



MGT201 All in One.....

Which of the following financial market is referred to the market for short-term government and corporate debt securities?

- ▶ **Money market**
- ▶ Capital market
- ▶ Primary market
- ▶ Secondary market

Which of the following would be deductible as an expense on the corporation's income statement?

- ▶ **Interest paid on outstanding bonds**
- ▶ Cash dividends paid on outstanding common stock
- ▶ Cash dividends paid on outstanding preferred stock
- ▶ All of the given options

In finance, we refer to the market where new securities are bought and sold for the first time as the _____ market.

- ▶ Money market
- ▶ Capital market
- ▶ **Primary market**
- ▶ Secondary market

Felton Farm Supplies, Inc., has an 8 percent return on total assets of Rs.300,000 and a net profit margin of 5 percent. What are its sales?

- ▶ 750,0Rs.3, 750,000
- ▶ **Rs.48Rs.480, 000**
- ▶ Rs.30Rs.300, 000
- ▶ Rs.1, Rs.1, 500,000

An investment proposal should be judged in whether or not it provides:

- ▶ A return equal to the return require by the investor
- ▶ A return more than required by investor
- ▶ A return less than required by investor
- ▶ **A return equal to or more than required by investor**

The value of a bond is directly derived from which of the following?

- ▶ Cash flows
- ▶ Coupon receipts
- ▶ Par recovery at maturity
- ▶ **All of the given options**

A statistical measure of the variability of a distribution around its mean is referred to as _____.

- ▶ A probability distribution
- ▶ The expected return
- ▶ **The standard deviation**
- ▶ Coefficient of variation

A well-diversified portfolio is defined as:

▶ **One that is diversified over a large enough number of securities that the nonsystematic variance is essentially zero**

One that contains securities from at least three different industry sectors

- ▶ A portfolio whose factor beta equals 1.0
- ▶ A portfolio that is equally weighted

What will happen to the expected return on a stock with a beta of 1.5 and a market risk premium of 9% if the Treasury bill yield increases from 3% to 5%?

- ▶ **The expected return will increase by 2.0%**
- ▶ The expected return will remain unchanged
- ▶ The expected return will increase by 1.0%
- ▶ The expected return will increase by 3.0%

How can you limit company-specific risks?

- ▶ Invest in that company's bonds
- ▶ **Invest in a variety of stocks**
- ▶ Invest in securities that do well in a recession
- ▶ Invest in securities that do well in a boom

Why markets and market returns fluctuate?

- ▶ Because of political factors
- ▶ Because of social factors
- ▶ Because of socio-political factors
- ▶ **Because of macro systematic factors**

The use of personal borrowing to change the overall amount of financial leverage to which the individual is exposed is called:

- ▶ Dividend recapture
- ▶ Financial leverage
- ▶ Private debt placement
- ▶ **Homemade leverage**

Which of the following best describes the statement; "The value of an asset is preserved regardless of the nature of the claims against it"?

- ▶ Law of diminishing marginal returns
- ▶ **Law of conservation of value**
- ▶ Law of return on equity
- ▶ Law of return on assets

The amount of current assets that varies with seasonal requirements is referred to as _____ working capital.

- ▶ Permanent
- ▶ Net
- ▶ **Temporary**
- ▶ Gross

Which of the following is an example of a natural hedge?

The prices and costs are both determined in the global market place.

- ▶ The prices are determined in the global market place and costs are determined in the domestic market place.
- ▶ The costs are determined in the global market place and prices are determined in the domestic market place.
- ▶ None of the given options is correct

How should a successful acquisition be evaluated in the long-run?

- ▶ The acquisition is successful if the acquirer is able to increase its earnings per share (EPS), relative to what it would have been without the acquisition.
- ▶ The acquisition is successful if the acquirer is able to reduce its debt-to-total asset ratio, and hence risk, relative to what it would have been without the acquisition.
- ▶ The acquisition is successful if the acquirer is able to diversify its asset base and reduce its overall risk.
- ▶ **The acquisition is successful if the market price of the acquirer's stock increases over what it would have been without the acquisition.**

Which of the following term is used when the firm can independently control considerable assets with a very limited amount of equity?

- ▶ Joint venture
- ▶ **Leveraged buyout (LBO)**
- ▶ Spin-off

► Consolidation
Which of the following would **NOT** be included in inventory carrying cost?

- Insurance expense for the inventory
- Opportunity cost of capital for inventory investment
- **Cost of inventory**
- Cost of shelf space

What would you expect to happen to the price of a share of stock on the day it goes ex-dividend?

- The price should increase by the amount of the dividend
- **The price should decrease by the amount of the dividend**
- The price should decrease by one-half the amount of the dividend
- The price should remain constant

Which of the following is the suggestion of Trade-off theory of capital structure?

- Firms should add leverage whenever interest rates are low
- **Firms with higher operating risk should use less debt**
- Firms should use 50% debt and 50% equity
- Firms should use debt to overcome high par values of stock

What is the basic purpose of financial management?

- **Finding the best opportunities for the use of finance**
- Maintaining the books of accounts of the organization
- Helping managers in managing the employees
- Assessing the nature of employees and motivating them

“Value line” is an agency in America which performs which of the following functions?

- Calculates the NPVs
- Calculates the Correlation coefficients
- Calculates the Annuities
- **Calculates the stock Betas**

In NPV (Net Present Value) calculations, which of the following is used?

- Expected rate of return
- **Required rate of return**
- Both expected rate of return and Required rate of return
- None of the given options

In a market where the SML (Security Market Line) has steep slope, most of the investors are:

- Risk lover
- **Risk averse**
- Gamblers
- None of the given options

If an asset B has steeper SML (security market line) than another asset A, which of the following statements is TRUE?

- Asset A is more risky than asset B
- **Asset B is more risky than asset A**
- Asset B is as risky as Asset A
- None of the given options

Which of the following shows ALL possible risk–return combinations of all stocks in a portfolio, whether these are efficient or not?

- Security market line
- Capital market line
- Parachute graph
- **All of the given options**

According to Traditionalist Theory, when a 100% Equity Firm takes on more and more debt, which of the following phenomenon is observed?

- Share Price first falls, then reaches minimum and finally rises
- Share Price first rises, then reaches minimum and finally falls
- **Share Price first rises, then reaches maximum and finally falls**
- None of the given options

Which of the following formula represents the yield to maturity?

- Interest yield + Market price
- Capital gain yield + Book value
- **Interest yield + Capital gain yield**
- Market price + Capital gain yield

In the WACC equation ($r_D X_D + r_E X_E + r_P X_P$), X_P represents which of the following?

- Weight or Fraction of Total Capital value raised from common stock

- Weight or Fraction of Total Capital value raised from bonds

Weight or Fraction of Total Capital value raised from preferred stock

Weight or Fraction of Total Capital value raised from retained earnings

The date on which the firm’s directors issue a statement about the announcement of dividend is known as:

- **Declaration Date**
- Holder-of-record Date
- Ex-Dividend Date
- Payment Date

You own 150 shares of ABC Company and it offers you the stock splits 2-for-

1. How many additional shares will you receive after stock splits?

- 100
- **150**
- 200
- 300

The decisions regarding working capital management of a firm are mainly concerned with which of the following?

- Current assets & long-term liabilities of balance sheet
- Current assets & current liabilities of balance sheet
- **Fixed assets & current liabilities of balance sheet**
- Fixed assets & long-term liabilities of balance sheet

ABC Company wants to use hedging approach to financing assets. How can the firm use this approach?

- **Finance temporary current assets with long-term liabilities**
- Finance short-term assets with equity
- Finance permanent working capital with long-term liabilities

Finance all assets financed with a mixture of 50% equity and 50% long-term debt

Which of the following is true regarding financial leverage?

- Whenever a firm's equity increases faster than its debt, financial leverage increases
- **Investors can undo the effects of the firm's capital structure by using home-made leverage**
- Increasing financial leverage will always increase the EPS for stockholders

The level of financial leverage that produces the minimum firm value is the most beneficial to stockholders

Suppose that there is no personal or corporate income tax and that the firm's WACC is not affected by its capital structure, then which of the following statements is true?

► **A firm's cost of equity depends on the firm's business and financial risks**

- The value of the firm is dependent on its capital structure
- The cost of equity increases as the firm's leverage decreases
- The greater the financial leverage, the more valuable is the firm

Which of the following is **NOT** a source of spontaneous financing?

- Trade credits
- **Short term loans**
- Accrued taxes
- Wages payable

Which of the following statements depicts the trade-off theory in a better way?

- It states a tradeoff between the costs and benefits of debt financing

It states the tradeoff between the debt financing and equity financing

- There is tradeoff between assets and liabilities of the firm
- There is tradeoff between revenues and expenses of the firm

Value of the firm can be calculated with the help of which of the following formulas?

- **Price of a share x No. of shares outstanding**
- Price of a share x debt / equity
- Price of a share / No. of shares outstanding
- Price of a share x earnings after tax / equity

Company A has to purchase another company. How do Company A pay for buying the other company?

- In Cash
- In Shares
- Bank Borrowing

- **All of the given options**

Which of the following mathematical expressions depicts divestiture?

- $5-1=4$
- $5-1=6$
- $5+1=6$

- **None of the given options**

What happens to the total risk when leverage increases with high rate?

- Total risk increases with slow rate than the leverage
- Total risk increases with decreasing rate
- Total risk remains the same

- **Total risk increases faster than the leverage**

From which of the followings, the stability of the firm can be judged?

- Financial leverage
- Weighted-average cost of capital
- **Capital structure**
- Business risk

You have 25 Indian Rupees and you want to exchange these Indian Rupees with Pakistan Rupees. You go to a money changer and he tells you the selling rate of 1 Indian Rupee is 1.8041 PKR. The rate 1.8041 PKR is referred as:

- Bid rate
- Forward rate
- Future rate
- **Ask rate**

The value at which buyers and sellers are willing to buy and sell any asset is known as:

- Liquidation value
- Book value
- Intrinsic value
- **Market value**

“Do not compare apples with oranges” is the concept in:

- **Discounting and Net present value**
- Risk & return
- Insurance management
- Time value of money

Which of the following statement best describes capital budgeting?

