Fundamentals of Investing 13th edition Smart Test Bank

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Fundamentals of Investing, 13e **(Smart)**
Chapter 2 Securities Markets and Transactions

2.1 Learning Goal 1

1) Stocks, bonds and mutual fund shares are bought and sold in the capital market.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

2) Capital markets deal exclusively in stock. Money markets deal exclusively in debt instruments.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

3) Primary markets deal in the stocks of larger, well-known companies; secondary markets deal in the stocks of smaller, less well-known companies.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

4) Short-term securities are bought and sold in the
A) capital market.
B) primary market.
C) money market.
D) stock market.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

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5) The governmental agency that oversees the capital markets is the
A) Federal Trade Commission.
B) Federal Reserve.
C) Securities and Exchange Commission.
D) Fair Trade and Banking Agency.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

6) Stocks purchased in the secondary market are purchased
A) directly from the issuing corporation.
B) from other investors.
C) from small, little-known brokerages.
D) indirectly through financial institutions.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

7) Stocks and bonds are traded in
A) securities and exchange commissions.
B) money markets.
C) federal trade commissions.
D) capital markets.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 1

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8) The primary market tends to be more active when
A) the economy is slowing and stock prices are falling.
B) the economy is expanding and stock prices are rising.
C) interest rates are rising.
D) early in the calendar year.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 1

2.2 Learning Goal 2

1) Underwriters are responsible for promoting and facilitating the sale of securities.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

2) The preliminary version of a prospectus is called a red herring.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

3) The purpose of the "quiet period" a company must observe from the time it files a registration statement with the SEC until after an IPO is complete is to assure that all investors receive the same information.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 2

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4) IPOs are typically underpriced so that the price rises during the first few days of trading.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

5) IPOs are relatively safe investments.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

6) The price of stock sold in an IPO is set by bids submitted in the month before trading begins.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 2

7) Which one of the following statements concerning the primary market is correct?
A) A transaction in the primary market is between two private stockholders.
B) The first public sale of a company's stock in the primary market is called a seasoned new issue.
C) The first public sale of a company's stock is called an IPO.
D) A rights offering is a direct sale of stock to an institution that participates in the primary market.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

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8) A rights offering is the
A) initial offering of securities to the public.
B) offering of new securities to current shareholders on a pro-rata basis.
C) sale of newly issued shares of stock to the general public.
D) sale of securities directly to a select group of investors.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

9) IPO activity tends to peak when stock prices
A) have fallen sharply.
B) have risen sharply.
C) are volatile and unstable.
D) Stock prices have relatively little influence on IPO activity.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 2

10) The document that describes the issuer of a security's management and financial position is known as a
A) balance sheet.
B) 10-K report.
C) prospectus.
D) red herring.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

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11) Companies offering their stock to the public for the first time usually seek the assistance of
A) investment bankers.
B) the Securities and Exchange Commission.
C) the Federal Reserve Bank.
D) prospectors.
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

12) The financial crisis of 2008 resulted in
A) a steep increase in the price of newly issued stock because supply was limited.
B) new regulations affecting initial public offerings.
C) a sharp reduction in the number of initial public offerings.
D) B and C, but not A.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 2

13) Investment bankers who join together to share the financial risk associated with buying an entire issue of new securities and reselling them to the public is called a(n)
A) selling group.
B) tombstone group.
C) underwriting syndicate.
D) primary market group.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

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14) Describe the initial public offering (IPO) process and explain the role of the underwriter, the Securities and Exchange Commission (SEC), and the red herring.
Answer: The underwriter is responsible for promoting the stock and facilitating the sale of the company's IPO shares. The SEC approves the registration statement including the prospectus. This statement includes the key aspects of the issue, the issuer, the company management, and the financial position of the company. The SEC does NOT recommend the investment nor offer an opinion on the value of the stock. The red herring is the preliminary prospectus issued on tentative offerings. The prospectus has red lettering on the front cover.
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 2

