Fundamentals of Corporate Finance 5th edition Parrino Test Bank

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Fundamentals of Corporate Finance, 5e **(Parrino)**
Chapter 2 The Financial System and the Level of Interest Rates

1) The role of the financial system is to gather money from households (individuals), businesses and government that have funds to invest and to channel that money to those who need it.
Answer: TRUE
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

2) The financial system only consists of a number of different types of financial markets.
Answer: FALSE
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

3) Without a financial market, purchasing a house would require a cash purchase.
Answer: TRUE
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

4) The financial markets where direct transactions take place are retail markets with a typical minimum transaction size of $1 million.
Answer: FALSE
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

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5) Major buyers and sellers of securities in direct financial markets include commercial banks, large corporations, the federal government, hedge funds, and some wealthy individuals.
Answer: TRUE
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

6) Governments are the principal lender-savers in the economy.
Answer: FALSE
Diff: 1
Learning Objective: LO 1
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

7) Businesses are the principal borrower-spenders that borrow the most in the economy.
Answer: TRUE
Diff: 1
Learning Objective: LO 1
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

8) Primary markets are markets where already-issued securities are resold to other investors. They provide the means for investors to sell their securities to other investors.
Answer: FALSE
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

9) Secondary markets are markets where the owners of securities can resell them to other investors. They provide the means for investors to convert their securities into cash.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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10) Direct financial markets could be broadly labeled as wholesale markets for funding.
Answer: TRUE
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

11) A privately held corporation that borrows from a regional commercial bank is an example of a direct market transaction.
Answer: FALSE
Diff: 1
Learning Objective: LO 2
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

12) The law that prohibited commercial banks from engaging in investment banking activities is the Financial Services Modernization Act of 1999.
Answer: FALSE
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: FSA
AICPA: Legal/Regulatory Perspective

13) With the passage of Financial Services Modernization Act, major money center banks in the United States today are allowed to provide investment banking services.
Answer: TRUE
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: FSA
AICPA: Legal/Regulatory Perspective

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14) When a company raises capital by issuing shares for the first time, the selling of newly issued stocks occurs in a secondary market.
Answer: FALSE
Explanation: A primary market is a financial market in which new security issues are sold by companies directly to investors. A secondary market is any market in which owners of outstanding securities can resell them to other investors.
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

15) Most securities that are sold on the New York Stock Exchange are secondary market transactions.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

16) An active secondary market for a security will help to enhance the price of that particular security in the primary market.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

17) The downside to a private placement transaction is that it does not require the fees and expenses associated with an SEC registration.
Answer: FALSE
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

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18) Brokers are market specialists who do not bear the risk of owning securities.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

19) Money market instruments are financial instruments that are highly marketable and can easily be converted into cash.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

20) Equities with maturities greater than one year generally are traded in the capital markets.
Answer: TRUE
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

21) Most companies use indirect market funding from financial institutions to obtain financing.
Answer: TRUE
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

22) Most companies finance their business investments by obtaining the majority of their funds from selling equity.
Answer: FALSE
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

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23) The nominal interest rate is the rate of interest that is adjusted for inflation.
Answer: FALSE
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

24) Real rates of interest are perfectly observable in the financial markets.
Answer: FALSE
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

25) It is impossible for the nominal rate of interest to be lower than real rate of interest.
Answer: FALSE
Diff: 1
Learning Objective: LO 6
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

26) It is difficult for individuals to participate in the direct financial markets for the following reason:
A) The direct financial markets are retail markets with a typical minimum transaction size of $1 million.
B) The direct financial markets are wholesale markets with a typical minimum transaction size of $1 million.
C) Major buyers and sellers of securities in indirect financial markets include commercial banks, large corporations, the federal government, hedge funds, and some wealthy individuals.
D) Major buyers and sellers of securities in direct financial markets do not include commercial banks, large corporations, the federal government, hedge funds, and some wealthy individuals.
Answer: B
Diff: 1
Learning Objective: LO 1
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

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27) An economy with a large flow of funds requires:
A) a lot of gold reserves.
B) a frictionless market.
C) an efficient financial system.
D) all of the these.
Answer: C
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

28) Financial markets and financial institutions are both parts of:
A) the U.S. Treasury.
B) the financial system.
C) the SEC.
D) none of these answers are correct.
Answer: B
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