It's a tool which is used to evaluate the projects and fixed assets of the company

- A technique used to assess the working capital requirement
- It will help the management to decide whether the new venture should be taken up or not.

- **All of the given options are correct**

In Pakistan which of the following is assigned to bond rating and risk?

- IMF
- Moody's
- Standard & poor
- **PACRA**

In Gordon's formula ($r_{CE} = DIV1 / P_0 + g$), r_{CE} is considered as _____ and “g” is considered as _____.

- Dividend yield, operating expenses
- Dividend yield, operating income
- Dividend yield, capital loss
- **Dividend yield, capital gain**

What is the long-run objective of financial management?

- Maximize earnings per share
- **Maximize the value of the firm's common stock**
- Maximize return on investment
- Maximize market share

Which of the following statement (in general) is correct?

- A low receivables turnover is desirable
- **The lower the total debt-to-equity ratio, the lower the financial risk for a firm**

► An increase in net profit margin with no change in sales or assets means a weaker ROI

The higher the tax rate for a firm, the lower the interest coverage ratio
What is the present value of a Rs.1,000 ordinary annuity that earns 8% annually for an infinite number of periods?

- Rs.80
- Rs.800
- Rs.1,000
- **Rs.12,500**

Companies and individuals running different types of businesses have to make the choices of the asset according to which of the following?

- Life span of the project
- Validity of the project
- Cost of the capital
- **Return on asset**

What is the advantage of a longer life of the asset?

- Cash flows from the asset becomes non-predictable
- **Cash flows from the asset becomes more predictable**
- Cash inflows from the asset becomes more predictable
- Cash outflows from the asset becomes more predictable

Consider two bonds, A and B. Both bonds presently are selling at their par value of Rs. 1,000. Each pays interest of Rs. 120 annually. Bond A will mature in 5 years while bond B will mature in 6 years. If the yields to maturity on the two bonds change from 12% to 10%, _____.

► Both bonds will increase in value, but bond A will increase more than bond B

► Both bonds will increase in value, but bond B will increase more than bond A

► Both bonds will decrease in value, but bond A will decrease more than bond B

► **Both bonds will decrease in value, but bond B will decrease more than bond A**

Given no change in required returns, the price of a stock whose dividend is constant will _____.

- **Remain unchanged**

► Decrease over time at a rate of $r\%$

► Increase over time at a rate of $r\%$

► Decrease over time at a rate equal to the dividend growth rate

For most firms, P/E ratios and risk _____.

- Will be directly related
- **Will have an inverse relationship**
- Will be unrelated
- Will both increase as inflation increases

Which of the following statement about portfolio statistics is CORRECT?

A portfolio's expected return is a simple weighted average of expected returns of the individual securities comprising the portfolio.

A portfolio's standard deviation of return is a simple weighted average of individual security return standard deviations.

The square root of a portfolio's standard deviation of return equals its variance.

The square root of a portfolio's standard deviation of return equals its coefficient of variation.

Which of the following is simply the weighted average of the possible returns, with the weights being the probabilities of occurrence?

- A probability distribution
- **The expected return**
- The standard deviation
- Coefficient of variation

The square of the standard deviation is known as the _____.

- Beta
- Expected return
- Coefficient of variation
- **Variance**

Why companies invest in projects with negative NPV?

- **Because there is hidden value in each project**
- Because they have chance of rapid growth
- Because they have invested a lot
- All of the given options

An investor was expecting a 18% return on his portfolio with beta of 1.25 before the market risk premium increased from 8% to 10%. Based on this change, what return will now be expected on the portfolio?

- ▶ 22.5%
- ▶ 20.0%
- ▶ **20.5%**
- ▶ 26.0%

Which of the following is the characteristic of a well diversified portfolio?

- ▶ Its market risk is negligible
- ▶ **Its unsystematic risk is negligible**
- ▶ Its systematic risk is negligible
- ▶ All of the given options

How the beta of a stock can be calculated?

- ▶ By monitoring price of the stock
- ▶ By monitoring rate of return of the stock
- ▶ **By comparing the changes in the stock market price to the changes in the stock market index**

Which of the following formula relates beta of the stock to the standard deviation?

- ▶ All of the given options
- ▶ Covariance of stock with market * variance of the market
- ▶ **Covariance of stock with market / variance of the market**
- ▶ Variance of the market / Covariance of stock with market
- ▶ Slope of the regression line

A beta greater than 1 for a stock shows:

- ▶ Stock is relatively more risky than the market
- ▶ If the market moves up by 10% the stock will move up by 12%
- ▶ As the market moves the stock will move in the same direction
- ▶ **All of the given options**

If stock is a part of totally diversified portfolio then its company risk must be equal to:

- ▶ **0**
- ▶ 0.5
- ▶ 1
- ▶ -1

If risk and return combination of any stock is above the SML, what does it mean?

- ▶ It is offering lower rate of return as compared to the efficient stock
- ▶ **It is offering higher rate of return as compared to the efficient stock**
- ▶ Its rate of return is zero as compared to the efficient stock
- ▶ It is offering rate of return equal to the efficient stock

An arbitrage opportunity exists if an investor can construct a _____ investment portfolio that will yield a sure profit.

- ▶ Positive
- ▶ Negative
- ▶ **Zero**
- ▶ All of the given options

Which of the following factors might affect stock returns?

- ▶ The business cycle
- ▶ Interest rate fluctuations
- ▶ Inflation rates
- ▶ **All of the given options**

If arbitrage opportunities are to be ruled out, what would be the expected excess return of each well-diversified portfolio?

- ▶ Inversely proportional to the risk-free rate
- ▶ Inversely proportional to its standard deviation
- ▶ Proportional to its standard deviation
- ▶ **Proportional to its beta coefficient**

Which of the following represent all Risk –Return Combinations for the efficient portfolios in the capital market?

- ▶ Parachute graph
- ▶ **CML straight line equation**
- ▶ Security market line
- ▶ All of the given options

What should be used to calculate the proportional amount of equity financing employed by a firm?

- ▶ The common stock equity account on the firm's balance sheet

- ▶ The sum of common stock and preferred stock on the balance sheet
- ▶ The book value of the firm
- ▶ **The current market price per share of common stock times the number of shares Outstanding**

Which of the following is the market for short term debt?

- ▶ **Money market**
- ▶ Capital market
- ▶ Real asset market
- ▶ Equity market

Bonds are issued in the market at _____.

- ▶ Premium
- ▶ Discount
- ▶ **Both premium and discount**
- ▶ None of the given options

Why debt is a less costly source of fund?

- ▶ **Because additional interest creates a new form of tax shield**
- ▶ Because additional money creates a new form of tax shield
- ▶ Because banks extend loan at lower interest rates
- ▶ None of the given options

Which of the following is as EBIT?

- ▶ Funds provided by operations
- ▶ Earnings before taxes
- ▶ Net income
- ▶ **Operating profit**

Calculate the degree of operating leverage (DOL) at 400,000 units of quantity sold. The firm has Rs.1, 000,000 in fixed costs. The firm anticipates selling each unit for Rs.25 with variable costs of Rs.5 per unit.

- ▶ **3.33**
- ▶ 1.25
- ▶ **1.14**
- ▶ There is not sufficient information provided to calculate the degree of operating leverage (DOL).

A firm has a DOL of 3.5 at Q units. What does this tell us about the firm?

- ▶ If sales rise by 3.5% at the firm, then EBIT will rise by 1%
- ▶ If EBIT rises by 3.5% at the firm, then EPS will rise by 1%
- ▶ If EBIT rises by 1% at the firm, then EPS will rise by 3.5%
- ▶ **If sales rise by 1% at the firm, then EBIT will rise by 3.5%**

Which of the following represents financial leverage?

- ▶ **Use of more debt capital to increase profit**
- ▶ Debt is not used in capital to increase profit
- ▶ High degree of solvency
- ▶ Low degree of solvency

Which of the following best describes the statement; “The value of an asset is preserved regardless of the nature of the claims against it”?

- ▶ Law of diminishing marginal returns
- ▶ **Law of conservation of value**
- ▶ Law of return on equity
- ▶ Law of return on assets

Firm ABC has Rs.5 million in outstanding debt, currently has 200,000 shares outstanding priced at Rs.60 a share, and has a borrowing rate of 10%. If the firm's return on equity is 15%, what is the firm's WACC?

- ▶ 5.00%
- ▶ **3.23%**
- ▶ 4.25%
- ▶ 2.16%

Which of the following statements regarding the M&M Propositions without taxes is true?

- ▶ The total value of the firm depends on how cash flows are divided up between stockholders and bondholders, under M&M Proposition I.
- ▶ The firm's capital structure is relevant under M&M Proposition I.
- ▶ The cost of equity depends on the firm's business risk but not its financial risk, under M&M Proposition II.

Which of the following is correct for the spot exchange rate?

- ▶ **The cost of equity rises as the firm increases its use of debt financing under M&M Proposition II.**

► **This is the rate today for exchanging one currency for another for immediate delivery**

► This is the rate today for exchanging one currency for another at a specific future date

► This is the rate today for exchanging one currency for another at a specific location on a specific future date

► This is the rate today for exchanging one currency for another at a specific location for immediate delivery

The restructuring of a firm should be undertaken, when:

► **The restructuring is expected to create value for shareholders**

► The restructuring is expected to increase earnings per share next year

► The restructuring is expected to increase the firm's market share power in industry

► The current employees will receive additional stock options to align employee interest

Question No: 37 (Marks: 1) - Please choose one

Which of the following term is used when the firm can independently control considerable assets with a very limited amount of equity?