15) Explain the role of investment bankers and brokerage firms in the issuance of new securities.
Answer: An investment banker assumes the role of the underwriter and bears the risk of reselling the securities purchased from an issuing corporation. The investment banker earns a profit by reselling at a price higher than the price paid to the issuer. Brokerage firms form a selling group with each firm accepting responsibility for selling a portion of the newly issued securities. The brokerage firms also earn a profit if they can resell the shares at a price higher than their purchase price.
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
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Question Status: Previous Edition
Learning Goal: Learning Goal 2

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2.3 Learning Goal 3

1) The NYSE and AMEX are examples of dealer markets.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

2) Only U.S. corporations can list their stocks on the NYSE.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

3) Firms that list their stock on an exchange can be delisted for failing to meet the requirements of the exchange.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

4) The NYSE is part of the world's largest international trading network known as NYSE Euronext.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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5) Exchange traded funds (ETFs) perform like a broad market index but are bought and sold like individual stocks.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

6) Most commodity futures are traded on the NYSE Amex.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

7) Securities that trade in the over-the-counter market are called unlisted securities.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

8) A market maker brings together buyers and sellers in an auction market.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

9) The income paid to a market maker is referred to as the spread.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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10) Federal laws that control the sale of securities are called blue sky laws.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

11) Federal securities laws are designed to protect financial institutions.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

12) Stocks of many large foreign companies such as Toyota trade on the NYSE as well as on exchanges in their own country.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

13) The majority of bonds trade in the OTC market.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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14) Market makers in dealer markets
A) bring sellers and buyers together by matching offers.
B) earn commissions paid by the sellers of securities.
C) buy securities at a bid price and hope to resell them at a higher offer price.
D) all of the above.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

15) Which one of the following statements about the NYSE is correct?
A) Each member of the exchange owns a trading post.
B) Any listed stock may be traded at any of 20 trading posts.
C) Brokerage firms are only permitted to have one individual trading on the floor of the exchange.
D) Buy orders are filled at the lowest price and sell orders are filled at the highest price.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

16) In recent years, trading in secondary markets has increasingly become a function of
A) securities exchanges.
B) dealer markets.
C) technology that by-passes both brokers and dealers.
D) broker-dealer markets using consolidated venues and technologies.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
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Learning Goal: Learning Goal 3

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17) The great majority of transactions on the NYSE are executed
A) automatically through electronic technology.
B) on the trading floor by brokers known as specialists.
C) by dealers known as market makers.
D) by auction in trading areas known as pits.
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

18) Which of the following are correct statements concerning the NYSE?

I. Each stock has a designated location, called a post, at which its shares are traded.
II. The NYSE is a dealer market.
III. Supply and demand determines the price of each security.
IV. A specialist buys and sells to maintain a market for a particular security.

A) I and II only
B) I and III only
C) I, III and IV only
D) I, II, III and IV
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

19) A market where securities are are bought from or sold to a market maker is known as a
A) broker market.
B) dealer market.
C) exchange floor.
D) board of exchange.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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20) Large technology companies such as IBM and Microsoft trade
A) exclusively on the NASDAQ.
B) exclusively on the NYSE.
C) on either the NASDAQ or the NYSE.
D) exclusively on alternative trading systems.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

21) Which of the following is currently a requirement for a stock to be listed on the NYSE?
A) A price of at least $10 per share.
B) Three consecutive years of profitable operations.
C) Gross revenue of at least $15,000,000.
D) Total value of shares available for public trading (float) of $15,000,000.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 3

22) The dominant exchange for trading options contracts is the _____. The dominant player in the trading of futures contracts is _____.
A) NYSE; Nasdaq OMX BX
B) PHLX; CBOE
C) CBOE; CME Group
D) ISE; CBOT
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 3

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23) Exchange traded funds are
A) mutual funds that trade on the Big Board.
B) baskets of securities that trade like a single stock.
C) index funds that trade on the NYSE.
D) groups of securities that trade only on regional exchanges.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

24) The dominant options exchange is the
A) Chicago Board Options Exchange.
B) American Stock Exchange.
C) Pacific Stock Exchange.
D) Philadelphia Options Exchange.
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

25) The NYSE Euronext includes exchanges in all of the following cities EXCEPT
A) Amsterdam.
B) Brussels.
C) Paris.
D) Tokyo.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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26) The purpose of the Intermarket Trading System is to link major exchanges and dealer markets to
A) eliminate competition between brokers and dealers.
B) allow brokers and dealers to make transactions at the best price.
C) allow individual to compare the prices offered by various dealers and brokers.
D) allow individual investors to traded directly with each other.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

