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***Principles of Managerial Finance, Brief Ed., 8e* (Zutter/Smart)**
Chapter 2 The Financial Market Environment

2.1 Financial institutions

1) A financial institution is an intermediary that channels the savings of individuals, businesses, and governments into loans or investments.
Answer: TRUE
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

2) Commercial banks advise firms on major transactions such as mergers or financial restructurings.
Answer: FALSE
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

3) As a key participant in financial transactions, individuals are _____.
A) net demanders of funds because they save more money than they borrow
B) net users of funds because they save less money than they borrow
C) net suppliers of funds because they save more money than they borrow
D) net purchasers of funds because they save more money than they borrow
Answer: C
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

4) Government is typically a _____.
A) net provider of funds because it borrows more than it saves
B) net demander of funds because it borrows more than it saves
C) net provider of funds because it can print money at will
D) net demander of funds because it saves more than it borrows
Answer: B
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

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5) Government can obtain funds _____.
A) by trading in the equity market
B) by issuing financial instruments such as futures and options
C) through the foreign exchange market
D) by selling debt securities
Answer: D
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

6) Firms that require funds from external sources can obtain them _____.
A) through financial institutions
B) from central bank directly
C) through the foreign exchange market
D) by issuing T-bills
Answer: A
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

7) Investment banks are institutions that _____.
A) perform all activities of commercial banks and retail banks
B) are exempted from Securities and Exchange Commission regulations
C) engage in trading and market making activities
D) are only limited to capital market activities
Answer: C
Diff: 1
Topic: Commercial Banks, Investment Banks, And The Shadow Banking System
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

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8) Which of the following serves as an intermediary channeling the savings of individuals, businesses, and governments into loans and investments?
A) financial institutions
B) financial markets
C) Securities and Exchange Commission
D) OTC market
Answer: A
Diff: 1
Topic: Financial Institutions
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

9) The shadow banking system describes a group of institutions that engage in lending activities, much like traditional banks.
Answer: TRUE
Diff: 1
Topic: Commercial Banks, Investment Banks, And The Shadow Banking System
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

10) Which of the following provides savers with a secure place to invest funds and offer both individuals and companies loans to finance investments?
A) investment banks
B) securities exchanges
C) mutual funds
D) commercial banks
Answer: D
Diff: 1
Topic: Commercial Banks, Investment Banks, And The Shadow Banking System
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

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11) Which of the following assists companies in raising capital, advise firms on major transactions such as mergers or financial restructuring, and engage in trading and market making activities?
A) investment banks
B) securities exchanges
C) mutual funds
D) commercial banks
Answer: A
Diff: 1
Topic: Commercial Banks, Investment Banks, And The Shadow Banking System
Learning Obj.: LG 1
Learning Outcome: F-01
AACSB: Analytical Thinking

2.2 Financial markets

1) Primary and secondary markets are markets for short-term and long-term securities, respectively.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

2) The over-the-counter (OTC) market is a market for trading smaller and unlisted securities.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

3) NASDAQ is considered an OTC market since it is not recognized by the SEC as a "listed exchange."
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

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4) In the OTC market, the ask price is the highest price offered by a dealer to purchase a given security.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

5) In the Eurobond market**,** corporations and governments typically issue bonds denominated in dollars and sell them to investors located outside the United States.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

6) Capital markets are for investors who want a safe temporary place to deposit funds where they can earn interest and for borrowers who have a short-term need for funds.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

7) Money markets are markets for long-term funds such as bonds and equity.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

8) An efficient market is a market that establishes correct prices for the securities that firms sell and allocates funds to their most productive use as a result of the intense competition among investors.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

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9) Money markets involve the trading of securities with maturities of one year or less.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

10) Eurocurrency deposits arise when a corporation or individual makes a deposit in a bank in a currency other than the local currency of the country where the bank is located.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

11) The Eurocurrency market is a market for short-term bank deposits denominated in U.S. dollars or other easily convertible currencies.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

