Fundamentals of Corporate Finance (Canadian) 7th edition Brealey Test Bank

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Chapter 02
Financial Markets and Institutions

True / False Questions

1. Only small companies can go through financial markets to obtain financing.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

2. The reinvestment of cash back into the firm's operations is an example of a flow of savings to investment.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

3. Smaller businesses are especially dependent upon internally generated funds.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

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4. An individual can save and invest in a corporation only by lending money to it or by purchasing additional shares.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-01 The Importance of Financial Markets and Institutions

5. Previously issued securities are traded among investors in the secondary markets.
TRUE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

6. Only the IPOs for large corporations are sold in primary markets.
FALSE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

7. The markets for long-term debt and equity are called capital markets.
TRUE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

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8. The derivative market is also a source of financing for corporations.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

9. Apple Computer is well known for its product innovations. Access to financing was vital to Apple's growth and profitability.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-01 The Importance of Financial Markets and Institutions

10. Whenever there is uncertainty, investors might be interested in trading, either to speculate or to lay off their risks, and a market may rise to meet the trading demand.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

11. Financing for public corporations must flow through financial markets.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

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12. Financing for private corporations must flow through financial intermediaries.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

13. Hedge fund managers, unlike mutual fund managers, do not receive fund-performance-related fees.
FALSE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

14. A financial intermediary invests in financial assets rather than real assets.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

15. The stocks of major corporations trade in many markets throughout the world on a continuous or near-continuous basis.
TRUE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-11 Liquidity

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16. The key to the banks' ability to make illiquid loans is their ability to pool liquid deposits from thousands of depositors.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-11 Liquidity

17. For corporate bonds, the higher the credit quality of an issuer, the higher the interest rate.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-13 Information Provided by Financial Markets

18. Like public companies, private companies can also use their stock price as a measure of performance.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-13 Information Provided by Financial Markets

19. Financial markets and intermediaries allow investors and businesses to reduce and reallocate risk.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-10 Risk Transfer and Diversification

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20. Almost all foreign exchange trading occurs on the floors of the FOREX exchanges in New York and London.
FALSE

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-04 Other Financial Markets

21. The cost of capital is the interest rate paid on a loan from a bank or some other financial institution.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

22. The opportunity cost of capital is the expected rate of return that shareholders can obtain in the financial markets on investments with the same risk as the firm's capital investments.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

23. The cost of capital is the minimum acceptable rate of return for capital investment.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

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24. The rates of return on investments outside the corporation set the minimum return for investment projects inside the corporation.
TRUE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

25. The effects of the financial crisis of 2007-2009 were confined to the U.S. and domestic companies.
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

26. One root of the financial crisis of 2007-2009 was the strict money policies promoted by the U.S. Federal Reserve and other central banks after the technology bubble burst (i.e., money was relatively expensive during this time).
FALSE

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
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Multiple Choice Questions

27. Which one of these is a money market security?
A. commercial paper
B. common stock
C. 2-year bond
D. 20-year bond

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

28. Which one of these assists in shifting an individual's consumption forward in time?
A. a bank line of credit
B. a bank savings account
C. a life insurance policy
D. a retirement savings plan

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-09 Transporting Cash Across Time

29. Which of the following is *not* typically considered a function of financial intermediaries?
A. providing a payment mechanism
B. investing in real assets
C. accumulating funds from smaller investors
D. spreading, or pooling risk among individuals

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

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30. Commodity and derivative markets:
A. are additional sources of financing for corporate projects.
B. enable the financial manager to adjust a firm's exposure to various business risks.
C. are always over-the-counter markets.
D. deal only in foreign currencies.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Hard
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

31. Which one of these transports income forward in time?
A. retirement savings
B. car loan
C. bank line of credit
D. credit card purchase

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-09 Transporting Cash Across Time

32. Who was responsible for the financial crisis of 2007-2009?
A. The U.S. Federal Reserve, for its policy of easy money
B. The U.S. government, for pushing banks to expand credit for low-income housing
C. bankers, who aggressively promoted and resold subprime mortgages
D. The U.S. Federal Reserve, the U.S. government, rating agencies, and bankers