► Joint venture

► **Leveraged buyout (LBO)**

► Spin-off

► Consolidation

cars per year, at a cost of Rs.750 per order, and a carrying cost of Rs.300 per automobile?

► 40 cars

► 71 cars

► **100 cars**

► 126 cars

As the amount of _____ increases the present value of net tax-shield benefits of debt increases.

► **Debt**

► Common equity

► Preferred equity

► Assets

Why the present value of the costs of financial distress increases with increases in the debt ratio?

► Expected return on assets increases

► Present value of the interest tax shield is greater

► Equity tax shield is depleted

► **Probability of default and/or bankruptcy is greater**

The DuPont Approach breaks down the earning power on shareholders' book value (ROE) as follows: $ROE =$ _____

► **Net profit margin \times Total asset turnover \times Equity multiplier**

► Total asset turnover \times Gross profit margin \times Debt ratio

► Total asset turnover \times Net profit margin

► Total asset turnover \times Gross profit margin \times Equity multiplier

Which group of ratios shows the extent to which the firm is financed with debt?

► Liquidity ratios

► **Debt ratios**

► Coverage ratios

► Profitability ratios

Interest paid (earned) on both the original principal borrowed (lent) and previous interest earned is often referred to as _____.

► Present value

► Simple interest

► Future value

► **Compound interest**

A capital budgeting technique that is NOT considered as discounted cash flow method is:

► **Payback period**

► Internal rate of return

► Net present value

► Profitability index

You are selecting a project from a mix of projects, what would be your first selection in descending order to give yourself the best chance to add most to the firm value, when operating under a single-period capital-rationing constraint?

► **Profitability index (PI)**

► Net present value (NPV)

► Internal rate of return (IRR)

► Payback period (PBP)

Which of the following is a legal agreement between the corporation issuing bonds and the bondholders that establish the terms of the bond issue?

► **Indenture**

► Debenture

► Bond

► Bond trustee

What is yield to maturity on a bond?

► It is below the coupon rate when the bond sells at a discount, and equal to the coupon rate when the bond sells at a premium

► **The discount rate that will set the present value of the payments equal to the bond price**

► It is based on the assumption that any payments received are reinvested at the coupon rate

► None of the given options

The value of direct claim security is derived from which of the following?

► Fundamental analysis

► **Underlying real asset**

► Supply and demand of securities in the market

► All of the given options

_____ is equal to (common shareholders' equity/common shares outstanding).

► **Book value per share**

► Liquidation value per share

► Market value per share

► None of the above

The present value of growth opportunities (PVGO) is equal to

The difference between a stock's price and its no-growth value per share

II) The stock's price

III) Zero if its return on equity equals the discount rate

IV) The net present value of favorable investment opportunities

► I and IV

► II and IV

► **I, III, and IV**

► II, III, and IV

Which of the following statement about portfolio statistics is **CORRECT**?

► **portfolio's expected return is a simple weighted average of expected returns of the individual securities comprising the portfolio.**

► portfolio's standard deviation of return is a simple weighted average

Which of the following is NOT a major cause of unsystematic risk.

New competitors ►

New product management ►

Worldwide inflation ►

Strikes ►

Which of the following is the characteristic of a well diversified portfolio?

Its market risk is negligible ►

Its unsystematic risk is negligible ►

Its systematic risk is negligible ►

All of the given options ►

Which of the following factor(s) do NOT affects the movements in the market index?

Macroeconomic factors ►

Socio political factors ►

Social factors ►

All of the given options ►

How much return would be offered by the stock whose (risk and return) pair lies below the SML?

- ▶ No return
- ▶ **Lower return**
- ▶ Average return
- ▶ Excessive return

Market risk is measured in terms of the _____ of the market portfolio or index.

- ▶ Variance
- ▶ Covariance
- ▶ **Standard deviation**
- ▶ Correlation coefficient

What is the meaning of the term “arbitrage”?

- ▶ Buying low and selling high

▶ **Earning risk-free economic profits**

- ▶ Negotiating for favorable brokerage fees
- ▶ Hedging your portfolio through the use of options

Which of the following is the market where tangible or physical asset change hand?

- ▶ Money market
- ▶ Capital market
- ▶ **Real asset market**
- ▶ Equity market

Which of the following is related to the use Lower financial leverage?

- ▶ Fixed cost
- ▶ Variable cost
- ▶ Debt financing

▶ **Common equity financing**

Which of the following will be confronted by the management in deciding the optimal level of current assets for the firm?

▶ **A trade-off between profitability and risk**

- ▶ A trade-off between liquidity and risk
- ▶ A trade-off between equity and debt
- ▶ A trade-off between short-term versus long-term borrowing

Which of the following is an example of a natural hedge?

▶ **The prices and costs are both determined in the global market place.**

- ▶ The prices are determined in the global market place and costs are determined in the domestic market place.
- ▶ The costs are determined in the global market place and prices are determined in the domestic market place.
- ▶ None of the given options is correct

For which of the following strategy; economies of scale, market share dominance, and technological advances are reasons most likely to be offered to justify?

- ▶ Financial acquisition
- ▶ **Strategic acquisition**
- ▶ Divestiture

- ▶ Supermajority merger approval provision

Which of the following is incorrect regarding the costs and benefits of holding inventories and cash?

- ▶ The benefit of higher inventory levels is the reduction in order costs associated with restocking and the reduced chances of running out of material.
- ▶ The costs of higher inventory levels are the carrying costs, which include the cost of space, insurance, spoilage, and the opportunity cost of the capital tied up in inventory.
- ▶ Cash provides liquidity, but it doesn't pay interest. Securities pay interest, but you can't use them to buy things.

▶ **As financial manager you want to hold cash up to the point where the incremental or marginal benefit of liquidity is 25% higher than the cost of holding cash, that is, the interest that you could earn on securities.**

Which of the following is the dividend that is normally paid to shareholders?

- ▶ Stock split
- ▶ Stock dividend
- ▶ Extra dividend
- ▶ **Regular dividend**

A technique that tells us the number of years required to recover our initial cash investment based on the project's expected cash flows is:

- ▶ **Pay back period**

- ▶ Internal rate of return
- ▶ Net present value
- ▶ Profitability index

Assume a company had Rs.1 billion in free cash flow last year, and it is expected to grow that cash flow at 3% into perpetuity. Assuming a 9% cost of equity, what is the present value of the company?

- ▶ **Rs.12.08 billion**
- ▶ Rs.18.15 billion
- ▶ Rs.14.16 billion
- ▶ Rs.16.67 billion

What is the present value of Rs.1,000 to be paid at the end of 5 years if the interest rate is 8% compounded annually?

- ▶ **Rs.680.58**
- ▶ Rs.1,462.23
- ▶ Rs.322.69
- ▶ Rs.401.98

What will be the market risk premium for stock C if the average share of stock C has a required return of 15% and treasury bonds yield is 10%?

- ▶ **5%**
- ▶ 10%
- ▶ 15%
- ▶ 25%

All of the following are used in calculation of required return on a particular stock using SML equation **EXCEPT**:

- ▶ Risk free rate
- ▶ Market risk premium
- ▶ Stock's beta
- ▶ **Stock's price**

On which of the following ground, the Arbitrage Pricing Model is different from the Capital Asset Pricing Model?

- ▶ It places more emphasis on market risk
- ▶ It minimizes the importance of diversification
- ▶ **It recognizes multiple systematic risk factors**
- ▶ It recognizes multiple unsystematic risk factors

According to Traditionalist Theory, when a 100% Equity Firm takes on more and more debt, which of the following phenomenon is observed?

- ▶ Share Price first falls, then reaches minimum and finally rises
- ▶ Share Price first rises, then reaches minimum and finally falls
- ▶ **Share Price first rises, then reaches maximum and finally falls**
- ▶ None of the given options

Which of the following formula represents the yield to maturity?

- ▶ Interest yield + Market price
- ▶ Capital gain yield + Book value
- ▶ **Interest yield + Capital gain yield**
- ▶ Market price + Capital gain yield

Bird-in-the-hand dividend theory was proposed by which of the following?

- ▶ Miller Modigliani
- ▶ **Myron Gordon and John Lintner**
- ▶ Henry Fayol
- ▶ William John and Lehman

XYZ Corporation has offered its shareholders the option that their dividends will be used to purchase additional shares of this corporation. This offer of XYZ Corporation is referred as:

- ▶ Stock repurchases
- ▶ **Dividend reinvestment**
- ▶ Stock dividends
- ▶ Stock splits

When $IRR < WACC$ it means that:

Investment is acceptable as required rate of return is less than cost of capital

▶ **Investment is not acceptable as required rate of return is less than cost of capital**

▶ Investment is acceptable as required rate of return is equal to the cost of capital

- ▶ None of the given options is true

Which of the following statement depicts the disadvantage of issuing debt?

- ▶ Debt financing leads toward unlimited liability

► **If company doesn't pay interest, it can be close down**

- It can improve the return on equity
- Not fixed payment of interest is required by investors

The decisions regarding capital structure of a firm are mainly concerned with which of the following?

► Assets side of balance sheet

► **Liabilities side of balance sheet**

- Expense side of profit and loss account
- Incomes side of profit and loss account

If Current assets = Rs. 16,000,

Current liabilities = Rs. 10,000

Inventory = Rs. 2500

Calculate quick ratio for the firm?

► **1.35**

- 6.0
- 1.60
- 0.25

If an investor is risk averse, then which of the following options best suits him?

- Debentures
- Common stock

► **T-Bills**

► Preferred stock

Capital structure theory is presented by which of the following?

► Robert Alan Hill

► **Modigliani & Miller**

- Brigham & Houston
- Van Horne & Gittman

Which of the following is true regarding financial leverage?