12) The money market is a financial relationship created by a number of institutions and arrangements that allows suppliers and demanders of long-term funds to make transactions.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

13) The over-the-counter (OTC) market is _____.
A) a highly liquid market as compared to NASDAQ
B) a market in which low risk-high return securities are traded
C) an organized market in which all financial derivatives are traded
D) a market where smaller, unlisted securities are traded
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

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14) Which of the following is TRUE of a primary market?
A) It is an organized market in which all financial derivatives are traded.
B) It is regulated by The Sarbanes-Oxley Act.
C) It is a market where smaller, unlisted securities are traded.
D) It is the only market in which the issuer is directly involved in the transaction.
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

15) Which of the following is TRUE of a secondary market?
A) It is a market for an unlisted company to raise equity capital.
B) It is a market where securities are issued through private placement
C) It is a market in which short-term money market instruments such as Treasury bills are traded.
D) It is a market in which preowned securities are traded.
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

16) Which of the following is TRUE of preferred stock?
A) It has features of bonds and a common stock.
B) It has a claim on assets prior to creditors in the event of liquidation.
C) Its dividends can be paid only after paying dividends to the common stockholders.
D) It usually has a maturity of thirty years.
Answer: A
Diff: 2
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

17) The key securities traded in the capital markets are _____.
A) commercial papers and Treasury bills
B) Treasury bills and certificates of deposit
C) stocks and bonds
D) bills of exchange and commercial papers
Answer: C
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

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18) Which of the following is TRUE of international equity markets?
A) In the international equity market, corporations cannot raise capital through IPOs, instead they can raise capital by trading in the secondary market.
B) In the international equity market, corporations can easily manipulate the price of the shares since it is not regulated by any regulatory bodies.
C) In the international equity market, corporations can only sell blocks of shares to institutional investors from European Union.
D) In the international equity market, corporations can sell blocks of shares to investors in a number of different countries simultaneously.
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

19) Which of the following is TRUE of a dealer market?
A) Buyers and sellers are never brought together directly.
B) Brokers execute the buy or sell orders in a dealer market.
C) It has centralized trading floors.
D) It is a part of the broker market.
Answer: A
Diff: 2
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

20) Which of the following is TRUE of a securities exchange?
A) It serves as an intermediary by channeling the savings of individuals, businesses, and governments into loans or investments.
B) It borrows funds directly from the financial institutions.
C) It is an association of banks who meet to buy and sell stocks and bonds.
D) It provides a marketplace in which firms can raise funds through the sale of new securities and purchasers can resell securities.
Answer: D
Diff: 2
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
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21) A market that establishes correct prices for the securities that firms sell and allocates funds to their most productive uses is called a(n) _____.
A) future market
B) forex market
C) efficient market
D) weak-form market
Answer: C
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

22) The _____ is created by a financial relationship between suppliers and demanders of short-term funds.
A) stock market
B) capital market
C) forex market
D) money market
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

23) By definition, the money market involves the buying and selling of _____.
A) stocks and bonds
B) short-term securities
C) all financial instruments except derivatives
D) secured premium notes
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
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24) Most money market transactions are made in _____.
A) common stock
B) marketable securities
C) commodities market
D) preferred stock
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

25) The _____ is created by a number of institutions and arrangements that allow the suppliers and demanders of long-term funds to make transactions.
A) forex market
B) capital market
C) money market
D) commodities market
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

26) Long-term debt instruments used by both government and business are known as _____.
A) preferred stocks
B) T-bills
C) bonds
D) equities
Answer: C
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
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27) Which of the following is an example of marketable securities?
A) U.S.Treasury bills
B) treasury stock
C) mortgage backed securities
D) loans
Answer: A
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

28) In a _____ market, the buyer and seller are brought together to trade securities in an organization called _____.
A) dealer; securities market
B) broker; over-the -counter market
C) broker; securities market
D) dealer; over-the-counter market
Answer: C
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

29) Financial markets are intermediaries that channel the savings of individuals, businesses, and government into loans or investments.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

