MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

1) Assume that you borrow $2000 at 10% annual interest to finance a new business project. For this loan to be profitable, the minimum amount this project must generate in annual earnings is
   A) $400.          B) $201.          C) $200.          D) $199.  

2) Which of the following can be described as direct finance?
   A) You take out a mortgage from your local bank.
   B) You buy shares in a mutual fund.
   C) You buy shares of common stock in the secondary market.
   D) You borrow $2500 from a friend.  

3) Well-functioning financial markets
   A) eliminate the need for indirect finance. 
   B) cause inflation.
   C) produce an efficient allocation of capital. 
   D) cause financial crises.  

4) Every financial market has the following characteristic:
   A) It determines the level of interest rates.
   B) It allows loans to be made.
   C) It allows common stock to be traded.
   D) It channels funds from lenders-savers to borrowers-spenders.  

5) When I purchase ________, I own a portion of a firm and have the right to vote on issues important to the firm and to elect its directors.
   A) stock     B) notes     C) bonds     D) bills  

6) Long-term debt has a maturity that is
   A) between five and ten years. 
   B) between one and ten years.
   C) ten years or longer.       D) less than a year.  

7) If the maturity of a debt instrument is less than one year, the debt is called

8) Which of the following benefit directly from any increase in the corporation’s profitability?
   A) a bond holder     B) a T-bill holder
   C) a shareholder     D) a commercial paper holder  

9) When an investment bank ________ securities, it guarantees a price for a corporation’s securities and then sells them to the public.
   A) underwrites    B) overwrites    C) overtakes    D) undertakes  

10) A financial market in which previously issued securities can be resold is called a ________ market.
    A) secondary     B) primary     C) tertiary     D) used securities
11) A corporation acquires new funds only when its securities are sold in the
   A) primary market by an investment bank.
   B) secondary market by a stock exchange broker.
   C) secondary market by a commercial bank.
   D) secondary market by an investment bank.

12) A liquid asset is
   A) a share of an ocean resort.
   B) always sold in an over-the-counter market.
   C) difficult to resell.
   D) an asset that can easily and quickly be sold to raise cash.

13) Equity instruments are traded in the ________ market.
   A) money               B) capital               C) commodities               D) bond

14) A financial market in which only short-term debt instruments are traded is called the ________ market.
    A) stock               B) bond               C) capital               D) money

15) Prices of money market instruments undergo the least price fluctuations because of
    A) the price ceiling imposed by government regulators.
    B) the lack of competition in the market.
    C) the heavy regulations in the industry.
    D) the short terms to maturity for the securities.

16) Equity of U.S. companies can be purchased by
    A) foreign citizens only.
    B) U.S. citizens only.
    C) U.S. mutual funds only.
    D) U.S. citizens and foreign citizens.

17) Bonds that are sold in a foreign country and are denominated in a currency other than that of the
    country in which it is sold are known as
    A) foreign bonds.
    B) country bonds.
    C) Eurobonds.
    D) equity bonds.

18) Bonds that are sold in a foreign country and are denominated in the country’s currency in which
    they are sold are known as
    A) equity bonds.
    B) Eurobonds.
    C) foreign bonds.
    D) country bonds.

19) U.S. dollar deposits in foreign banks outside the U.S. or in foreign branches of U.S. banks are called
    A) Atlantic dollars.
    C) Eurodollars.
    D) outside dollars.

20) In the United States, loans from ________ are far ________ important for corporate finance than are
    securities markets.
    A) financial intermediaries; less
    C) government agencies; less
    B) government agencies; more
    D) financial intermediaries; more

21) The process of indirect finance using financial intermediaries is called
    A) direct lending.
    C) financial liquidation.
    B) resource allocation.
    D) financial intermediation.
22) Financial institutions that accept deposits and make loans are called ________ institutions.
   A) contractual savings   B) depository
   C) investment            D) underwriting

23) Which of the following is a depository institution?
   A) A mutual fund
   B) A life insurance company
   C) A credit union
   D) A pension fund

24) The primary liabilities of a commercial bank are
   A) deposits.
   B) mortgages.
   C) commercial paper.
   D) bonds.

25) Which of the following is a contractual savings institution?
   A) A mutual fund
   B) A life insurance company
   C) A credit union
   D) A savings and loan association

26) Money market mutual fund shares function like
   A) currency.
   B) bonds.
   C) checking accounts that pay interest.
   D) stocks.