29) Savings provided by _____ in small dollar amounts is the origin of much of the money that funds business loans in an economy.
A) households
B) the U.S. government
C) small businesses
D) none of these answers are correct
Answer: A
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

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30) The primary function of a financial system is to funnel funds from:
A) wealthy individuals to non-wealthy individuals.
B) lender-savers to borrower-spenders.
C) borrower-spenders to lender-savers.
D) the government to wealthy individuals.
Answer: B
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

31) _____ are the principal lender-savers in the economy.
A) Households
B) Investment banks
C) State governments
D) Businesses
Answer: A
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

32) An important function of financial intermediation is:
A) to convert financial securities with one set of characteristics into securities with a different set of characteristics.
B) to direct the money from lenders to borrowers.
C) to direct the money from borrowers to savers.
D) for commercial banks to use consumer CD deposits to make deposits to small businesses.
Answer: A
Diff: 1
Learning Objective: LO 1
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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33) An important function of the financial system is:
A) to direct funds from savers to the best investment opportunities in the economy.
B) to allow the federal government to view all financial transactions.
C) to help state governments to coordinate state tax levies.
D) to direct the money from borrower-lenders to lender-savers.
Answer: A
Diff: 1
Learning Objective: LO 1
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

34) Direct financing occurs when:
A) a lender-saver borrows directly from a borrower-spender.
B) a borrower-spender borrows directly from a lender-saver.
C) a lender-saver borrows from the federal government.
D) a borrower-spender borrows from the federal government.
Answer: B
Diff: 1
Learning Objective: LO 1
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

35) Which of the following are major participants in the direct financial markets?
A) Large corporations
B) Wealthy individuals
C) Financial Institutions
D) All of these
Answer: D
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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36) The major players in the direct financial markets are:
A) investment banks.
B) money center banks.
C) regional banks.
D) both investment banks and money center banks.
Answer: D
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

37) What is the typical minimum denominated transaction size in the direct financial markets?
A) $10,000
B) $100,000
C) $1,000,000
D) $10,000,000
Answer: C
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

38) Which of the following Acts is responsible for rolling back many of the rules prohibiting commercial banks from engaging in investment banking activities?
A) The Securities Act of 1933
B) The Securities Exchange Act of 1934
C) The Glass-Steagall Act of 1933
D) The Financial Services Modernization Act of 1999
Answer: D
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: FSA
AICPA: Legal/Regulatory Perspective

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39) Which of the following is a process by which investment bankers purchase new securities directly from the issuing company and resell them to the investors?
A) Agency marketing
B) Underwriting
C) Distribution
D) Private placement
Answer: B
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

40) Stocks that are traded in the _____ are typically those of smaller and less well-known firms.
A) National Stock Exchange
B) New York Stock Exchange
C) American Stock Exchange
D) over-the-counter markets
Answer: D
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

41) The financial market where a new security is sold for the first time is called:
A) a primary market.
B) a secondary market.
C) an indirect financial market.
D) none of these answers are correct.
Answer: A
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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42) Secondary financial markets are similar to:
A) direct auction markets.
B) new-car markets.
C) used-car markets.
D) direct financial market.
Answer: C
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

43) If you just purchased a share of IBM through a New York Stock Exchange-based transaction, you participated in:
A) a primary market transaction.
B) a secondary market transaction.
C) a futures market transaction.
D) none of these answers are correct.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Application
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

44) The ease with which a security can be sold and converted into cash is called:
A) convertibility.
B) liquidity.
C) marketability.
D) none of these answers are correct.
Answer: C
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

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45) The presence of a secondary market increases the marketability of a financial security by:
A) insuring the price of the security.
B) reducing the transaction costs from selling the security.
C) guaranteeing the accuracy of information produced by the issuer of the security.
D) none of these answers are correct.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

46) One of the main services provided by investment banks to companies is:
A) helping companies sell new debt or equity issues in the financial markets.
B) making loans to companies.
C) taking deposits from companies.
D) all of these.
Answer: A
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

47) The NYSE is an example of:
A) an over-the-counter market exchange.
B) an organized exchange.
C) a commodities exchange.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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48) Which of the following markets has no central trading location?
A) A futures and options market
B) An over-the-counter market
C) An auction market
D) None of these answers are correct
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

49) A highly liquid financial instrument with a maturity of 90 days would be traded in:
A) the money market.
B) the bond market.
C) the stock market.
D) none of these answers are correct.
Answer: A
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