30) A public offering is the sale of a new security issue—typically debt or preferred stock—directly to an investor or group of investors.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
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31) A primary market is a financial market in which pre-owned securities are traded.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

32) Most businesses raise money by selling their securities in a _____.
A) public offering
B) forex market
C) futures market
D) commodities market
Answer: A
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

33) Which of the following is a means of selling bonds or stocks to the public?
A) private placement
B) public offering
C) organized selling
D) direct placement
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

34) Which of the following is a forum in which suppliers and demanders of funds can transact business directly?
A) shadow banking system
B) financial markets
C) commercial banks
D) financial institutions
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
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35) The sale of a new security directly to an investor or a group of investors is called _____.
A) arbitraging
B) short selling
C) a capital market transaction
D) a private placement
Answer: D
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

36) The money market is a market where investors trade highly liquid securities with maturities of 1 year or less.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Reflective Thinking

37) The market for short-term bank deposits denominated in dollars and other currencies is the _____.
A) money market
B) Eurocurrency market
C) primary market
D) broker market
Answer: B
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Reflective Thinking

38) The Eurocurrency market is a market where investors can exchange currencies, for example by trading dollars for euros.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
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39) The _____ market is where securities are initially issued and the _____ market is where pre-owned securities (not new issues) are traded.
A) primary; secondary
B) money; capital
C) secondary; primary
D) primary; money
Answer: A
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

40) An efficient market is one where _____.
A) prices of stocks move up and down widely without apparent reason
B) prices of stocks remain low for long periods of time
C) prices of stocks are unaffected by market news
D) the price of a security is an unbiased estimate of its true value
Answer: D
Diff: 1
Topic: The Capital Market
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

41) The _____ represents income to a market maker who helps facilitate securities trading.
A) commission
B) IPO underpricing
C) bid/ask spread
D) cost of doing business
Answer: C
Diff: 2
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

42) You submit an order to buy 100 shares of stock. The price that you pay for the stock is more likely to be the ask price rather than the bid price.
Answer: TRUE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

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43) The money market is a market _____.
A) that enables suppliers and demanders of long-term funds to make transactions
B) which brings together suppliers and demanders of short-term funds
C) where smaller, unlisted securities are traded
D) where all derivatives are traded
Answer: B
Diff: 2
Topic: The Capital Market
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Analytical Thinking

44) In a securities market, the bid price is typically higher than the ask price.
Answer: FALSE
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

45) A _____ is someone who helps facilitate securities trading by offering to buy or sell them at stated bid/ask prices.
A) market maker
B) stockbroker
C) day trader
D) middle man
Answer: A
Diff: 1
Topic: Financial Markets
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

46) Apex Inc. issues a bond of $1,000 which pays interest semiannually at a coupon interest rate of 8%. The maturity of the bond is 15 years. Where should this bond be traded?
A) forex market
B) money market
C) capital market
D) commodities market
Answer: C
Diff: 2
Topic: The Capital Market
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

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47) One piece of evidence suggesting that the stock market is efficient is that most individual investors cannot earn returns that beat the overall market average return, but professional investors such as mutual fund and pension fund managers generally do earn higher-than-average returns.
Answer: FALSE
Diff: 1
Topic: Market Efficiency
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

48) One sign that the stock market is efficient is that prices in the market move seemingly at random, display almost no predictable, repeating patterns.
Answer: TRUE
Diff: 1
Topic: Market Efficiency
Learning Obj.: LG 3
Learning Outcome: F-01
AACSB: Reflective Thinking

2.3 Regulation of financial markets and institutions

1) The Glass-Steagall Act was imposed to allow commercial and investment banks to combine and work together.
Answer: FALSE
Diff: 1
Topic: Financial Institutions and Markets
Learning Obj.: LG 2
Learning Outcome: F-01
AACSB: Analytical Thinking

