

TEST BANK FOR

Essentials Of Investments Zvi Bodie, Alex Kane, Alan J. Marcus

Chapter 1-22

Answers are at the end of Each Chapter

Chapter 1

Student name: _____

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

- 1) Financial assets represent _____ of total assets of U.S. households in 2019.
 - A) about 70%
 - B) over 90%
 - C) under 10%
 - D) about 30%

- 2) Real assets in the economy include all but which one of the following?
 - A) Land
 - B) Buildings
 - C) Consumer durables
 - D) Common stock

- 3) In 2019, net worth represented _____ of the liabilities and net worth of commercial banks.
 - A) about 51%
 - B) about 91%
 - C) about 11%
 - D) about 31%

4) According to the *Flow of Funds Accounts of the United States*, the largest single asset of U.S. households is_____.

- A) mutual fund shares
- B) real estate
- C) pension reserves
- D) corporate equity

5) According to the *Flow of Funds Accounts of the United States*, the largest liability of U.S. households is_____.

- A) mortgages
- B) consumer credit
- C) bank loans
- D) gambling debts

6) _____is *not* a derivative security.

- A) A share of common stock
- B) A call option
- C) A futures contract
- D) A put option

7) According to the *Flow of Funds Accounts of the United States*, the largest financial asset of U.S. households is_____.

- A) mutual fund shares
- B) corporate equity
- C) pension reserves
- D) deposits

- 8) Active trading in markets and competition among securities analysts helps ensure that:
1. Security prices approach informational efficiency.
 2. Riskier securities are priced to offer higher potential returns.
 3. Investors are unlikely to be able to consistently find under- or overvalued securities.

- A) 1 only
- B) 1 and 2 only
- C) 2 and 3 only
- D) 1, 2, and 3

- 9) The material wealth of society is determined by the economy's _____, which is a function of the economy's _____.

- A) investment bankers; financial assets
- B) investment bankers; real assets
- C) productive capacity; financial assets
- D) productive capacity; real assets

- 10) Which of the following is *not* a money market security?

- A) U.S. Treasury bill
- B) 6-month maturity certificate of deposit
- C) common stock
- D) mortgage backed security

- 11) _____ assets generate net income to the economy, and _____ assets define allocation of income among investors.

- A) Financial; financial
- B) Financial; real
- C) Real; financial
- D) Real; real

12) Which of the following are financial assets?

1. Debt securities
2. Equity securities
3. Derivative securities

- A) 1 only
- B) 1 and 2 only
- C) 2 and 3 only
- D) 1, 2, and 3

13) _____are examples of financial intermediaries.

- A) Commercial banks
- B) Insurance companies
- C) Investment companies
- D) All of the choices are correct.

14) *Asset allocation* refers to_____.

- A) the allocation of the investment portfolio across broad asset classes
- B) the analysis of the value of securities
- C) the choice of specific assets within each asset class
- D) None of the choices are correct.

15) Which one of the following best describes the purpose of derivatives markets?

- A) Transferring risk from one party to another.
- B) Investing for a short time period to earn a small rate of return.
- C) Investing for retirement
- D) Earning interest income

- 16) *Security selection* refers to the _____.
- A) allocation of the investment portfolio across broad asset classes
 - B) analysis of the broad asset classes
 - C) choice of specific securities within each asset class
 - D) top-down method of investing
- 17) Which of the following is an example of an agency problem?
- A) Managers engage in empire building.
 - B) Managers protect their jobs by avoiding risky projects.
 - C) Managers overconsume luxuries such as corporate jets.
 - D) All of the options are examples of agency problems.
- 18) _____ is (are) a mechanism for mitigating potential agency problems.
- A) Tying income of managers to success of the firm
 - B) Directors defending top management
 - C) Antitakeover strategies
 - D) All of the choices are correct.
- 19) _____ is (are) real assets.
- A) Bonds
 - B) Production equipment
 - C) Stocks
 - D) Life insurance
- 20) _____ portfolio construction starts with selecting attractively priced securities.

- A) Bottom-up
- B) Top-down
- C) Upside-down
- D) Side-to-side

21) In a market economy, capital resources are primarily allocated by_____.

- A) governments
- B) corporation CEOs
- C) financial markets
- D) investment bankers

22) _____represents an ownership share in a corporation.

- A) A call option
- B) Common stock
- C) A fixed-income security
- D) Preferred stock

23) The value of a derivative security_____.

- A) depends on the value of another related security
- B) affects the value of a related security
- C) is unrelated to the value of a related security
- D) can be integrated only by calculus professors

24) Commodity and derivative markets allow firms to adjust their_____.

- A) management styles
- B) focus from their main line of business to their investment portfolios
- C) ways of doing business so that they'll always have positive returns
- D) exposure to various business risks

25) _____ portfolio management calls for holding diversified portfolios without spending effort or resources attempting to improve investment performance through security analysis.

- A) Active
- B) Momentum
- C) Passive
- D) Market-timing

26) Financial markets allow for all but which one of the following?