27) Options contracts on stocks may
A) grant the owner the right to buy the stock at a specified price over a specified period of time.
B) grant the owner the right to sell the stock at a specified price over a specified period of time.
C) depending on the type of contract, grant the owner the right to either buy or sell the stock at a specified price over a specified period of time.
D) legally oblige the owner to buy the stock at a specified price over a specified period of time.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 3

28) The automated system for trading highly active OTC securities is the
A) Big Board.
B) Kansas City Board.
C) Chicago Board of Trade.
D) NASDAQ.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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29) The over-the-counter (OTC) market is a
A) centrally located auction market.
B) telecommunications network connecting dealers.
C) market solely for institutional traders.
D) geographically dispersed auction market.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

30) ECNs are
A) publicly owned auction markets for listed stocks.
B) privately owned networks that transact trades between institutional investors.
C) facilities used by market makers for trading unlisted securities.
D) part of the third market which trades listed securities between individual investors.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

31) The price an individual investor will pay to purchase a stock in the OTC market is the
A) spread.
B) ask price.
C) bid price.
D) broker price.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

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32) Which of the following are associated with bull markets?

I. investor pessimism
II. government stimulus
III. economic recovery
IV. low inflation

A) I and II only
B) II and III only
C) I, II and III only
D) II, III and IV only
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

33) Which of the following are associated with bear markets?

I. investor pessimism
II. rising profits
III. economic slowdown
IV. rising security prices

A) I and III only
B) II and III only
C) I, II and III only
D) II, III and IV only
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
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Learning Goal: Learning Goal 3

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34) There are many differences between broker markets and dealer markets. These differences include such things as membership, location, regulation, and several other characteristics. Discuss at least five key differences between these two markets.
Answer: BROKER MARKETS—listing requirements, central physical location, members own seats, transactions occur through an auction process, specialists maintain fair and orderly markets, limited securities traded, limited number of securities traded, brokers charge commission to execute trades; largest in terms of dollar volume.
DEALER MARKETS—unlisted securities, most bonds traded here, primary and secondary market, decentralized locations, NASD membership required to trade; dealers make profit from bid/ask spread; largest in terms of number of companies.
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 3

2.4 Learning Goal 4

1) Diversification is the inclusion of a number of different investments in a portfolio with the goal of increasing returns or reducing risk.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

2) The financial markets are becoming more globally integrated.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

3) Participation in foreign stock markets is complicated and expensive for American investors.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

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4) The U.S. stock markets tend to produce the highest rate of return each year.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

5) Including foreign investments in a portfolio
A) increases the overall risk of the portfolio.
B) reduces the potential rate of return.
C) provides potential benefits from changes in currency values.
D) limits the diversification amongst industries.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

6) Which one of the following statements about foreign investments is true?
A) In general, major foreign markets always tend to underperform the U.S. market.
B) Investing in foreign markets may involve specific risks not encountered with domestic securities.
C) Investing in foreign markets will always produce higher returns because of exchange rate fluctuations.
D) Foreign markets include equity securities only.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

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7) Functioning securities exchanges are located in

I. Brazil
II. China
III. Russia
IV. South Korea

A) I, II, III and IV
B) I, II and IV only
C) I and IV only
D) II, III, and IV only
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 4

8) Dollar-denominated debt securities issued by foreign corporations and traded in U.S. markets are called
A) ADRs.
B) Yankee bonds.
C) ETFs.
D) global bonds.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

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9) Which of the following can be encountered when investing in foreign markets?