2) The Glass-Steagall Act _____.
A) was intended to regulate the activities in the secondary market
B) created the Securities Exchange Commission
C) separated the activities of commercial and investment banks
D) was intended to regulate the activities in the primary market
Answer: C
Diff: 2
Topic: Regulations Governing Financial Institutions
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

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3) The Securities Act of 1933 focuses on regulating the sale of securities in the primary market, whereas the 1934 Act deals with the regulations governing the transactions in the secondary market.
Answer: TRUE
Diff: 1
Topic: Regulations Governing Financial Markets
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

4) The Federal Deposit Insurance Corporation (FDIC) _____.
A) is an agency, created by the Glass-Steagall Act, that monitors banks on a regular basis to ensure that they were safe and sound
B) is an agency that monitors business combinations between commercial banks, investment banks, and insurance companies
C) guarantees individuals will not lose any money held at any type of financial institution that fails
D) guarantees individuals will not lose any money, up to a specified amount, held at any type of financial institution that fails
Answer: A
Diff: 1
Topic: Regulations Governing Financial Institutions
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

5) The Gramm-Leach-Bliley Act _____.
A) is created to monitor banks on a regular basis to ensure that they were safe and sound
B) allows business combinations between commercial banks and investment banks, but not insurance companies
C) allows business combinations between commercial banks, investment banks, and insurance companies
D) was signed during the Great Depression because of the financial crisis
Answer: C
Diff: 1
Topic: Regulations Governing Financial Institutions
Learning Obj.: LG 5
Learning Outcome: F-01
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6) Which of the following acts regulates the secondary market?
A) The Securities Act of 1933
B) The Gramm-Leach-Bliley Act
C) The Securities Exchange Act of 1934
D) The Glass-Steagall Act
Answer: C
Diff: 1
Topic: Regulations Governing Financial Markets
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

7) The _____ created new agencies including the Financial Stability Oversight Council and the Bureau of Consumer Financial Protection.
A) Securities Exchange Act of 1934
B) Dodd-Frank Wall Street Reform and Consumer Protection Act
C) Securities Act of 1933
D) Gramm-Leach-Bliley Act
Answer: B
Diff: 1
Topic: Regulations Governing Financial Markets
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Reflective Thinking

8) Which of the following acts regulates the primary market in which securities are originally issued to the public?
A) The Securities Act of 1933
B) The Gramm-Leach-Bliley Act
C) The Securities Exchange Act of 1934
D) The Glass-Steagall Act
Answer: A
Diff: 1
Topic: Regulations Governing Financial Markets
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

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2.4 The securities issuing process

1) A firm conducting an IPO of common stock sold 1 million new shares in the offering at an offer price of $10 per share. After the offering, the firm had 5 million shares outstanding, and the price of those shares in the secondary market was $12. The firm's market capitalization is _____.
A) $60 million
B) $50 million
C) $12 million
D) $10 million
Answer: A
Diff: 2
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

2) A firm conducting an IPO of common stock sold 1 million new shares in the offering at an offer price of $10 per share. After the offering, the firm had 5 million shares outstanding, and the price of those shares in the secondary market was $12. The firm's IPO was underpriced by _____.
A) 0%
B) 100%
C) 20%
D) 16.7%
Answer: C
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

3) A firm conducting an IPO of common stock sold 1 million new shares in the offering at an offer price of $10 per share. After the offering, the firm had 5 million shares outstanding, and the price of those shares in the secondary market was $12. The total proceeds from the firm's IPO were _____.
A) $60 million
B) $50 million
C) $10 million
D) $12 million
Answer: C
Diff: 2
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
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4) Small business investment companies (SBICs) are corporations chartered by the federal government that can borrow at attractive rates from the U.S. Treasury and use the funds to make venture capital investments in private companies.
Answer: TRUE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-15
AACSB: Analytical Thinking

5) Angel capitalists or angels are wealthy individual investors who do not operate as a business but invest in early-stage companies in exchange for a portion of equity.
Answer: TRUE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-15
AACSB: Analytical Thinking