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

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33. Which one of the following funds not provides a tax advantage to individual investors?
A. balanced funds
B. pension funds
C. bond funds
D. funds that are invested in foreign countries

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

34. Which of the following financial assets is *least* likely to have an active secondary market?
A. common stock of a large public firm
B. bank loans made to smaller firms
C. bonds of a major, multinational corporation
D. debt issued by the federal government

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Hard
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

35. A company can pay for its expansion in all the following ways *except*:
A. by using the earnings generated from its sale of obsolete equipment.
B. by persuading a director's mother to make a personal loan to the company.
C. by purchasing bonds in the secondary market.
D. by selling stock certificates for a new subsidiary.

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

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36. Short-term financing decisions commonly occur in the:
A. primary markets.
B. secondary markets.
C. capital markets.
D. money markets.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

37. Long-term financing decisions commonly occur in the:
A. option markets.
B. secondary markets.
C. capital markets.
D. money markets.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

38. Which type of financial institution generally does not accept deposits but does underwrite stock offerings?
A. Insurance company
B. Mutual fund
C. Commercial bank
D. Investment bank

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

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39. You can buy silver in the:
A. capital markets.
B. foreign exchange markets.
C. commodities markets.
D. option markets.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-04 Other Financial Markets

40. Which of the following actions does *not* help reduce risk?
A. extending the service warranty for your notebook
B. converting your money market account to a mutual fund account
C. contracting to sell your farm produce to the neighborhood grocery
D. buying Japanese yen now when you plan to study in Japan next year

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-10 Risk Transfer and Diversification

41. Financing for public corporations flows through:
A. the financial markets only.
B. financial intermediaries only.
C. derivatives markets.
D. the financial markets, financial intermediaries, or both.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
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Topic: 02-02 The Flow of Savings to Corporations

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42. One reason suggesting that banks may be better than individuals at matching lenders to borrowers is that banks:
A. can shift loan risk to their deposit customers.
B. are motivated by the potential for profit.
C. do not have any income tax liability.
D. have information to evaluate creditworthiness.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

43. Which of the following factors contributed to the financial crisis of 2007-2009?
A. Greece's debt
B. Subprime mortgages
C. Drought conditions in the mid-west
D. Both Greece's debt and subprime mortgages

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

44. Which one of the following financial intermediaries has shown the greatest preference for investing in *long-term* financial assets?
A. Commercial banks
B. Insurance companies
C. Finance companies
D. Savings banks

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

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45. Financial markets and intermediaries:
A. channel savings to real investment.
B. increase risks for businesses.
C. generally reduce the liquidity of securities.
D. prevent the transportation of cash across time.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

46. A bond differs from a share of stock in that a bond:
A. represents a claim on the firm.
B. has more risk.
C. has guaranteed dividend payments.
D. has a maturity date.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

47. Short term corporate debt instruments are most commonly traded:
A. on the TSX.
B. on commodities.
C. in the money market.
D. in the over the counter market.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

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48. Which one of these may provide a financial return to some investors while not providing any financial return to other investors?
A. Mutual funds
B. Pension funds
C. Insurance companies
D. Hedge fund

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

49. Which one of these parties *cannot* invest in a hedge fund?
A. small retail investors
B. pension funds
C. insurance companies
D. wealthy individuals

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

50. Which of the following are both a financial intermediary and a financial institution?
A. mutual funds
B. pension funds
C. insurance companies
D. hedge funds

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries
Topic: 02-06 Financial Institutions
Topic: 02-08 Functions of Financial Markets and Intermediaries

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51. Which one of these was a contributing factor to the need for many foreign banks to seek aid from their governments as a result of the financial crisis of 2007-2009?
A. decrease in their exchange rates
B. investments in U.S. subprime mortgages
C. interest rate spikes
D. currency controls