- Whenever a firm's equity increases faster than its debt, financial

leverage increases

► **Investors can undo the effects of the firm's capital structure by using home-made leverage**

► Increasing financial leverage will always increase the EPS for stockholders

► The level of financial leverage that produces the minimum firm value is the most beneficial to stockholders

If a firm wants to use short-term bank loan to finance its temporary current assets and even to buy some of its permanent current inventory, then which of the following policy it is going to adopt?

► **Moderate working capital policy**

- Conservative working capital policy
- Aggressive working capital policy
- Any of the given policy

Which of the following statements depicts the trade-off theory in a better way?

- It states a tradeoff between the costs and benefits of debt financing

► **It states the tradeoff between the debt financing and equity financing**

- There is tradeoff between assets and liabilities of the firm

- There is tradeoff between revenues and expenses of the firm

Modigliani and Miller presented capital structure theory in which of the following years?

► 1950

► **1958**

► 1963

► 1965

In which of the following, synergies are not expected?

- Operating merger
- **Financial merger**
- Vertical Merger
- Horizontal Merger

"Company X wants to merge with Company Y but Company X's management is resisting the merger. Company X asks the shareholders of Company Y to tender their shares in exchange the offered price." This statement refers to which of the following?

► Horizontal Merger

► Vertical Merger

► **Hostile Merger**

► Conglomerate Merger

What happens to the total risk when leverage increases at a slow rate?

- Total risk increases with slow rate than the leverage

- Total risk increases with decreasing rate

- Total risk remains the same

► **Total risk increases faster than the leverage**

According to _____, the firm's cost of equity increases with greater debt financing, while the WACC first decreases and then increases.

► M&M Proposition I with taxes

► M&M Proposition I without taxes

► The traditional theory of capital structure

► **M&M Proposition II without taxes**

Which of the following is incorrect regarding Modigliani and Miller's (MM's) famous debt irrelevance proposition?

It states that firm value can't be increased by changing capital structure

► MM show that the extra return and extra risk balance out, leaving shareholders no better or worse off

► MM's argument rests on simplifying assumptions i.e. efficient capital markets and ignores taxes and costs of financial distress

► **Firm value increases when more debt is used**

Which of the following refers to a unique type of Japanese corporate organization based on a close partnership between government and businesses?

► **Keiretsu**

► Chaebols

► Lean and mean

► Options

Calculate the Forward Rate for Rupee if the interest on 1 Year Maturity in Pakistan is 10% and in Australia is 6% and the current spot rate is Rs.76/ AUD.

► Rs. 6 per AUD

► Rs. 76 per AUD

► **Rs. 79 per AUD**

► Rs. 456 per AUD

Calculate the Forward Rate for Rupee using Interest Rate Parity if the interest on 1 Year Maturity in Pakistan is 10% and on Euro is 6% and the forward rate is Rs.124/ EUR.

► Rs. 6 per EUR

► Rs. 120 per EUR

► **Rs. 124 per EUR**

► Rs. 1240 per EUR

Which of the following would **NOT** improve the current ratio?

► **Borrow short term to finance additional fixed assets**

► Issue long-term debt to buy inventory

► Sell common stock to reduce current liabilities

► Sell fixed assets to reduce accounts payable

Which group of ratios measures how effectively the firm is using its assets?

► Liquidity ratios

► Debt ratios

► **Coverage ratios**

► Activity ratios

The RBS pays 5.60%, compounded daily (based on 360 days), on a 9-month certificate of deposit, if you deposit Rs. 20, 000 you would expect to earn around _____ in interest.

► Rs.840

► **Rs.858**

► Rs.1,032

► Rs.1,121

Assume that the interest rate is greater than zero. Which of the following cash-inflow streams totaling Rs.1, 500 would you prefer? The cash flows are listed in order for Year 1, Year 2, and Year 3 respectively.

► **Rs.700 Rs.500 Rs.300**

- ▶ Rs.300 Rs.500 Rs.700
- ▶ Rs.500 Rs.500 Rs.500
- ▶ Any of the above, since they each sum to Rs.1,500

Which of the following would be considered a cash-flow item from an "operating activity"?

▶ **Cash outflow to the government for taxes**

- ▶ Cash outflow to shareholders as dividends
- ▶ Cash inflow to the firm from selling new common equity shares
- ▶ Cash outflow to purchase bonds issued by another company

Which of the following will **NOT** equate the future value of cash inflows to the present value of cash outflows?

- ▶ Discount rate
- ▶ **Profitability index**
- ▶ Internal rate of return
- ▶ Multiple Internal rate of return

Which of the following is a legal agreement between the corporation issuing bonds and the bondholders that establish the terms of the bond issue?

▶ **Indenture**

- ▶ Debenture
- ▶ Bond
- ▶ Bond trustee

_____ is a high-risk, high-yield bond.

- ▶ Zero coupon bond
- ▶ Mortgage bond
- ▶ **Junk bond**
- ▶ Income bond

A coupon bond pays annual interest, has a par value of Rs.1,000, matures in 4 years, has a coupon rate of 10%, and has a yield to maturity of 12%. What is the current yield on this bond?

- ▶ **10.65%**
- ▶ 10.45%
- ▶ 10.95%
- ▶ 10.52%

When a bond will sell at a discount?

- ▶ The coupon rate is greater than the current yield and the current yield is greater than yield to maturity
- ▶ The coupon rate is greater than yield to maturity
- ▶ The coupon rate is less than the current yield and the current yield is greater than the yield to maturity

▶ **The coupon rate is less than the current yield and the current yield is less than yield to maturity**

What is the price of a stock?

- ▶ The future value of all expected future dividends, discounted at the dividend growth rate
- ▶ The present value of all expected future dividends, discounted at the dividend growth rate
- ▶ The future value of all expected future dividends, discounted at the investor's required return

▶ **The present value of all expected future dividends, discounted at the investor's required return**

Which of the following combinations will produce the highest growth rate? Assume that the firm's projects offer a higher expected return than the market capitalization rate.

- ▶ **A high plowback ratio and a high P/E ratio**
- ▶ A high plowback ratio and a low P/E ratio
- ▶ A low plowback ratio and a low P/E ratio
- ▶ A low plowback ratio and a high P/E ratio

Diversification can reduce risk by spreading your money across many different _____.

- ▶ Investments
- ▶ Markets
- ▶ Industries
- ▶ **All of the given options**

The square of the standard deviation is known as the _____.

- ▶ Beta

- ▶ Expected return
- ▶ Coefficient of variation

▶ **Variance**

Which of the following is **NOT** a major cause of systematic risk.

- ▶ A worldwide recession
- ▶ A world war
- ▶ World energy supply

▶ **Company management change**

_____ means expanding the number of investments which cover different kinds of stocks.

- ▶ **Diversification**
- ▶ Standard deviation
- ▶ Variance
- ▶ Covariance

Which of the following would **NOT** be the part of the risk if the stock is a single stock investment?

- ▶ Company specific risk
- ▶ Un-diversifiable risk
- ▶ **Diversifiable risk**
- ▶ Random risk

To limit volatility what should be the appropriate action?

- ▶ **To diversify**
- ▶ To check the stocks prices daily
- ▶ To own just a few securities
- ▶ Not to invest in risky securities

In efficient market the stock price depends upon the required return which depends upon _____.

- ▶ **Market risk**
- ▶ Total risk
- ▶ Diversified risk
- ▶ Non-Systematic risk

Why markets and market returns fluctuate?

- ▶ Because of political factors
- ▶ Because of social factors
- ▶ Because of socio-political factors

▶ **Because of macro systematic factors**

The overall (weighted average) cost of capital is composed of weighted averages of which of the following?

- ▶ The cost of common equity and the cost of debt
- ▶ The cost of common equity and the cost of preferred stock
- ▶ The cost of preferred stock and the cost of debt

▶ **The cost of common equity, the cost of preferred stock, and the cost of debt**

Which of the following costs would be considered a fixed cost?

- ▶ Raw materials
- ▶ **Depreciation**
- ▶ Bad-debt losses
- ▶ Production labor

Assume the nominal interest rates (annual) in the country of Freedonia and the United States are 6% and 12% respectively. What is the implied 90-day forward rate if the current spot rate is 5 Freedonian marks (FM) per U.S. dollar?

- ▶ 4.732
- ▶ **4.927**
- ▶ 5.074
- ▶ 5.283

$1 + (.12/4) = 1.03$; $1 + (.06/4) = 1.015$; $FM / 5 = (1.015 / 1.03)$; $FM = 4.927$.

A firm that acquires another firm as part of its strategy to sell off assets, cut costs, and operates the remaining assets more efficiently is engaging in

- ▶ A strategic acquisition
- ▶ **A financial acquisition**
- ▶ Two-tier tender offer
- ▶ Shark repellent

When a firm can acquire another firm?

- ▶ Only by purchasing the assets of the target firm
- ▶ Only by purchasing the common stock of the target firm

► By either purchasing the assets or the common equity of the target firm

- None of the given options

Which of the following is **NOT** a type of financial lease arrangement?

► Sale and leaseback

► **Indirect leasing**

► Leveraged leasing

► All of the given options

The Board of Directors announces the amount and date of the next dividend on the _____ date; while the _____ date is the first date on which the purchaser of a stock is no longer entitled to the recently declared dividend.

► Declaration; record

► Ex-dividend; record

► **Declaration; ex-dividend**

► Payment; record

What would you expect to happen to the price of a share of stock on the day it goes ex-dividend?

► **The price should increase by the amount of the dividend**

► The price should decrease by the amount of the dividend

► The price should decrease by one-half the amount of the dividend

► The price should remain constant

What is the amount of the annual interest tax shield for a firm with Rs. 3 million in debt that pays 12% interest if the firm is in the 35% tax bracket?