50) Money market instruments are generally issued by:
A) firms in dire need of cash to maintain their credit rating.
B) firms with the highest credit rating.
C) firms with lower credit ratings.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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51) The term *money market* is used because:
A) firms that issue securities in this market are in dire need of cash.
B) it is a market where stocks are converted into money.
C) the instruments traded in this market are close substitutes for cash.
D) none of these answers are correct.
Answer: C
Diff: 3
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

52) If a firm needs to adjust its liquidity position, then it would participate in:
A) the money market.
B) the bond market.
C) the stock market.
D) the auction market.
Answer: A
Diff: 2
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

53) If a firm needs to finance a new corporate headquarters building, then it would most likely seek the funds in the:
A) money market.
B) capital market.
C) futures market.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

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54) Which of the following statements about the OTC market is true?
A) Securities that are listed on an organized exchange are bought and sold in the OTC market.
B) An OTC market is an organized exchange where there is a central trading location.
C) OTC security transactions are made on the floor of an exchange by traders.
D) Securities that are not listed on an organized exchange are bought and sold on the OTC market.
Answer: D
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

55) The most common reason that corporate firms use the futures and options markets is to:
A) hedge risk.
B) take risk.
C) make deposits.
D) none of these answers are correct.
Answer: A
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

56) Which of the following theories states that security prices reflect all public information, but not all private information?
A) Weak-form efficiency
B) Semistrong-form efficiency
C) Strong-form efficiency
D) Nominal-form efficiency
Answer: B
Diff: 1
Learning Objective: LO 4
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

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57) Which of the following theories states that security prices reflect all information, whether public or private?
A) Weak-form efficiency
B) Semistrong-form efficiency
C) Strong-form efficiency
D) Nominal-form efficiency
Answer: C
Diff: 1
Learning Objective: LO 4
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

58) If your firm obtains most of its financing from commercial banks, then it primarily accesses the capital markets through:
A) direct financing.
B) indirect financing.
C) a legal loophole that allows all commercial banks the ability to underwrite securities.
D) none of these answers are correct.
Answer: B
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

59) The process of converting financial securities with one set of characteristics into securities with another set of characteristics is called:
A) financial bundling.
B) financial intermediation.
C) financial disintermediation.
D) none of these answers are correct.
Answer: B
Diff: 1
Learning Objective: LO 5
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

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60) A line of credit to a corporation is like _____ to an individual.
A) a term loan
B) a bond
C) a credit card
D) a debit card
Answer: C
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

61) Which of the following can be a primary investment vehicle(s) for the funds in which life insurance companies must invest?
A) CDs
B) Equity securities
C) Long-term corporate bonds
D) Both equity securities and long-term corporate bonds
Answer: D
Diff: 2
Learning Objective: LO 5
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

62) Casualty insurance companies sell:
A) protection against loss of income in the event of the death of the insured.
B) protection against loss of property from fire, theft, accidents, and other predictable causes.
C) protection against a loss of pension revenue for retirees.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

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63) Which of the following is least likely to be included in a pension fund's investment portfolio?
A) Commercial paper
B) Long-term corporate bonds
C) Stocks
D) Long-term government securities
Answer: A
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

64) A mutual fund is an example of:
A) a line of credit.
B) an endowment fund.
C) an investment fund.
D) a pension fund.
Answer: C
Diff: 1
Learning Objective: LO 5
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

65) Large firms are most likely to use money markets:
A) to finance long term investments.
B) to adjust their liquidity position.
C) to make long term investments.
D) to buy commercial paper at lower interest rates than it could sell through a bank.
Answer: B
Diff: 1
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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66) If a small business chooses not to borrow funds from a commercial bank, then what will probably be its next best alternative source of capital?
A) An insurance company
B) A pension
C) An investment fund
D) A business finance company
Answer: D
Diff: 1
Learning Objective: LO 5
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

67) The cost of borrowing money is called:
A) inflation.
B) return.
C) interest.
D) all of these.
Answer: C
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

68) Which of the following statements best describes the relationship between interest rates and the business cycle?
A) Typically, the Fed tightens credit to stimulate the economy, which puts further downward pressure on interest rates.
B) Interest rates tend to rise during economic expansion and decline during economic contraction.
C) During an expansion, there is downward pressure on interest rates as businesses begin to grow and borrow more money.
D) During a recession, the demand for goods and services is lower, businesses borrow more, and as a result the economy slows down and the interest rates decline.
Answer: B
Diff: 1
Learning Objective: LO 6
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