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

52. Which one of these enterprises generally acts as an underwriter for an initial public offering?
A. commercial bank
B. government
C. investment bank
D. insurance company

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

53. The financial crisis of 2007-2009 contributed to the largest sovereign default in history by which one of these countries?
A. Italy
B. Portugal
C. Ireland
D. Greece

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

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54. The cost of capital:
A. is the expected rate of return on a capital investment.
B. is an opportunity cost determined by the risk-free rate of return.
C. is the interest rate that the firm pays on a loan from a bank or insurance company.
D. for risky investments is normally higher than the firm's borrowing rate.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Hard
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

55. The cost of capital:
A. is the interest rate that the firm pays on a loan from a financial institution.
B. is the maximum acceptable rate of return on a project.
C. is the minimum acceptable rate of return on a project.
D. is always less than 10%.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

56. During the Financial Crisis of 2007-2009, the U.S. government bailed out all of the following firms *except*:
A. AIG.
B. Fannie Mae.
C. Lehman Brothers.
D. Freddie Mac.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

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57. A mother in a developing country wants to borrow the equivalent of $20 to enable her to start a small restaurant run by her family. Which type of financing is she looking to obtain?
A. public bond issue
B. IPO
C. micro loan
D. futures contract on a commodity

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

58. Which of the following information is *not* provided by the financial markets?
A. the price of six ounces of gold
B. the cost of borrowing $500,000 for 5 years
C. Microsoft's earnings in 2013
D. the cost of one million yen in U.S. dollars

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-13 Information Provided by Financial Markets

59. Which one of the following is the biggest provider of payment mechanisms?
A. hedge funds
B. banks
C. mutual funds
D. insurance companies

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-12 The Payment Mechanism

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60. "Reinvestment" means:
A. new investment in new operations.
B. additional investment in existing operations.
C. new investment by new shareholders.
D. additional savings by existing shareholders.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

61. Liquidity is important to a mutual fund primarily because:
A. a fund that is less liquid will attract more investors.
B. the fund's shareholders may want to redeem their shares at any time.
C. new investors may invest in the fund at any time.
D. the fund requires cash to pay its taxes.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Hard
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-11 Liquidity

62. One contributing factor to the 2007-2009 financial crisis was the structuring of mortgage loans with:
A. high initial payments, offset by significantly lower payments later.
B. low initial payments, offset by significantly higher payments later.
C. no initial payments, offset by significantly high payments later.
D. equal payments over the life of the loan.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
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63. NINJA stands for
A. No income, No Job, No Assets
B. No income, No job, Assets
C. No interest rate, No Job, No Assets
D. No insider information, No Jeopardy, No Assets

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

64. Foreign currencies are traded:
A. only by banks in New York and London.
B. over the counter.
C. on both the NYSE and NASDAQ.
D. on the Intercontinental Exchange.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

65. When Patricia sells her Air Canada common stock at the same time that Brian purchases the same amount of Air Canada stock, Air Canada receives:
A. the dollar value of the transaction.
B. the dollar amount of the transaction, less brokerage fees.
C. only the par value of the common stock.
D. nothing.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
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Topic: 02-03 The Stock Market

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66. The main cause of the financial crisis of 2007-2009 was caused by which financial market factor?
A. Corporate greed
B. Agency
C. Poor economic advice
D. Lack of understanding about who financial markets operate

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Hard
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

67. The primary distinction between securities sold in the primary and secondary markets is the:
A. riskiness of the securities.
B. price of the securities.
C. previous issuance of the securities.
D. profitability of the issuing corporation.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

68. Which one of these is generally a key difference between U.S. and foreign commercial banks?
A. pooling and investing savings
B. accepting investor deposits
C. providing debt financing to corporations
D. making equity investments in corporations

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
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Topic: 02-06 Financial Institutions

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69. A financial institution:
A. is a kind of financial intermediary.
B. simply pools and invests savings.
C. raises financing by selling shares.
D. invests primarily in commodities.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Hard
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

70. Which one of the following is *least* liquid?
A. foreign currency
B. Government of Canada Treasury bonds
C. real estate
D. savings deposit