27) An investment bank helps ________ issue securities.
   A) foreign governments
   B) the SEC
   C) a corporation
   D) the United States government

28) Which of the following is not a goal of financial regulation?
   A) Reducing adverse selection
   B) Ensuring the soundness of the financial system
   C) Ensuring that investors never suffer losses
   D) Reducing moral hazard

29) Increasing the amount of information available to investors helps to reduce the problems of
   ________ and ________ in the financial markets.
   A) adverse selection; risk sharing
   B) moral hazard; transactions costs
   C) adverse selection; economies of scale
   D) adverse selection; moral hazard

30) U.S. Treasury bills pay no interest but are sold at a ________. That is, you will pay a lower
    purchase price than the amount you receive at maturity.
    A) collateral
    B) premium
    C) default
    D) discount

31) U.S. Treasury bills are considered the safest of all money market instruments because there is
    almost no risk of
    A) default.
    B) desertion.
    C) demarcation.
    D) defeat.

32) A debt instrument sold by a bank to its depositors that pays annual interest of a given amount and
    at maturity pays back the original purchase price is called
    A) federal funds.
    B) a negotiable certificate of deposit.
    C) a municipal bond.
    D) commercial paper.
33) A short-term debt instrument issued by well-known corporations is called
   A) commercial mortgages.         B) corporate bonds.
   C) municipal bonds.              D) commercial paper.

34) _______ are short-term loans in which Treasury bills serve as collateral.
   A) Federal funds                     B) U.S. government agency securities
   C) Repurchase agreements            D) Negotiable certificates of deposit

35) Collateral is _______ the lender receives if the borrower does not pay back the loan.
   A) an offering                         B) an asset
   C) a present                           D) a liability

36) Federal funds are
   A) loans made by banks to each other.
   B) loans made by banks to the Federal Reserve System.
   C) loans made by the Federal Reserve System to banks.
   D) funds raised by the federal government in the bond market.

37) The British Banker’s Association average of interbank rates for dollar deposits in the London market is called the
   A) federal funds rate.                     B) prime rate.
   C) Libor rate.                             D) Treasury Bill rate.

38) Which of the following are short-term financial instruments?
   A) A residential mortgage
   B) A Treasury note with a maturity of four years
   C) A share of Walt Disney Corporation stock
   D) A repurchase agreement

39) Which of the following instruments are traded in a money market?
   A) U.S. Treasury bills
   B) Corporate bonds
   C) U.S. government agency securities
   D) State and local government bonds

40) Which of the following instruments are traded in a money market?
   A) Residential mortgages
   B) Commercial paper
   C) Bank commercial loans
   D) State and local government bonds

41) Which of the following instruments is not traded in a money market?
   A) Residential mortgages
   B) Commercial paper
   C) U.S. Treasury Bills
   D) Negotiable bank certificates of deposit

42) Bonds issued by state and local governments are called _______ bonds.
   A) corporate                     B) Treasury
   C) commercial                   D) municipal

43) Equity and debt instruments with maturities greater than one year are called _______ market instruments.
   A) money                         B) capital
   C) federal                      D) benchmark

44) Which of the following is a long-term financial instrument?
   A) A U.S. Treasury bond
   B) A U.S. Treasury bill
   C) A repurchase agreement
   D) A negotiable certificate of deposit
45) Which of the following instruments are traded in a capital market?
A) Negotiable bank CDs  B) U.S. Government agency securities
C) Repurchase agreements  D) U.S. Treasury bills

46) Which of the following instruments are traded in a capital market?
A) Negotiable bank CDs  B) Corporate bonds
C) Repurchase agreements  D) U.S. Treasury bills

47) Which of the following are not traded in a capital market?
A) Corporate bonds  B) U.S. government agency securities
C) State and local government bonds  D) Repurchase agreements

48) The most liquid securities traded in the capital market are
A) mortgage-backed securities.  B) municipal bonds.
C) corporate bonds.  D) U.S. Treasury bonds.

49) Bonds that are sold in a foreign country and are denominated in a currency other than that of the country in which it is sold are known as
A) country bonds.  B) foreign bonds.
C) equity bonds.  D) Eurobonds.

