. bond price index

Difficulty: Medium

75. A corporation in a 34% tax bracket invests in the preferred stock of another company and earns a 6% pre-tax rate of return. An individual investor in a 15% tax bracket invests in the same preferred stock and earns the same pre-tax return. The after tax return to the corporation is _____ and the after tax return to the individual investor is _____.

- A. 3.96%; 5.1%
- B. 5.39%; 5.1%**
- C. 6.00%; 6.00%
- D. 3.96%; 6.00%

After-tax return to corporate investor after 70% exclusion = $0.06 - (0.06 * 0.30) * 0.34 = 5.39\%$

After-tax return to individual investor = $0.06 * (1 - 0.15) = 5.1\%$

Difficulty: Hard

76. All but which one of the following indices is value weighted?

- A. Nasdaq Composite
- B. S&P 500
- C. Wilshire 5000
- D. DJIA**

Difficulty: Easy

77. What is the tax exempt equivalent yield on a 9% bond yield given a marginal tax rate of 28%?

- A. 6.48%**
- B. 7.25%
- C. 8.02%
- D. 9.00%

after tax yield = $.09(1 - .28) = .0648$

Difficulty: Medium

78. A tax free municipal bond provides a yield of 3.2%. What is the equivalent taxable yield on the bond given a 35% tax bracket?

- A. 3.20%
- B. 3.68%
- C. 4.92%**
- D. 5.00%

$$\text{Yield} = \frac{.032}{1 - .35} = 0.0492$$

Difficulty: Medium

79. An index computed from a simple average of returns is a/an _____.

- A. equal weighted index**
- B. value weighted index
- C. price weighted index
- D. share weighted index

Difficulty: Medium

80. A tax free municipal bond provides a yield of 2.34%. What is the equivalent taxable yield on the bond given a 28% tax bracket?

- A. 2.34%
- B. 2.68%
- C. 3.25%**
- D. 4.92%

$$\text{Yield} = \frac{.0234}{1 - .28} = 0.0325$$

Difficulty: Medium

81. The Chompers Index is a price weighted stock index based on the 3 largest fast food chains. The stock prices for the three stocks are \$54, \$23, and \$44. What is the price weighted index value of the Chompers Index?

- A. 23.43
- B. 35.36
- C. 40.33**
- D. 49.58

$$\text{Index} = \frac{54 + 23 + 44}{3} = 40.33$$

Difficulty: Medium

82. The Hydro Index is a price weighted stock index based on the 5 largest boat manufacturers in the nation. The stock prices for the five stocks are \$10, \$20, \$80, \$50 and \$40. The price of the last stock was just split 2 for 1 and the stock price was halved from \$40 to \$20. What is the new divisor for a price weighted index?

- A. 5.00
- B. 4.85
- C. 4.50**
- D. 4.75

$$\text{Index}_0 = \frac{\$10 + \$20 + \$80 + \$50 + \$40}{5} = 40$$

$$\text{Index}_1 = \frac{\$10 + \$20 + \$80 + \$50 + \$20}{X} = 40; X = 4.50$$

Difficulty: Hard

Chapter 02 - Asset Classes and Financial Instruments

83. A benchmark index has three stocks priced at \$23, \$43, and \$56. The number of outstanding shares for each is 350,000 shares, 405,000 shares, and 553,000 shares, respectively. If the market value weighted index was 970 yesterday and the prices changed to \$23, \$41, and \$58, what is the new index value?

- A. 960
- B. 970
- C. 975**
- D. 985

$$\text{Index} = \frac{\$23 \times 350000 + \$41 \times 405000 + \$58 \times 553000}{\$23 \times 350000 + \$43 \times 405000 + \$56 \times 553000} \times 970 = 975$$

Difficulty: Hard

84. A benchmark market value index is comprised of three stocks. Yesterday the three stocks were priced at \$12, \$20, and \$60. The number of outstanding shares for each is 600,000 shares, 500,000 shares, and 200,000 shares, respectively. If the stock prices changed to \$16, \$18, and \$62 today respectively, what is the one day rate of return on the index?

- A. 5.78%
- B. 4.35%
- C. 6.16%**
- D. 7.42%

$$\text{Index return} = \left[\frac{\$16 \times 600000 + \$18 \times 500000 + \$62 \times 200000}{\$12 \times 600000 + \$20 \times 500000 + \$60 \times 200000} \right] - 1 = 6.164\%$$

Difficulty: Hard

85. Which of the following mortgage scenarios will benefit the homeowner the most?

- A. Adjustable rate mortgage when interest rate increases.
- B. Fixed rate mortgage when interest rates falls.
- C. Fixed rare mortgage when interest rate rises.**
- D. None of the above, as banker's interest will always be protected.

Difficulty: Medium