► **Rs.126, 000**

► Rs.234, 000

► Rs.360, 000

► Rs.1, 050,000

Tax Shield $=(\text{income} - (\text{debt} \times \text{interest rate})) \times \text{tax rate}$
 $= (3000000) \times 12\% \times 35\%$

While calculating the Stock Portfolio Risk using 3x3 Matrix Approach, non-diagonal terms shown in Boxes are called:

► Variance

► Coefficient

► **Covariance**

► Correlation

While calculating the stock beta graphically, the formula to calculate the beta coefficient for stock B is:

► $(r_M^* - r_{RF}) / (r_B^* - r_{RF})$

► **$(r_B^* - r_{RF}) / (r_M^* - r_{RF})$**

► $(r_B^* - r_{RF}) / r_{RF}$

► $(r_B^* - r_{RF}) / r_M^*$

While analyzing any portfolio the value of "r" represents which of the following?

► Internal rate of return

► Expected rate of return

► **Required rate of return**

► Assumed rate of return

If a stock is part of totally diversified portfolio then which of the following is TRUE for that stock?

► Stock's total Risk = Company Risk

► Stock's total Risk = Market Risk

► **Stock's total Risk = Market Risk + Company Risk**

► All of the given options

High uncertainty is associated with which of the following?

► Preferred stock

► **Common stock**

► Bonds

► T-Bills

The date on which the names of stockholders in the Stock Transfer Register of firm are documented is referred as:

► Declaration Date

► **Holder-of-record Date**

► Ex-Dividend Date

► Payment Date

Operating revenue can be calculated from which of the following formulas?

► Operating Revenue = Fixed cost * Quantity + Variable cost

► Operating Revenue = Price / Quantity + Variable cost

► Operating Revenue = Sale price * Quantity

► Operating Revenue = Variable cost * Quantity / Fixed cost

Which of the following statements is **TRUE** about an aggressive approach to finance working capital?

► Financing seasonal requirements of current assets with short-term debt and permanent requirement of current assets with long term debt

► Financing permanent requirements of current assets with short-term debt and seasonal requirement of current assets with long term debt

► **Financing seasonal as well as permanent requirements of current assets with short-term debt**

► Financing seasonal as well as permanent requirements of current assets with long term debt

Capital structure theory is presented by which of the following?

► Robert Alan Hill

► **Modigliani & Miller**

► Brigham & Houston

► Van Horne & Gittman

All of the following are the examples of permanent financing **EXCEPT**:

► Common Equity

► **Current Liabilities**

► Long-term Loans

► Bonds

Which of the followings proposes that the value of the firm is independent of its capital structure?

► The Capital Asset Pricing Model

► **M&M capital structure theory**

► The law of variable proportion

► The Law of One Price

Value of the firm can be calculated with the help of which of the following formulas?

► Price of a share x No. of shares outstanding

► Price of a share x debt / equity

► Price of a share / No. of shares outstanding

► Price of a share x earnings after tax / equity

If the sales are expected to be poor in future than management wants to raise capital through which of the following:

► Debt financing

► Equity financing (common & preferred stock)

► Term finance certificates

► National saving certificates

Company A has to purchase another company. How do Company A pay for buying the other company?

► In Cash

► In Shares

► Bank Borrowing

► All of the given options

Which of the following mathematical expressions depicts divestiture?

► $5-1=4$

► $5-1=6$

► $5+1=6$

► **None of the given options**

Under efficient market, the effect of debt on WACC can be represented with the help of which of the following?

► **Straight line**

► U shaped curve

► Concave

► Time to time fluctuation

Under traditional view, the effect of debt on WACC can be represented with the help of which of the following?

► Straight line

► **U shaped curve**

► Concave

► Time to time fluctuation

According to the trade off theory, value of the firm rises as a result of

► **Tax saving**

- Increase in EPS
- Increase in EBIT
- Saving in cost of debt

Which of the following statements is true about business risk?

- The financial risk of a firm decreases when it takes on a risky project
- The financial risk of a firm increases when it takes on more equity

The business risk of a firm increases when it takes on a risky project

- The business risk of a firm increases when it takes on more debt

Under Net income approach, which of the following is a correct sequence of calculating cost of capital?

- Net income – Total firm's market value – WACC
- Net income – WACC – total firm's market value
- WACC – Net income – market value of equity
- Market value of firm – WACC – Net income

From which of the following equations, net income can be calculated?

- $NI = (EBIT - x_D r_D) (1 - T_c)$
- $NI = (EAT - x_D r_D) (1 - T_c)$
- $NI = (EBIT + x_D r_D) (1 - T_c)$
- $NI = (EBIT - x_D r_D) / (1 - T_c)$

Which of the following refers to a unique type of Japanese corporate organization based on a close partnership between government and businesses?

- **Keiretsu**
- Chaebols
- Lean and mean
- Options

Which of the following is a South Korea type business in that is a conglomerate with Monopoly power?

- Keiretsu
- **Chaebols**
- Lean and mean
- Options

What is bid rate for currency?

- **Buying rate for currency**
- Selling rate of currency
- Forward rate of currency
- Ask rate of currency

What is the primary principle for money changers?

- Ask rate should be less than bid rate
- **Ask rate should be greater than bid rate**
- Ask rate should be equal to bid rate
- Bid rate should be greater than ask rate

Which type of responsibilities are primarily assigned to Controller and Treasurer respectively?

► **Operational; financial management**

- Financial management; accounting
- Accounting; financial management
- Financial management; operations

Which of the following statement (in general) is correct?

- A low receivables turnover is desirable

► The lower the total debt-to-equity ratio, the lower the financial risk for a firm

► An increase in net profit margin with no change in sales or assets means a weaker ROI

The higher the tax rate for a firm, the lower the interest coverage ratio

Which group of ratios measures a firm's ability to meet short-term obligations?

- **Liquidity ratios**
- Debt ratios
- Coverage ratios
- Profitability ratios

Which group of ratios measures how effectively the firm is using its assets?

- Liquidity ratios
- Debt ratios
- Coverage ratios
- **Activity ratios**

Which group of ratios shows the extent to which the firm is financed with debt?

- Liquidity ratios
- **Debt ratios**
- Coverage ratios
- Profitability ratios

Interest payments, principal payments, and cash dividends are _____ the typical budgeting cash-flow analysis because they are _____ cash flows.

- Included in; financing
- **Excluded from; financing**
- Included in; operating
- Excluded from; operating

Which of the following make the calculation of NPV difficult?

- Estimated cash flows
- Discount rate
- Anticipated life of the business
- **All of the given options**

If a company issues bonus shares, what will be its effect on the debt equity ratio?

- It will improve
- It will deteriorate

► **No effect**

- None of the given options

For most firms, P/E ratios and risk _____.

- Will be directly related
- **Will have an inverse relationship**

- Will be unrelated

- Will both increase as inflation increases

Which of the following is the variability of return on stocks or portfolios not explained by general market movements. It is avoidable through diversification?

- Systematic risk
- Standard deviation
- **Unsystematic risk**
- Financial risk

The wider the range of possible outcomes i.e. _____.

► The greater the variability in potential Returns that can occur, the greater the Risk

► The greater the variability in potential Returns that can occur, the lesser the Risk

► The greater the variability in potential Returns that can occur, the level of risk remain constant

- None of the given options

Assume that the expected returns of the portfolios are the same but their standard deviations are given in the options given below, which of the option represent the most risky portfolio according to standard deviation?

- 1.5%
- 2.0%
- 3.0%
- **4.0%**

Which of the following is a drawback of percentage of sales method?

- It is a rough approximation
- There is change in fixed asset during the forecasted period
- Lumpy assets are not taken into account
- **All of the given options**

The objective of financial management is to maximize _____ wealth.

- Stakeholders
- **Shareholders**
- Bondholders
- Directors

Which of the following is correct regarding the opportunity cost of capital for a project?

► The opportunity cost of capital is the return that investors give up by investing in the project rather than in securities of equivalent risk.

► Financial managers use the capital asset pricing model to estimate the opportunity cost of capital

► The company cost of capital is the expected rate of return demanded by investors in a company.

► **All of the given options**

Which of the following is equal to the market risk, beta, of a security?

► **The covariance between the security's return and the market return divided by the variance of the market's returns**

► The covariance between the security and market returns divided by the standard deviation of the market's returns

► The variance of the security's returns divided by the covariance between the security and market returns

► The variance of the security's returns divided by the variance of the market's returns

If risk and return combination of any stock is above the SML, what does it mean?

► It is offering lower rate of return as compared to the efficient stock

► **It is offering higher rate of return as compared to the efficient stock**

► Its rate of return is zero as compared to the efficient stock

► It is offering rate of return equal to the efficient stock

If we invest in many securities which are _____ to each other then it is possible to reduce overall risk for your investment.

► Comparable

► Parallel

► Highly correlated

► **Negatively correlated**

Why common stock of a company must provide a higher expected return than the debt of the same company?

► There is less demand for stock than for bonds

► There is greater demand for stock than for bonds

► **There is more systematic risk involved for the common stock**

► There is a market premium required for bonds

The ABC Company relies on preferred stock, bonds, and common stock for its long-term financing. Rank in ascending order (i.e., 1 = lowest, while 3 = highest) the likely after-tax component costs of the ABC's long-term financing.

► 1 = bonds; 2 = common stock; 3 = preferred stock

► 1 = bonds; 2 = preferred stock; 3 = common stock

► **1 = common stock; 2 = preferred stock; 3 = bonds**

► 1 = preferred stock; 2 = common stock; 3 = bonds

Which of the following is **NOT** a recognized approach for determining the cost of equity?

► Dividend discount model approach

► **Before-tax cost of preferred stock plus risk premium approach**

► Capital-asset pricing model approach

► Before-tax cost of debt plus risk premium approach

Which of the following will be confronted by the management in deciding the optimal level of current assets for the firm?