50) Conflicts of interest are a type of _______ problem that can happen when an institution provides multiple services.
A) moral hazard  B) free-riding
C) adverse selection  D) discounting

51) The primary assets of a finance company are
A) municipal bonds.  B) consumer and business loans.
C) corporate stocks and bonds.  D) mortgages.

52) Savings and loan associations are regulated by the

53) When compared to exchange systems that rely on money, disadvantages of the barter system include:
A) lowering the cost of exchange to those who would specialize.
B) the requirement of a double coincidence of wants.
C) encouraging specialization and the division of labor.
D) lowering the cost of exchanging goods over time.

54) If the interest rates on all bonds rise from 5 to 6 percent over the course of the year, which bond would you prefer to have been holding?
A) A bond with twenty years to maturity  B) A bond with one year to maturity
C) A bond with five years to maturity  D) A bond with ten years to maturity

55) The global financial crisis lead to a decline in stock prices because
A) higher current dividends.
B) higher expected future stock prices.
C) of a lowered expected dividend growth rate.
D) of a lowered required return on investment in equity.
56) Although debt contracts require less monitoring than equity contracts, debt contracts are still subject to ______ since borrowers have an incentive to take on more risk than the lender would like.

A) agency theory  
B) the "lemons" problem  
C) moral hazard  
D) diversification

57) The economic hardship resulting from a financial crisis is severe, however, there are also social consequences such as

A) currency devaluations.  
B) loss of output.  
C) difficulty getting a loan.  
D) increased crime.

58) When you deposit $50 in your account at First National Bank and a $100 check you have written on this account is cashed at Chemical Bank, then

A) the reserves at First National fall by $50.  
B) the assets of First National rise by $50.  
C) the liabilities at Chemical Bank rise by $50.  
D) the assets of Chemical Bank rise by $50.

59) Depositors have a strong incentive to show up first to withdraw their funds during a bank crisis because banks operate on a

A) last-in, first-out constraint.  
B) everyone-shares-equally constraint.  
C) double-coincidence of wants constraint.  
D) sequential service constraint.

60) Allowing bank branching across state lines gives banks greater ability to coordinate bank operations. This makes it easier for them to receive the benefits of

A) economies of scale.  
B) interest-rate irregularities.  
C) the dual banking system.  
D) disintermediation.

61) Which of the following is a duty of the Board of Governors of the Federal Reserve System?

A) All governors advise the president of the United States on economic policy.  
B) Regulating credit with the approval of the president under the Credit Control Act of 1969.  
C) Setting the maximum interest rates payable on certain types of time deposits under Regulation Q.  
D) Setting margin requirements, the fraction of the purchase price of the securities that has to be paid for with cash.

62) Everything else held constant, an increase in the money market fund ratio will mean ______ in the M2 money multiplier and ______ in the M2 money supply.

A) a decrease; a decrease  
B) an increase; a decrease  
C) an increase; an increase  
D) a decrease; an increase

63) The time-inconsistency problem with monetary policy tells us that, if policymakers use discretionary policy, there is a higher probability that the ______ will be higher, compared to policy makers following a behavior rule.

A) interest rate  
B) foreign exchange rate  
C) unemployment rate  
D) inflation rate
64) When the effects of the global financial crisis started to spread more quickly throughout the rest of the world, the U.S. dollar ________ because demand for U.S. assets ________.
   A) depreciated; increased  B) depreciated; decreased  C) appreciated; decreased  D) appreciated; increased

65) The United States chooses to have ________ and ________ and therefore, cannot have a fixed exchange rate at the same time.
   A) capital control, an independent monetary policy  B) free capital mobility, an independent monetary policy  
   C) capital control, no control of monetary policy  D) free capital mobility, no control of monetary policy
Answer Key
Testname: UNTITLED1

1) B
2) D
3) C
4) D
5) A
6) C
7) C
8) C
9) A
10) A
11) A
12) D
13) B
14) D
15) D
16) D
17) C
18) C
19) C
20) D
21) D
22) B
23) C
24) A
25) B
26) C
27) C
28) C
29) D
30) D
31) A
32) B
33) D
34) C
35) B
36) A
37) C
38) D
39) A
40) B
41) A
42) D
43) B
44) A
45) B
46) B
47) D
48) D
49) D
50) A
Answer Key
Testname: UNTITLED1

51) B
52) A
53) B
54) B
55) C
56) C
57) D
58) A
59) D
60) A
61) D
62) C
63) D
64) D
65) B