6) A prospectus is another term for a firm's annual report showing the firm's prospects for the coming year.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-15
AACSB: Analytical Thinking

7) Which of the following is an attribute of investment bankers?
A) They make long-term investments for banking institutions.
B) They bear the risk of selling a security issue.
C) They act as middlemen between the issuer and the banker.
D) They provide the issuer with advice relating to the amounts of dividend to be paid.
Answer: B
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-09
AACSB: Analytical Thinking

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8) A prospectus is a portion of the security registration statement that describes the key aspects of the issue, the issuer, and its management and financial position.
Answer: TRUE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-15
AACSB: Analytical Thinking

9) An underwritten issue of common stock is one in which a firm purchases insurance to cover unexpected losses suffered by shareholders.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-15
AACSB: Analytical Thinking

10) A(n)_____ is hired by a firm to find prospective buyers for its new stock or bond issue.
A) securities analyst
B) trust officer
C) commercial loan officer
D) investment banker
Answer: D
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Analytical Thinking

11) When an investment bank buys new securities from a firm and takes on the responsibility of reselling those securities to the public it is engaged in _____.
A) market manipulation
B) underwriting
C) the road show
D) underpricing the security offering
Answer: B
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

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12) _____ is a financial intermediary that specializes in selling new security issues.
A) An investment bank
B) A commercial bank
C) A securities dealer
D) A stock exchange
Answer: A
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

13) The term red herring refers to _____.
A) the fact that most firms conducting an IPO are losing money, also known as running red ink
B) a firm that is conducting an IPO without fully complying with all government regulations
C) the fact that IPOs are typically underpriced
D) an early version of the prospectus with red printing to indicate that the information the document contains is not final
Answer: D
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

14) The IPO offer price is the price at which a newly public firm's shares begin trading in the secondary market.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

15) Which ordering below best describe the level of responsibility for helping a firm conduct an IPO offering (ordering goes from most responsible to least responsible)?
A) originating investment bank > underwriting syndicate > selling group
B) originating investment bank > selling group > underwriting syndicate
C) underwriting syndicate > originating investment bank > selling group
D) selling group > underwriting syndicate > originating investment bank
Answer: A
Diff: 2
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

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16) A group formed by an investment banker to share the financial risk associated with underwriting new securities is called a(n) _____.
A) underwriting syndicate
B) selling group
C) investment banking consortium
D) broker pool
Answer: A
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-09
AACSB: Analytical Thinking

17) The term initial public offering describes a transaction in which a firm sells securities directly to an investor or to a small group of investors.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

18) The document that a company conducting an initial public offering produces to describe the key aspects of the securities offered for sale is called the _____.
A) annual report to stockholders
B) term sheet
C) prospectus
D) tombstone
Answer: C
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

19) When a firm sells stock to the public for the first time the transaction is called _____.
A) an initial public offering
B) a seasoned equity offering
C) a private placement
D) a secondary market offering
Answer: A
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

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20) A venture capitalist is considering investing in a very risky, early stage startup. Compared to investments that the VC might make in less risky companies _____.
A) the VC will pay more for the equity it receives and it will demand a greater share of the startup's equity
B) the VC will pay less for the equity it receives and it will demand a greater share of the startup's equity
C) the VC will pay more for the equity it receives and it will be willing to take a smaller share of the startup's equity
D) the VC will pay less for the equity it receives and it will be willing to take a larger share of the startup's equity
Answer: B
Diff: 2
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

21) Based on the risks of the investments that they make, venture capital firms generally look for rates of return in the 5% to 15% range.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

22) Venture capital firms are usually organized as corporations, and the public shareholders of the VC firm have a stake in the investments that the firm makes.
Answer: FALSE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
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23) One difference between angel investors and venture capitalists is _____.
A) venture capitalists are typically businesses, whereas angel investors are usually individuals
B) venture capitalists invest in risky startups, whereas angel investors put their money into more mature businesses
C) venture capitalists make private equity investments whereas angel investors buy shares in companies in the same way that the rest of the investing public does
D) angel investors are active and typically take a seat of the board of directors of any firm that they provide financing for, whereas venture capital investors are more passive
Answer: A
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