► **A trade-off between profitability and risk**

► A trade-off between liquidity and risk

► A trade-off between equity and debt

► A trade-off between short-term versus long-term borrowing

Your firm has a philosophy that is analogous to the hedging (maturity matching) approach. Which of the following is the most appropriate non-spontaneous form for financing the excess seasonal current asset needs?

► Trade credit

► 6-month bank notes

► Accounts payable

► **Common stock equity**

Which of the following is the common currency created by the group of European countries?

► The EU currency

► The European Union

► The EMU

► **The Euro**

Which of the following statements is most correct as it relates to the recording of a capital lease?

► The capital lease is shown on the lessee's balance sheet as an asset and amortized over the asset's useful life.

► **The capital lease is listed as an asset on the lessor's balance sheet and amortized over lease term.**

► A capital lease is listed as an asset on the lessee's balance sheet and must be amortized over the lease period.

► A capital lease is listed as an asset on the lessee's balance sheet and must be amortized over the asset's useful life.

Which of the following is the dividend that is normally paid to shareholders?

► Stock split

► Stock dividend

► Extra dividend

► **Regular dividend**

Which of the following signals is most likely to elicit a decrease in share price for slow growth utility company that currently pays a small dividend?

► A repurchase of 5% of the firm's stock

► An unexpected increase in the regular quarterly dividend

► **An unexpected decrease in the regular quarterly dividend**

► Borrowing funds in order to pay a cash dividend

The presence of which of the following costs is **NOT** used as a major argument against the M&M arbitrage process?

► Transaction costs

► **Insurance costs**

► Bankruptcy costs

► Agency costs

Which term would most likely be associated with the phrase "actions speak louder than words?"

► Incentive signaling

► Shareholder wealth maximization

► **Financial signaling**

► Optimal capital structure

When taxes are considered, the value of a levered firm equals the value of the _____.

► Unlevered firm

► Unlevered firm plus the value of the debt

► **Unlevered firm plus the present value of the tax shield**

► Unlevered firm plus the value of the debt plus the value of the tax shield

When financial disaster is looming, why management may borrow to invest in projects having a negative expected NPV?

► The firm's beta is now negative

► Taxes are no longer a concern

► The interest tax shield will cover the loan costs

► **The lender bears all the risk**

What is the present value of Rs.6,500 to be paid at the end of 8 years if the interest rate is 10% compounded annually?

► **Rs.3,032**

► Rs.3,890

► Rs.3,190

► Rs.4,301

What is the present value of Rs.717 to be paid at the end of 2 years if the interest rate is 9% compounded annually?

► **Rs.604**

► Rs.417

► Rs.715

► Rs.556

All of the following are the components of CML (capital market line) equation **EXCEPT**:

► Risk free rate of return

► Risk of the market

► Risk of stock portfolio

► **Net present value**

In NPV (Net Present Value) calculations, which of the following is used?

▶ Excepted rate of return
 ▶ **Required rate of return**
 ▶ Both expected rate of return and Required rate of return
 ▶ None of the given options

If Share A's Beta = +2.0 then it represents which of the following?

▶ **Share is twice as risky (or volatile) as the KSE market**
 ▶ Share is exactly as risky (or volatile) as the KSE market
 ▶ Share is half as risky (or volatile) as the KSE market
 ▶ Share would be exactly as volatile as the KSE market BUT in the opposite way

Beta coefficient is actually the slope of the line that shows the relationship between which of the following?

▶ Stock required rate of return on y-axis and market rate of return on x-axis
 ▶ **Stock expected rate of return on y-axis and market rate of return on x-axis**
 ▶ Stock required rate of return on y-axis and stock expected rate of return on x-axis

Which of the following is/are ideal source(s) of capital for profitable firms because of no transaction costs?

▶ Sizeable Cash
 ▶ Retained Earnings
 ▶ **Both Sizeable Cash and Retained Earnings**
 ▶ None of the given options

According to Traditionalist Theory, when an un-leveraged firm takes on more and more debt, which of the following phenomenon is observed?

▶ Cost of Capital increases, reaches a minimum point, and then falls
 ▶ **Cost of Capital decreases, reaches a minimum point, and then rises**
 ▶ Cost of Capital increases, reaches a maximum point, and then rises
 ▶ None of the given options

In the WACC equation ($r_D x_D + r_E x_E + r_P x_P$), x_E represents which of the following?

▶ Weight or Fraction of Total Capital value raised from bonds
 ▶ Weight or Fraction of Total Capital value raised from preferred stock
 ▶ **Weight or Fraction of Total Capital value raised from common stock**
 ▶ Weight or Fraction of Total Capital value raised from debentures

In the WACC equation ($r_D x_D + r_E x_E + r_P x_P$), x_D represents which of the following?

▶ **Weight or Fraction of Total Capital value raised from bonds**
 ▶ Weight or Fraction of Total Capital value raised from preferred stock
 ▶ Weight or Fraction of Total Capital value raised from common stock

Weight or Fraction of Total Capital value raised from retained earnings

Which of the following represents the tax shield?

▶ **Interest on capital**
 ▶ Dividends to shareholders
 ▶ Retained earnings
 ▶ Establishment expenses

On declaration date of dividend, if ABC Company announces dividend higher than the previous years, which of the following phenomenon is likely to be observe?

▶ Stock price falls
 ▶ **Stock price rises**
 ▶ Stock price remains the same
 ▶ None of the given options

When $IRR < WACC$ it means that:

▶ Investment is acceptable as required rate of return is less than cost of capital
 ▶ **Investment is not acceptable as required rate of return is less than cost of capital**
 ▶ Investment is acceptable as required rate of return is equal to the cost of capital
 ▶ None of the given options is true

ABC Company moves from a "conservative" working capital policy to an "aggressive" policy. Which of the following results it should expect to achieve?

▶ Liquidity to decrease, whereas expected profitability would increase
 ▶ **Expected profitability to increase, whereas risk would decrease**

▶ Liquidity would increase, whereas risk would also increase
 ▶ Risk as well as profitability to decrease

Mr. A, a sole proprietor has purchased the raw material on credit; this transaction has generated which of the following?

▶ Permanent Financing
 ▶ **Spontaneous Financing**
 ▶ Short-term Loan
 ▶ All of the given options

Capital structure that minimizes the WACC is also a structure that maximizes the firm's _____.

▶ Earnings before interest & taxes (EBIT)
 ▶ Earning after tax (EAT)
 ▶ **Earning per share (EPS)**
 ▶ Return on equity (ROE)

In calculations regarding lease, net advantage of leasing is the difference between which of the following?

▶ Present value of net cash flows and present value of cost of leasing
 ▶ **Present value of cost of owning the asset and present value of cost of leasing**
 ▶ Present value of cost of owning the asset and present value of net cash flows
 ▶ None of the given options

A car manufacturing firm buys steel from a steel mill. Both these entities combined together to form a new firm. It is referred to which of the following?

▶ Horizontal Merger
 ▶ **Vertical Merger**
 ▶ Congeneric Merger
 ▶ Conglomerate Merger

Which of the following is a form of divestiture in which a subsidiary or division becomes an independent company?

▶ Sell-off
 ▶ **Spin-off**
 ▶ Liquidation
 ▶ Merger

From which of the following equations, net income can be calculated?

▶ **$NI = (EBIT - x_D r_D) (1 - T_c)$**
 ▶ $NI = (EAT - x_D r_D) (1 - T_c)$
 ▶ $NI = (EBIT + x_D r_D) (1 - T_c)$
 ▶ $NI = (EBIT - x_D r_D) / (1 - T_c)$

Which of the following is the formula to calculate the tax shield?

▶ **Corporate tax rate x Market value of debt**
 ▶ Corporate tax rate / Market value of debt
 ▶ Corporate tax rate + Market value of debt
 ▶ Corporate tax rate - Market value of debt

Which one of the following is correct for the spot exchange rate?

▶ It is the effective exchange rate for a foreign currency for delivery at a specific location on a specific future date
 ▶ **It is the effective exchange rate for a foreign currency for immediate delivery at a specific location**
 ▶ It is the effective exchange rate for a foreign currency for delivery at a specific future date
 ▶ It is the effective exchange rate for a foreign currency for delivery on the current day

What is the primary principle for money changers?

▶ Ask rate should be less than bid rate
 ▶ **Ask rate should be greater than bid rate**
 ▶ Ask rate should be equal to bid rate
 ▶ Bid rate should be greater than ask rate

ABC's and XYZ's debt-to-total assets ratio is 0.4. What is its debt-to-equity ratio?

▶ 0.2
 ▶ 0.77
 ▶ **0.667**
 ▶ 0.333

As interest rates go up, the present value of a stream of fixed cash flows _____.

- ▶ Goes down
- ▶ Goes up
- ▶ Stays the same
- ▶ Can not be found

A 5-year ordinary annuity has a future value of Rs.1,000. If the interest rate is 8 percent, the amount of each annuity payment is closest to which of the following?

- ▶ **Rs.231.91**
- ▶ Rs.184.08
- ▶ Rs.181.62
- ▶ Rs.170.44

$$=i*(1-(1/(1+i)^n))/i$$

$$=(1.08)*(1-(1/(1.08)^5))/0.08=4.312127$$

$$PV=1000/4.312127=231.91$$

Managers prefer IRR over net present value because they evaluate investments:

- ▶ In terms of dollars
- ▶ **In terms of Percentages**
- ▶ Intuitively
- ▶ Logically

When there is single period capital rationing, what would be the most sensible way of making investment decisions?

- ▶ **Choose all projects with a positive NPV**
- ▶ Group projects together to allocate the funds available and select the group of projects with the highest NPV
- ▶ Choose the project with the highest NPV
- ▶ Calculate IRR and select the projects with the highest IRRs

Which of the following is the value of bond that we expect the bond to be?