I. foreign taxation of dividends
II. different accounting standards for financial disclosure
III. restrictions on types of investments
IV. illiquid markets

A) II and III only
B) II and IV only
C) I, II and IV only
D) I, II, III and IV
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

10) American Depositary Receipts represent
A) receipts for dollar deposits in foreign banks.
B) receipts from foreign broker-dealers establishing ownership of foreign stocks.
C) receipts for the stocks of foreign companies held by banks in the companies' home country.
D) receipts for shares of foreign companies held by U.S. broker-dealers.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

11) Assume the foreign exchange rate for the euro was U.S. $1.00 = .91 euro last month. This month, the exchange rate is U.S. $1.00 = .88 euro. This information indicates that over the past month the
A) U.S. dollar remained unchanged relative to the euro.
B) U.S. dollar appreciated relative to all foreign currencies.
C) euro appreciated relative to the dollar.
D) euro depreciated relative to the dollar.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 3 Analytical thinking
Question Status: Revised
Learning Goal: Learning Goal 4

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12) Assume the foreign exchange rate for the euro was U.S. $1.00 = .91 euro last month. This month, the exchange rate is U.S. $1.00 = .88 euro. All things equal, the dollar value of European stocks
A) decreased.
B) increased.
C) stayed the same.
D) would vary depending on the country.
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 3 Analytical thinking
Question Status: Revised
Learning Goal: Learning Goal 4

13) American investors can participate in international stock markets by
A) purchasing shares in a mutual fund that invests in foreign companies.
B) purchasing shares of a U.S. based company such as Coca Cola or McDonald's with extensive international operations.
C) purchasing ADSs (American Depositary shares).
D) all of the above.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

14) The effects of fluctuating foreign exchange rates may

I. increase a U. S. investor's rate of return.
II. decrease a U. S. investor's rate of return.
III. can be avoided by investing in ADRs.
IV. can be avoided by investing in mutual funds that specialize in foreign stocks.

A) I and II only
B) I and III only
C) III and IV only
D) I, II, III and IV
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 4

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15) Kayla invested $3,000 and purchased shares of a German corporation when the exchange rate was $1.00 = .91 euro. After six months, she sold all of the shares for 3,180 euros, when the exchange rate was $1.00 = .88 euro. No dividends were paid during the time Heidi owned the shares of stock. What is the amount of Kayla's gain or loss on this investment?
A) $613.64 loss
B) $613.64 gain
C) $497.60 loss
D) $497.60 gain
Answer: B
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 3 Analytical thinking
Question Status: Revised
Learning Goal: Learning Goal 4

2.5 Learning Goal 5

1) After hours markets tend to be less volatile and more liquid than the regular trading sessions.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

2) SEC regulations strictly prohibit trading outside the normal hours of 9:30 A.m. to 4:00 P.M. EST.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

3) The Securities Act of 1933 deals mostly with primary markets.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

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4) Research indicates that investors are more likely to overreact to news when trading after hours.
Answer: FALSE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: New Question
Learning Goal: Learning Goal 5

5) Insider trading is the use of nonpublic information about a security to gain a profit.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

6) The Sarbanes-Oxley Act of 2002 strengthens accounting disclosure requirements and ethical guidelines for financial officers.
Answer: TRUE
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

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7) Which of the following characteristics apply to trading before and after regular hours?

I. Most after hours trades match a bid price to a corresponding offer price.
II. Most brokerage firms require individual investors to place only market orders for after-hours trades.
III. Electronic Communications Networks (ECNs) play a key role in after hours trading.
IV. After-hours trading begins at 4:00 P.M. and ends at 9:30 A.M. eastern time.

A) II and IV only
B) I, II and III only
C) I and IV only
D) I, III and IV only
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Revised
Learning Goal: Learning Goal 5

8) The Sarbanes-Oxley Act of 2002 focuses on
A) insider trading.
B) IPOs.
C) accounting and other public disclosures of information.
D) regulation of the OTC markets.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

9) Which of the following acts abolished fixed commission schedules?
A) Investment Advisers Act of 1940
B) Investment Company Act of 1940
C) Securities Acts Amendments of 1975
D) Insider Trading and Fraud Act of 1988
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

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10) An act explicitly defining and prohibiting insider trading was passed in
A) 1934.
B) 1975.
C) 1988.
D) 2002.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Revised
Learning Goal: Learning Goal 5

11) Which of the following are provisions of the Sarbanes-Oxley Act of 2002?