- A) Shift consumption through time from higher-income periods to lower.
- B) Price securities according to their riskiness.
- C) Channel funds from lenders of funds to borrowers of funds.
- D) Allow most participants to routinely earn high returns with low risk.

27) Financial intermediaries exist because small investors cannot efficiently_____.

- A) diversify their portfolios
- B) gather information
- C) assess and monitor the credit risk of borrowers
- D) All of the choices are correct.

28) Methods of encouraging managers to act in shareholders' best interest include:

1. Threat of takeover.
2. Proxy fights for control of the board of directors.
3. Tying managers' compensation to stock price performance.

- A) 1 only
- B) 1 and 2 only
- C) 2 and 3 only
- D) 1, 2, and 3

29) Firms that specialize in helping companies raise capital by selling securities to the public are called_____.

- A) pension funds
- B) investment banks
- C) savings banks
- D) REITs

30) In securities markets, there should be a risk-return trade-off with higher-risk assets having_____expected returns than lower-risk assets.

- A) higher
- B) lower
- C) the same
- D) The answer cannot be determined from the information given.

31) When the market is more optimistic about a firm, its share price will_____; as a result, it will need to issue_____shares to raise funds that are needed.

- A) rise; fewer
- B) fall; fewer
- C) rise; more
- D) fall; more

32) *Security selection* refers to_____.

- A) choosing specific securities within each asset class
- B) deciding how much to invest in each asset class
- C) deciding how much to invest in the market portfolio versus the riskless asset
- D) deciding how much to hedge

33) An example of a derivative security is _____.

- A) a common share of General Motors
- B) a call option on Intel stock
- C) a Ford bond
- D) a U.S. Treasury bond

34) _____ portfolio construction starts with asset allocation.

- A) Bottom-up
- B) Top-down
- C) Upside-down
- D) Side-to-side

35) Which one of the following firms falsely claimed to have a \$4.8 billion bank account, eventually resulting in the firm's bankruptcy?

- A) WorldCom
- B) Enron
- C) Parmalat
- D) Global Crossing

36) Debt securities promise:

1. A fixed stream of income.
2. A stream of income that is determined according to a specific formula.
3. A share in the profits of the issuing entity.

- A) 1 only
- B) 1 or 2 only
- C) 1 and 3 only
- D) 2 or 3 only

37) The Sarbanes-Oxley Act tightened corporate governance rules by requiring all but which one of the following?

- A) Required that corporations have more independent directors.
- B) Required that the CFO personally vouch for the corporation's financial statements.
- C) Required that firms could no longer employ investment bankers to sell securities to the public.
- D) Required the creation of a new board to oversee the auditing of public companies.

38) The success of common stock investments depends on the success of_____.

- A) derivative securities
- B) fixed-income securities
- C) the firm and its real assets
- D) government methods of allocating capital

39) The historical average rate of return on large company stocks since 1926 has been _____.

- A) about 5%
- B) about 8%
- C) about 12%
- D) about 20%

40) The average rate of return on U.S. Treasury bills since 1926 was_____.

- A) less than 1%
- B) less than 4%
- C) over 4%
- D) over 12%

41) An example of a real asset is:

1. A college education
2. Customer goodwill
3. A patent

- A) 1 only
- B) 2 only
- C) 1 and 3 only
- D) 1, 2, and 3

42) The 2002 law designed to improve corporate governance is titled the_____.

- A) Pension Reform Act
- B) ERISA
- C) Financial Services Modernization Act
- D) Sarbanes-Oxley Act

43) Which of the following is *not* a financial intermediary?

- A) A mutual fund
- B) An insurance company
- C) A real estate brokerage firm
- D) A credit union

44) The combined liabilities of American households in 2019 represent approximately _____of combined assets.

- A) 11%
- B) 13%
- C) 25%
- D) 33%

45) In 2019 real assets represented approximately _____ of the total asset holdings of American households.

- A) 29%
- B) 42%
- C) 48%
- D) 55%

46) In 2019, mortgages represented approximately _____ of total liabilities and net worth of American households.

- A) 9%
- B) 14%
- C) 28%
- D) 42%

47) Liabilities equal approximately _____ of total assets for nonfinancial U.S. businesses in 2019.

- A) 14%
- B) 24%
- C) 44%
- D) 56%

48) Which of the following is *not* an example of a financial intermediary?

- A) Goldman Sachs
- B) Allstate Insurance
- C) First Interstate Bank
- D) IBM

49) Real assets represent about _____ of total assets for commercial banks and savings institutions in 2019.

- A) 1%
- B) 15%
- C) 25%
- D) 40%

50) Money market securities are characterized by:

1. Maturity less than 1 year
2. Safety of the principal investment
3. Low rates of return

- A) 1 only
- B) 1 and 2 only
- C) 1 and 3 only
- D) 1, 2, and 3

51) After much investigation, an investor finds that Intel stock is currently underpriced. This is an example of_____.

- A) asset allocation
- B) security analysis
- C) top-down portfolio management
- D) passive management