- ▶ Intrinsic value
- ▶ Fair value
- ▶ **Both intrinsic and fair value**
- ▶ Market price

An investment opportunity set formed with two securities that are perfectly negatively correlated. What will be standard deviation in the global minimum variance portfolio?

- ▶ **Equal to zero**
- ▶ Greater than zero
- ▶ Equal to the sum of the securities' standard deviations
- ▶ Equal to -1

Which of the following value of the shares changes with investor's perception about the company's future and supply and demand situation?

- ▶ Par value
- ▶ **Market value**
- ▶ Intrinsic value
- ▶ Face value

Which of the following statement about portfolio statistics is **CORRECT**?

▶ **A portfolio's expected return is a simple weighted average of expected returns of the individual securities comprising the portfolio.**

▶ A portfolio's standard deviation of return is a simple weighted average of individual security return standard deviations.

▶ The square root of a portfolio's standard deviation of return equals its variance.

▶ The square root of a portfolio's standard deviation of return equals its coefficient of variation.

Which of the following is simply the weighted average of the possible returns, with the weights being the probabilities of occurrence?

- ▶ A probability distribution
- ▶ **The expected return**
- ▶ The standard deviation
- ▶ Coefficient of variation

The ratio of the standard deviation of a distribution to the mean of that distribution is referred to as _____.

- ▶ A probability distribution
- ▶ The expected return
- ▶ The standard deviation
- ▶ **Coefficient of variation**

The Higher the Risk of a Share, the _____ its Rate of Return and the _____ its Market Price.

- ▶ **Higher; Lower**
- ▶ Lower; Higher
- ▶ Higher; Higher
- ▶ Lower; Lower

are employed to assess the financial viability of the project.

- ▶ Financial planning
- ▶ Financial forecasting
- ▶ **Capital budgeting**
- ▶ Capital rationing

The logic behind _____ is that instead of looking at net cash flows you look at cash inflows and outflows separately for each point in time.

- ▶ IRR
- ▶ **MIRR**
- ▶ PV
- ▶ NPV

Expected Portfolio Return = _____

- ▶ **$r_P = x_A r_A + x_B r_B$**
- ▶ $r_P = x_A r_A - x_B r_B$
- ▶ $r_P = x_A r_A / x_B r_B$
- ▶ $r_P = x_A r_A * x_B r_B$

Market risk is measured in terms of the _____ of the market portfolio or index.

- ▶ Variance
- ▶ Covariance
- ▶ **Standard deviation**
- ▶ Correlation coefficient

Which of the following represent all Risk –Return Combinations for the efficient portfolios in the capital market?

- ▶ Parachute graph
- ▶ **CML straight line equation**
- ▶ Security market line
- ▶ All of the given options

Generally companies want to keep the balance in the form of:

- ▶ Debt
- ▶ Equity
- ▶ Hybrid security
- ▶ **Both debt and equity**

A firm has a DFL of 3.5 at X dollars. What does this tell us about the firm?

- ▶ If sales rise by 3.5% at the firm, then EBIT will rise by 1%
- ▶ If EBIT rises by 3.5% at the firm, then EPS will rise by 1%
- ▶ **If EBIT rises by 1% at the firm, then EPS will rise by 3.5%**
- ▶ If sales rise by 1% at the firm, then EBIT will rise by 3.5%

Which of the following is the maximum amount of debt (and other fixed-charge financing) that a firm can adequately service?

- ▶ **Debt capacity**
- ▶ Debt-service burden

- ▶ Adequacy capacity
- ▶ Fixed-charge burden

Which of the following represents financial leverage?

- ▶ **Use of more debt capital to increase profit**
- ▶ Debt is not used in capital to increase profit
- ▶ High degree of solvency
- ▶ Low degree of solvency

Which of the following statements regarding leverage is true?

- ▶ **The ultimate effect of leverage depends on the firm's EBIT**
- ▶ If things go poorly for the firm, increased leverage provides greater returns to shareholders.
- ▶ As a firm lever up, shareholders are exposed to less risk
- ▶ The benefits of leverage always outweigh the costs of financial distress

Your firm has a philosophy that is analogous to the hedging (maturity matching) approach. Which of the following is the most appropriate form for financing a new capital investment in plant and equipment?

- ▶ 6-month bank notes
- ▶ Accounts payable
- ▶ **Common stock equity**
- ▶ Trade credit

Which of the following term is used when the firm can independently control considerable assets with a very limited amount of equity?

- ▶ Joint venture
- ▶ **Leveraged buyout (LBO)**
- ▶ Spin-off
- ▶ Consolidation

Which of the following is **NOT** a form of short-term, spontaneous credit?

- ▶ Accrued wages
- ▶ Trade credit
- ▶ **Commercial paper**
- ▶ Accrued taxes

Which of the following would **NOT** be included in inventory carrying cost?

- ▶ Insurance expense for the inventory
- ▶ Opportunity cost of capital for inventory investment
- ▶ **Cost of inventory**
- ▶ Cost of shelf space

What would be the result when there is an increase in the number of shares outstanding by reducing the par value of stock?

- ▶ **Stock split**
- ▶ Stock dividend
- ▶ Extra dividend
- ▶ Regular dividend

What would you expect to happen to the price of a share of stock on the day it goes ex-dividend?

- ▶ The price should increase by the amount of the dividend
- ▶ **The price should decrease by the amount of the dividend**
- ▶ The price should decrease by one-half the amount of the dividend

▶ The price should remain constant

Which of the following add up to the costs of financial distress?

- ▶ Direct bankruptcy costs, primarily legal and administrative costs
- ▶ Indirect bankruptcy costs, reflecting the difficulty of managing a company when it is in bankruptcy proceedings
- ▶ Costs of the threat of bankruptcy, such as poor investment decisions resulting from conflicts of interest between debtholders and stockholders

- ▶ **All of the given options are correct**

A technique that tells us the number of years required to recover our initial cash investment based on the project's expected cash flows is:

- ▶ **Pay back period**
- ▶ Internal rate of return
- ▶ Net present value
- ▶ Profitability index

Which is the best measure of risk for a single asset held in an isolation, and which is the best measure for an asset held in a diversified portfolio?

- ▶ Variance, correlation coefficient
- ▶ **Standard deviation, correlation coefficient**
- ▶ Beta, variance
- ▶ Coefficient of variation, beta

All of the following are used in calculation of required return on a particular stock using SML equation **EXCEPT**:

- ▶ Risk free rate
- ▶ Market risk premium
- ▶ Stock's beta
- ▶ **Stock's price**

What will be the Stock Y's risk premium if the average share of stock Y has a required return of 20% and beta for that stock is 1.0? In addition, treasury bonds yield is 10%?

- ▶ 5%
- ▶ **10%**
- ▶ 20%
- ▶ 30%

Question No: 34 (Marks: 1) - Please choose one

What should be used to calculate the proportional amount of equity financing employed by a firm?

- ▶ The book value of the firm
- ▶ The sum of common stock and preferred stock on the balance sheet

▶ **The current market price per share of common stock times the number of shares outstanding**

▶ The common stock equity account on the firm's balance sheet

According to Traditionalist Theory, when an un-leveraged firm takes on more and more debt, which of the following phenomenon is observed?

▶ Cost of Capital increases, reaches a minimum point, and then falls

▶ **Cost of Capital decreases, reaches a minimum point, and then rises**

▶ Cost of Capital increases, reaches a maximum point, and then rises

▶ None of the given options

In the WACC equation ($r_D X_D + r_E X_E + r_P X_P$), X_D represents which of the following?

▶ **Weight or Fraction of Total Capital value raised from bonds**

▶ Weight or Fraction of Total Capital value raised from preferred stock

▶ Weight or Fraction of Total Capital value raised from common stock

▶ Weight or Fraction of Total Capital value raised from retained earnings

In residual dividend model, what does the term 'Conservatism' refer?

- ▶ Overvaluation of free cash flows
- ▶ **Underestimation of free cash flows**
- ▶ Overestimation of free cash flows
- ▶ None of the given option

The date on which the names of stockholders in the Stock Transfer Register of firm are documented is referred as:

- ▶ Declaration Date

- ▶ **Holder-of-record Date**
- ▶ Ex-Dividend Date
- ▶ Payment Date

XYZ Corporation has offered its shareholders the option that their dividends will be used to purchase additional shares of this corporation. This offer of XYZ Corporation is referred as:

- ▶ Stock repurchases
- ▶ **Dividend reinvestment**
- ▶ Stock dividends
- ▶ Stock splits

When $IRR < WACC$ it means that:

▶ Investment is acceptable as required rate of return is less than cost of capital

▶ **Investment is not acceptable as required rate of return is less than cost of capital**

▶ Investment is acceptable as required rate of return is equal to the cost of capital

▶ None of the given options is true

Which of the following statement depicts the advantage of raising capital through debt?

- ▶ Debt adds to company specific risk
- ▶ If company does not pay interest it can be close down
- ▶ **It can improve the return on equity**
- ▶ Not required to pay fixed amount of interest

Which of the following can be defined as "additional risk faced by common stockholders if firms take debt."?

- ▶ Unsystematic risk
- ▶ Systematic risk
- ▶ Business risk
- ▶ **Financial risk**

The decisions regarding working capital management of a firm are mainly concerned with which of the following?

- ▶ Current assets & long-term liabilities of balance sheet
- ▶ Current assets & current liabilities of balance sheet
- ▶ **Fixed assets & current liabilities of balance sheet**
- ▶ Fixed assets & long-term liabilities of balance sheet

If Current assets = Rs. 16,000,

Current liabilities = Rs. 10,000

Inventory = Rs. 2500

Calculate **quick ratio** for the firm?

- ▶ **1.35**
- ▶ 6.0
- ▶ 1.60
- ▶ 0.25

Question No: 45 (Marks: 1) - Please choose one

Which of the following states that "Cash is King and only Cash can pay the bills"?