I. an oversight board to monitor the accounting industry
II. tougher penalties for executives who commit corporate fraud
III. stricter prohibitions against insider trading
IV. guidelines for analysts conflicts of interest

A) II and IV only
B) I, II and III only
C) I and IV only
D) I, II and IV only
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

12) The Consumer Financial Protection Agency was established by
A) Investment Company Act of 1940.
B) The Securities Acts Amendments of 1975.
C) The Sarbanes-Oxley Act of 2002.
D) The Dodd-Frank Act of 2010.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

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13) Which of the following practices is prohibited by the Insider Trading and Fraud Act of 1988?
A) the use of nonpublic information to make profitable stock transactions
B) selling of stock by officers of the company
C) the granting of stock options to corporate executives in lieu of salaries
D) private sales of stock between executives of the company
Answer: A
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

14) Crossing markets are those that
A) trade foreign securities.
B) conduct transactions between institutional and individual traders.
C) fill only the orders which have opposing orders at identical prices.
D) conduct business at locations in varying time zones.
Answer: C
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

15) The Securities Exchange Act of 1934
A) requires full disclosure of information on all new security issues.
B) authorized the SEC to regulate mutual funds.
C) established trade associations such as the NASD.
D) created the SEC as the regulator of the securities exchanges.
Answer: D
Learning Outcome: F-01 Describe the different financial markets and the role of the financial managers
AACSB: 8 Application of knowledge (Able to translate knowledge of business and management into practice)
Question Status: Previous Edition
Learning Goal: Learning Goal 5

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2.6 Learning Goal 6

1) Margin trading requires the borrowing of securities.
Answer: FALSE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

2) Margin trading will magnify losses on a percentage basis.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

3) Short selling requires the borrowing of securities.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

4) Short selling involves the sale of depreciated stock at a price below the amount borrowed on margin.
Answer: FALSE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

5) When a person sells a common stock short, she or he is betting that the price of the stock will fall.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

6) Losses on a stock purchase are limited to the price of the stock, but losses on a short sale are potentially unlimited.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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7) The minimum initial margin requirement for both long and short positions is set by the Federal Reserve Board and currently is 50%.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

8) A brokerage firm may set a higher margin requirement than that set by the Federal Reserve Board.
Answer: TRUE
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

9) The purchase of stock with cash in the hope of earning a capital gain is known as taking a
A) long position in the stock.
B) short position in the stock.
C) long, margined position in the stock.
D) short, margined position in the stock.
Answer: A
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

10) Which one of the following statements about margin trading is correct?
A) The Federal Reserve sets the minimum margin requirement for margin trading.
B) If Fred buys $1,000 worth of stock using 60% margin, he will need to pay $400 in cash to make the purchase.
C) Purchasing stocks on margin is less risky than purchasing stocks by paying cash for the entire purchase.
D) Margin trading increases the potential profits while lowering the potential losses on a percentage basis.
Answer: A
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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11) Which one of the following statements about margin trading is correct?
A) The Securities Exchange Commission sets the minimum margin requirement for margin trading.
B) If Fred buys $1,000 worth of stock using 60% margin, he will need to pay $600 in cash to make the purchase.
C) Margin traders are willing to accept lower return to reduce their risk.
D) Margin traders are pessimistic about the future price of the stock.
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

12) Megan bought 200 shares of stock at a price of $10 a share. She used her 70% margin account to make the purchase. Megan sold her stock after a year for $12 a share. Ignoring margin interest and trading costs, what is Megan's return on investor's equity for this investment?
A) 67%
B) 29%
C) 14%
D) 10%
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

13) Joseph bought 100 shares of stock at a price of $24 a share. He used his 70% margin account to make the purchase. Joseph sold his stock after a year for $20 a share. Ignoring margin interest and trading costs, what is Joseph's return on investor's equity for this investment?
A) -17%
B) -24%
C) 24%
D) -56%
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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14) Michael purchased 1000 shares of stock at a price of $16 a share. He utilized his 50% margin account to make the purchase. What is Michael's initial equity in this investment?
A) -$16,000
B) $16,000
C) $8,000
D) -$8,000
Answer: C
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

15) Jessica purchased 200 shares of stock at $38 using her 70% margin account. Her maintenance margin is 40%. Jessica has no other securities in her account. At what price will she receive a margin call?
A) $26.60
B) $19.00
C) $11.40
D) $7.60
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