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-11 Liquidity

71. Excess cash held by a firm should be:
A. reinvested by the firm in projects offering the lowest rate of return.
B. reinvested by the firm in projects offering rates of return higher than the cost of capital.
C. reinvested by the firm in the financial markets.
D. distributed to bondholders in the form of extra coupon payments.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-16 The Opportunity Cost of Capital

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72. Which of the following functions does *not* require financial markets?
A. transporting of cash across time
B. provision of liquidity
C. risk reduction by investment in diversified portfolios
D. provision of pricing information

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Hard
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-04 Other Financial Markets
Topic: 02-08 Functions of Financial Markets and Intermediaries

73. Which one of these was a major cause of the deep recession and severe unemployment throughout much of Europe that followed the financial crisis of 2007-2009?
A. government actions to raise interest rates
B. investor speculation
C. risk-adverse investor attitudes
D. government actions to lower government debt

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

74. A primary market would be utilized when:
A. investors buy or sell existing securities.
B. shares of common stock are exchanged.
C. securities are initially issued.
D. a commission must be paid on the transaction.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

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75. "Balanced" mutual funds:
A. invest in both stocks and bonds.
B. spread their investments equally over a specified geographic area.
C. spread their investments equally over various industries.
D. charge a management fee that is proportionate to the investment return.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

76. Insurance companies primarily reduce an individual's risk by:
A. transporting that risk forward in time.
B. providing payment services.
C. spreading that risk across many individuals.
D. providing low-interest-rate loans.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-10 Risk Transfer and Diversification

77. When corporations need to raise funds through stock issues, they rely on the:
A. primary market.
B. secondary market.
C. tertiary market.
D. centralized NASDAQ exchange.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

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78. Corporate financing comes ultimately from:
A. savings by households and foreign investors.
B. cash generated from the firm's operations.
C. the financial markets and intermediaries.
D. the issue of shares in the firm.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-02 The Flow of Savings to Corporations

79. Firms can often determine the current price of any commodities they use in their production process by consulting the price quotes provided by:
A. their investment bank.
B. the New York Mercantile Exchange.
C. the New York Stock Exchange.
D. the Standard & Poor's market indexes.

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-13 Information Provided by Financial Markets

80. A share of Canadian Tire stock is purchased by an individual investor for $75 and later sold to another investor for $125. Who profits from this sale?
A. Canadian Tire
B. the first investor
C. the second investor
D. Canadian Tire and both investors

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-03 The Stock Market

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81. Insurance companies can usually cover the claims of policyholders because:
A. the incidence of claims normally averages out across all policyholders.
B. they issue a very limited number of policies.
C. they are fully insured by the Canadian government.
D. their stockholders will cover any cash shortfalls encountered by the company.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-06 Financial Institutions

82. Which one of the following statements is *not* a characteristic of mutual funds?
A. they are always considered to be financial institutions.
B. they raise money by selling shares to investors.
C. they pool the savings of many investors.
D. they offer professional management and portfolio diversification.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

83. A capital investment that generates a 10% rate of return is worthwhile if:
A. corporate bonds of similar risk offer 8% rates of return.
B. corporate bonds of similar risk offer 11% rates of return.
C. top-quality corporate bonds offer 10% rates of return.
D. the expected rate of return on the stock market is 12%.

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Easy
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-14 Value Maximization and the Cost of Capital

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84. How is the relationship between a bond's credit rating and its interest rate best defined?
A. inverse relationship
B. direct relationship
C. unrelated
D. logarithmic

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-13 Information Provided by Financial Markets

85. If Apple Computer Inc. is used as the model, then new firms should expect to raise capital in which one of these orders? Start with the first money raised.
A. owners, venture capitalists, suppliers, public investors
B. owners, suppliers, venture capitalists, public investors
C. venture capitalists, owners, public investors, suppliers
D. owners, public investors, venture capitalists, suppliers