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69) The nominal rate of interest is comprised of:
A) the real rate of interest.
B) inflation expectation.
C) a commodity cross-index return.
D) both the real rate of interest and inflation expectation.
Answer: D
Diff: 1
Learning Objective: LO 6
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

70) The real rate of interest can be fundamentally determined by:
A) compensation for inflation.
B) compensation for deferring consumption.
C) compensation for the level of international borrowing.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 6
Bloomcode: Comprehension
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

71) If you are a borrower, which would you prefer to occur during the life of your loan?
A) A level of inflation that is higher than that anticipated at the outset of the loan
B) A level of inflation that is lower than that anticipated at the outset of the loan
C) A level of inflation that is exactly the same as anticipated at the outset of the loan
D) No inflation at all
Answer: A
Diff: 2
Learning Objective: LO 6
Bloomcode: Application
AACSB: Reflective Thinking
IMA: Corporate Finance
AICPA: Resource Management

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72) If inflation is anticipated to be 6 percent during the next year, while the real rate of interest for a one-year loan is 5 percent, then what should the nominal rate of interest be for a risk-free one-year loan?
A) 6%
B) 11%
C) 5%
D) 12%
Answer: B
Diff: 2
Learning Objective: LO 6
Bloomcode: Application
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

73) If inflation is anticipated to be 5 percent during the next year, while the nominal rate of interest for a risk-free one-year loan is 10 percent, then what should the real rate of interest for a one-year loan be?
A) 5 percent
B) 10 percent
C) 15 percent
D) 25 percent
Answer: A
Diff: 2
Learning Objective: LO 6
Bloomcode: Application
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

74) The general level of interest rates tends to follow:
A) deflation.
B) the business cycle.
C) the default cycle.
D) all of these.
Answer: B
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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75) During an economic expansion, we would expect:
A) interest rates to increase.
B) interest rates to decrease.
C) interest rates to remain the same.
D) the cost of money to decrease.
Answer: A
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

76) In the United States, the real rate of interest has historically been around:
A) 1 percent.
B) 3 percent.
C) 5 percent.
D) 7 percent.
Answer: B
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Global Perspective

77) You loaned $100 to a friend for one year at a nominal rate of interest of 3 percent. Inflation during that year was 2 percent. Has the purchasing power of your money increased or decreased and by how much?
A) Increased by 1 percent.
B) Decreased by 1 percent
C) Increased by 5 percent.
D) Decreased by 5 percent
Answer: A
Diff: 2
Learning Objective: LO 6
Bloomcode: Analysis
AACSB: Analytic
IMA: Business Economics
AICPA: Resource Management

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78) You loaned $100 to a friend for one year at a nominal rate of interest of 5 percent. Inflation during that year was 8 percent. Has the purchasing power of your money increased or decreased and by how much?
A) Increased by approximately 3 percent
B) Decreased by approximately 3 percent
C) Increased by approximately 13 percent
D) Decreased by approximately 13 percent
Answer: B
Diff: 2
Learning Objective: LO 6
Bloomcode: Analysis
AACSB: Analytic
IMA: Business Economics
AICPA: Resource Management

79) If the supply of loanable funds decreases relative to the demand for those loanable funds, then we would expect:
A) interest rates to remain unchanged.
B) interest rates to increase.
C) interest rates to decrease.
D) the cost of money to remain unchanged.
Answer: B
Diff: 1
Learning Objective: LO 6
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Resource Management

80) Which of the following terms relates to the process in which a firm sells common stocks to the public for the very first time?
A) An underwriting
B) An initial public offering
C) A financial intermediation
D) An origination
Answer: B
Diff: 1
Learning Objective: LO 2
Bloomcode: Knowledge
AACSB: Analytic
IMA: Corporate Finance
AICPA: Industry/Sector Perspective

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81) Explain why secondary markets are so important to businesses that need to raise capital.
Answer: Secondary markets provide liquidity to the buyers of securities. They facilitate the sale of securities because they enable investors to buy and sell securities as frequently as they want. Secondary markets are important to corporations because investors are willing to pay higher prices for securities in primary markets if the securities are expected to have active secondary markets. This lowers the cost of capital for the corporations that issue securities.
Diff: 3
Learning Objective: LO 3
Bloomcode: Comprehension
AACSB: Analytic
IMA: Business Economics
AICPA: Industry/Sector Perspective

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