16) A restricted account is defined as a margin account wherein the equity is
A) less than the initial margin amount.
B) greater than the initial margin amount.
C) less than the maintenance margin amount.
D) greater than the maintenance margin amount.
Answer: A
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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17) Emily bought 200 shares of ABC Co. stock for $29.00 per share on 60% margin. Assume she holds the stock for one year and that her interest costs will be $80 over the holding period. Ignoring commissions, what is her percentage return (loss) on invested capital if the stock price went down 10%?
A) -32%
B) -19%
C) -16%
D) -10%
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Revised
Learning Goal: Learning Goal 6

18) Gerry bought 100 shares of stock for $30.00 per share on 70% margin. Assume Gerry holds the stock for one year and that his interest costs will be $45 over the holding period. Gerry also received dividends amounting to $0.30 per share. Ignoring commissions, what is his percentage return on invested capital if he sells the stock for $34 a share?
A) 106.17%
B) 20.48%
C) 18.33
D) 9.16%
Answer: C
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

19) Justin just made a margin purchase of 100 shares of DEF Corp. for $22.50 per share. The initial margin is 70%. The maintenance margin is 30%. How low can the price of each share of DEF be before Justin will have to add equity to his account?
A) $4.73
B) $5.25
C) $6.75
D) $9.64
Answer: D
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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20) Maintenance margin is the
A) minimum amount of loan that can be used for margin trading.
B) initial amount of equity required for a margin purchase.
C) minimum amount of equity that an investor can have to avoid a margin call.
D) amount of additional funds that need to be added to an account to meet minimal equity requirements.
Answer: C
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

21) If an investor does not respond to a margin call, the broker will
A) sell enough of the investor's holdings that the margin account can be closed.
B) sell some of the investor's holdings to cover the margin call.
C) notify the Federal Reserve so they can cover the call.
D) sell all of the investor's holdings and close their brokerage account.
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

22) Which one of the following is a major advantage of margin trading?
A) increase in potential diversification
B) increase in potential profits on a percentage basis
C) possibility of increased gains on a dollar basis
D) interest free loans
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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23) Which of the following are characteristics of short selling?

I. borrowing shares of stock from a brokerage firm or other investors
II. selling shares of stock you do not own
III. betting the stock price will increase
IV. limiting losses per share to the price at which the stock was sold

A) I and II only
B) III and IV only
C) I, II and IV only
D) I, II, III only
Answer: A
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

24) Jocelyn sells short 1000 shares of JKLO stock at $31.25 per share and six months later purchases the shares at $29.00 each. Ignoring margin interest and brokerage fees, Nancy will
A) earn a total profit of $3,125.
B) lose a total of $2,900.
C) earn a total profit of $2,250.
D) Lose a total of $2,250.
Answer: C
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

25) Which of the following statements about short selling is (are) true?

I. Short selling requires an initial margin deposit.
II. Short sellers begin a transaction with a sale and end it with a purchase.
III. Short sellers profit when the stock prices rises.
IV. Short selling can be a risky strategy.

A) IV only
B) I and II only
C) I, II and IV only
D) I, II, III and IV
Answer: C
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

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26) Last week, Seward Company stock was selling at $66 a share when Ryan sold 300 shares of the stock short. Today Ryan bought 300 shares of the same stock at a price of $70.00 share to cover his position. Ignoring trading costs, what is the dollar return on Ryan's investment?
A) $1,200
B) -$400
C) $400
D) $-1,200
Answer: D
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: Previous Edition
Learning Goal: Learning Goal 6

27) Aria has heard a rumor that a major food company will be forced to recall millions of jars of peanut butter. due to contamination If the rumors are true, the company's stock price will decline sharply. Which one of the following strategies would allow Jennifer to earn a profit if the rumor proves to be true?
A) Take a long position in the stock today.
B) Sell the stock short today.
C) Buy the stock on margin today.
D) Take a long position in the stock one month from today.
Answer: B
Learning Outcome: F-11 Explain the relationship between risk and return in capital markets
AACSB: 3 Analytical thinking
Question Status: New Question
Learning Goal: Learning Goal 6

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