Accessibility: Keyboard Navigation
Blooms: Apply
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-01 The Importance of Financial Markets and Institutions

86. Which one of these correctly applies to mutual funds?
A. mutual funds are a costly means of achieving portfolio diversification.
B. funds are required to limit their annual fees and expenses to less than 1 percent of the portfolio value.
C. you can generally buy additional shares in the fund at any time.
D. shareholders sell their shares to other shareholders.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-05 Financial Intermediaries

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87. A _____ is an alternative currency, or medium of exchange, in the form of a digital asset.
A. Cryptocurrency
B. Digital wallet
C. Cyber money
D. Virtual Money

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

88. Assets such as this operate outside of central banking systems and use cryptography and ____ control to create and secure financial transactions and verify the transfer of assets.
A. decentralized
B. centralized
C. physical
D. virtual

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

89. Decentralized control is made possible through a distributed ledger technology, such as a _____, that serves as a public financial transaction database.
A. *block chain*
B. *blocked chain*
C. *daisy chain*
D. *linked chain*

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

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90. Cryptocurrencies often involve elements known as ____, *wallets*, and *anonymity*.
A. *mining*
B. *digging*
C. *pan handling*
D. *extracting*

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-04 Other Financial Markets

Short Answer Questions

91. What are three major types of financial markets? Describe what the main characteristics of each market are.

Equity market - stock market
Bond market - buy and sell bonds
Capital market - long term financing
Money Market - short term financing

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Hard
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-01 The Importance of Financial Markets and Institutions

92. Describe the difference between the primary and the secondary market.

Primary market is for the sale or NEW securities.
Secondary market is for the sale of already issued securities.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Topic: 02-01 The Importance of Financial Markets and Institutions

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93. Describe the difference between the money and the capital market. Provide one example of each type of security that is traded in each market.

Money market - short term financing Example - commercial paper
Capital market - long term financing Example - bonds, shares

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-01 The Importance of Financial Markets and Institutions

94. Describe the difference between the stock market and the fixed income market. Provide one example of each type of security that is traded in each market.

Stock market - buy and sell shares - shares
Fixed income market - debt - bonds

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-01 The Importance of Financial Markets and Institutions

95. Describe what a financial intermediary is and does.

An organization that raises money from investors and provides financing for individuals, corporations and other organizations.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-01 The Importance of Financial Markets and Institutions

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96. Describe what a mutual fund is.

A managed investment fund, pooling the savings of many investors and investing in a portfolio of securities.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Learning Objective: 02-01 Describe how financial markets and institutions channel savings to corporate investment.
Learning Objective: 02-02 Describe the basic structure of mutual funds, pension funds, banks, and insurance companies.
Topic: 02-01 The Importance of Financial Markets and Institutions

97. What is meant by the term of liquidity why is it important?

The ability to sell or exchange and asset for cash on short notice, without a significant loss in economic value. It is important because bills are normally paid in cash as they become due. Lack of liquidity will lead to default and eventually bankruptcy.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Learning Objective: 02-03 Enumerate the functions of financial markets and institutions.
Topic: 02-08 Functions of Financial Markets and Intermediaries

98. Define what cost of capital is and describe why it is important.

Cost of capital is the minimum required rate of return on capital investments. It is important because it helps an organization differentiate between investments that will increase or decrease the value of the organization.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Medium
Learning Objective: 02-04 Explain why the cost of capital for corporate investment is determined by investment opportunities in financial markets.
Topic: 02-14 Value Maximization and the Cost of Capital

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99. Identify a minimum of four major market factors that contributed to the financial crisis of 2007-2009.

1. The Federal Reserve for its easy money policy
2. The US government for encouraging banks to expand credit for low income housing
3. The rating agencies for providing triple-A ratings for mortgage bonds that shortly afterward went into default
4. Bankers for promoting and reselling subprime mortgages.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Hard
Learning Objective: 02-05 Recount the main events behind the financial crisis of 2007-2009 and the subsequent eurozone crisis.
Topic: 02-17 The Crisis of 2007-2009

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