24) When venture capitalists invest money in a firm, they are making a private equity investment.
Answer: TRUE
Diff: 1
Topic: Issuing Common Stock
Learning Obj.: LG 5
Learning Outcome: F-01
AACSB: Reflective Thinking

2.5 Financial markets in crisis

1) When home prices are rising it is easier for homeowners who have fallen behind on their mortgages to get caught up because _____.
A) they can sell their house and buy a smaller one
B) lenders will allow homeowners to use the built-up equity in their home to refinance their mortgages
C) they can rent out an extra room in their homes to earn extra income
D) with rising home prices homeowners will pay less in property taxes and use the savings to make mortgage payments
Answer: B
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 6
Learning Outcome: F-01
AACSB: Analytical Thinking

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2) Subprime mortgages are _____.
A) mortgages that charge the borrower an interest rate that is less than the prime rate of interest
B) mortgages on pieces of real estate located in less than prime neighborhoods
C) loans to borrowers with lower incomes and/or poorer credit histories compared to prime borrowers
D) mortgages on which the borrower has already fallen behind on payments or defaulted
Answer: C
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 6
Learning Outcome: F-01
AACSB: Reflective Thinking

3) Securitization is the process of pooling mortgages or other types of loans and selling the claims or securities against that pool in the secondary market.
Answer: TRUE
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

4) A crisis in the financial sector often spills over into other industries because when financial institutions _____ borrowing, activity in most other industries _____.
A) increase; slows down
B) contract; slows down
C) increase; increases
D) contract; increases
Answer: B
Diff: 1
Topic: Spillover Effects And The Great Recession
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

5) Securitization made it harder for banks to lend money because they could not pass the risk on to other investors.
Answer: FALSE
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

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6) Mortgage-backed securities are securities that represent claims on the cash flows generated by a pool of mortgages.
Answer: TRUE
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

7) Prior to the 2008 financial crisis, most investors viewed mortgage-backed securities as relatively safe investments.
Answer: TRUE
Diff: 1
Topic: Falling Home Prices And Delinquent Mortgages
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

8) Subprime mortgages are mortgage loans made to borrowers with high incomes and better than average credit histories.
Answer: FALSE
Diff: 1
Topic: Falling Home Prices And Delinquent Mortgages
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

9) Recessions associated with a banking crisis tend to be more severe than other recessions because many businesses rely on credit to operate.
Answer: TRUE
Diff: 1
Topic: Spillover Effects And The Great Recession
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

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10) The process of pooling mortgages or other types of loans and selling the claims or securities against that pool in the secondary market is called _____.
A) valuation
B) securitization
C) private placement
D) capital restructuring
Answer: B
Diff: 1
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

11) The primary risk of mortgage-backed securities is _____.
A) that the prices of have high volatility
B) that the prices of housing will increase
C) that the government will not be able to meet the guarantees on the cash flows
D) that homeowners may not be able to, or choose not to, repay their loans
Answer: D
Diff: 2
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

12) Which of the following is TRUE of mortgage-backed securities?
A) Mortgage-backed securities assure a flat 15% return.
B) Mortgage-backed securities are guaranteed by the U.S. government.
C) Mortgage-backed securities can only be purchased by investment banks.
D) Mortgage-backed securities represent claims on the cash flows generated by a pool of homeloans.
Answer: D
Diff: 2
Topic: Financial Institutions and Real Estate Finance
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Analytical Thinking

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13) When home prices are falling, we would expect a(n) _____.
A) high mortgage default rates
B) low mortgage default rates
C) unchanged mortgage default rates
D) higher percentage of owner home equity
Answer: A
Diff: 2
Topic: Falling Home Prices And Delinquent Mortgages
Learning Obj.: LG 4
Learning Outcome: F-01
AACSB: Reflective Thinking

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