- ▶ Fat cat working capital policy
- ▶ Lean & Mean perspective
- ▶ **Balance Sheet Perspective**
- ▶ Moderate working capital policy

Which of the following depicts the break even point in best way?

- ▶ **EBIT = 0**
- ▶ $EBIT < 0$
- ▶ $EBIT > 0$
- ▶ None of the given options

Financial leverage is considered good in which of the following?

- ▶ Earning after interest & tax / Total asset $>$ Interest cost
- ▶ Earning after interest & tax / Total asset $<$ Interest cost
- ▶ Earning before interest & tax / Total asset $<$ Interest cost

▶ **Earning before interest & tax / Total asset $>$ Interest cost**

Suppose that there is no personal or corporate income tax and that the firm's WACC is not affected by its capital structure, then which of the following statements is true?

▶ **A firm's cost of equity depends on the firm's business and financial risks**

- ▶ The value of the firm is dependent on its capital structure
 - ▶ The cost of equity increases as the firm's leverage decreases
 - ▶ The greater the financial leverage, the more valuable is the firm
- Company A has to purchase another company. How do Company A pay for buying the other company?

- ▶ In Cash
- ▶ In Shares
- ▶ Bank Borrowing
- ▶ **All of the given options**

Among the pairs given below select a(n) example of a principal and a(n) example of an agent respectively.

- ▶ **Shareholder; manager**
- ▶ Manager; owner
- ▶ Accountant; bondholder
- ▶ Shareholder; bondholder

Who determines the market price of a share of common stock?

- ▶ **Individuals buying and selling the stock**
- ▶ The board of directors of the firm
- ▶ The stock exchange on which the stock is listed
- ▶ The president of the company

Which of the following would be deductible as an expense on the corporation's income statement?

- ▶ Interest paid on outstanding bonds
- ▶ Cash dividends paid on outstanding common stock
- ▶ Cash dividends paid on outstanding preferred stock
- ▶ **All of the given options**

How a company can improve (lower) its debt-to-total asset ratio?

- ▶ By borrowing more
- ▶ By shifting short-term to long-term debt
- ▶ By shifting long-term to short-term debt
- ▶ **By selling common stock**

Which of the following statement is most accurate?

- ▶ Coverage ratios also shed light on the "liquidity" of current ratios
- ▶ **Receivable- and inventory-based activity ratios also shed light on the "liquidity" of current assets**
- ▶ Receivable- and inventory-based activity ratios also shed light on the firm's use of financial leverage
- ▶ Liquidity ratios also shed light on the firm's use of financial leverage

Which of the following statements is most correct?

▶ **The future value of an annuity due is greater than an otherwise identical ordinary annuity**

▶ A reduction in the discount rate will increase the future value of an otherwise identical cash flow stream

▶ Continuous compounding will result in a higher present value relative to an otherwise identical investment that is compounded monthly at the same nominal rate

▶ The FVIFA ($i\%$, N periods) equals the sum of the PVIF($i\%$, n) for $n=1$ to N periods

The estimated benefits from a capital budgeting project are expected as cash flows rather than income flows because

- ▶ It is more difficult to calculate income flows than cash flows
- ▶ **It is cash, not accounting income that is central to the firm's capital budgeting decision**

- ▶ This is required by the accounting profession
- ▶ This is required by the Internal Revenue Service (IRS) and enforced through filings with the Securities and Exchange Commission (SEC)

Which of the following technique would be used for a project that has non-normal cash flows?

- ▶ Internal rate of return
- ▶ **Multiple internal rate of return**
- ▶ Modified internal rate of return
- ▶ Net present value

Which one of the following is **NOT** the disadvantage of the asset with very short life?

- ▶ Money has to be reinvested in some other project with uncertain NPV
- ▶ **Money has to be reinvested in some other project with certain NPV**
- ▶ Money has to be reinvested in some other project with return so risky
- ▶ None of the given options

When a bond will sell at a discount?

- ▶ The coupon rate is greater than the current yield and the current yield is greater than yield to maturity
- ▶ The coupon rate is greater than yield to maturity
- ▶ The coupon rate is less than the current yield and the current yield is greater than the yield to maturity
- ▶ **The coupon rate is less than the current yield and the current yield is less than yield to maturity**

Which of the following is designated by the individual investor's optimal portfolio?

- ▶ The point of tangency with the opportunity set and the capital allocation line
- ▶ The point of highest reward to variability ratio in the opportunity set
- ▶ **The point of tangency with the indifference curve and the capital allocation line**
- ▶ The point of the highest reward to variability ratio in the indifference curve

Which of the following statement about portfolio statistics is **CORRECT**?

- ▶ **A portfolio's expected return is a simple weighted average of expected returns of the individual securities comprising the portfolio.**
- ▶ A portfolio's standard deviation of return is a simple weighted average of individual security return standard deviations.
- ▶ The square root of a portfolio's standard deviation of return equals its variance.
- ▶ The square root of a portfolio's standard deviation of return equals its coefficient of variation.

Which of the following is simply the weighted average of the possible returns, with the weights being the probabilities of occurrence?

- ▶ A probability distribution
- ▶ **The expected return**
- ▶ The standard deviation
- ▶ Coefficient of variation

How can you limit company-specific risks?

- ▶ Invest in that company's bonds
- ▶ **Invest in a variety of stocks**
- ▶ Invest in securities that do well in a recession
- ▶ Invest in securities that do well in a boom

To limit volatility what should be the appropriate action?

- ▶ **To diversify**
- ▶ To check the stocks prices daily
- ▶ To own just a few securities
- ▶ Not to invest in risky securities

If risk and return combination of any stock is above the SML, what does it mean?

- ▶ It is offering lower rate of return as compared to the efficient stock

▶ **It is offering higher rate of return as compared to the efficient stock**

- ▶ Its rate of return is zero as compared to the efficient stock
- ▶ It is offering rate of return equal to the efficient stock

What is the meaning of the term "arbitrage"?

- ▶ Buying low and selling high
- ▶ **Earning risk-free economic profits**
- ▶ Negotiating for favorable brokerage fees
- ▶ Hedging your portfolio through the use of options

The ABC Company relies on preferred stock, bonds, and common stock for its long-term financing. Rank in ascending order (i.e., 1 = lowest, while 3 = highest) the likely after-tax component costs of the ABC's long-term financing.

- ▶ 1 = bonds; 2 = common stock; 3 = preferred stock
- ▶ 1 = bonds; 2 = preferred stock; 3 = common stock
- ▶ **1 = common stock; 2 = preferred stock; 3 = bonds**
- ▶ 1 = preferred stock; 2 = common stock; 3 = bonds

Which of the following is **NOT** a recognized approach for determining the cost of equity?

- ▶ Dividend discount model approach
- ▶ **Before-tax cost of preferred stock plus risk premium approach**
- ▶ Capital-asset pricing model approach
- ▶ Before-tax cost of debt plus risk premium approach

The overall (weighted average) cost of capital is composed of weighted averages of which of the following?

- ▶ The cost of common equity and the cost of debt
- ▶ The cost of common equity and the cost of preferred stock
- ▶ The cost of preferred stock and the cost of debt
- ▶ **The cost of common equity, the cost of preferred stock, and the cost of debt**

the cost of debt

Which of the following is related to the use Lower financial leverage?

- ▶ Fixed cost
- ▶ Variable cost
- ▶ Debt financing
- ▶ **Common equity financing**

Which of the following is the cash required during a specific period to meet interest expenses and principal payments?

- ▶ Debt capacity
- ▶ **Debt-service burden**
- ▶ Adequacy capacity
- ▶ Fixed-charge burden

Suppose that the Euro is selling at a forward discount in the forward-exchange market. This implies that most likely

- ▶ The Euro has low exchange-rate risk
- ▶ The Euro is gaining strength in relation to the dollar

▶ **Interest rates are higher in Euroland than in the United States**

- ▶ Interest rates are declining in Europe

Which of the following is a reason suggested by the authors for a divestiture, such as a sell-off or spin-off?

- ▶ Synergy
- ▶ **Reverse synergy**
- ▶ Hubris

- ▶ Economies of scale

The trade terms "1/10, net 45" indicate that _____.

A 45% discount is permitted if payment is made within 10 days

- ▶ A 1% discount is permitted if payment is made within 10 days
- ▶ A 10% discount is permitted if payment is made within 45 days
- ▶ A 1% discount is permitted if payment is made within 45 days

Which of the following refers to a policy of dividend "smoothing"?

- ▶ Maintaining a constant dividend payout ratio
- ▶ Keeping the regular dividend at the same level indefinitely

Maintaining a steady progression of dividend increase over time

- ▶ Alternating cash dividends with stock dividends

Why Investors may prefer lower dividends to higher dividends?

- ▶ The low dividends are more predictable
- ▶ Capital gains may be taxed less heavily than dividends
- ▶ **Of the "bird in the hand" logic**
- ▶ Low dividends indicate heavy investment for the future

Which of the following is **NOT** correct regarding issuing company's repurchase of their shares?

- ▶ Companies pay out money to shareholders by repurchasing their shares
- ▶ **Stock repurchases have grown slowly but gradually in recent years; however they do not substitute for dividends**
- ▶ Instead, repurchases are generally used to make major one-off changes to the firm's capital structure, particularly when cash resources have outrun good investment opportunities

Repurchases can be like bumper dividends; they cause large amounts of cash to be paid to investors when the firm buys back their shares

http://highered.mcgraw-hill.com/sites/0073012386/student_view0/chapter16/multiple_choice_quiz.html

According to MM II, what happens when a firm's debt-to-equity ratio increases?

- ▶ Its financial risk increases
- ▶ Its operating risk increases
- ▶ **The expected return on equity increases**
- ▶ The expected return on equity decreases

If the following are the balance sheet changes, which one of them would **NOT** represent use of funds by a company?

- ▶ **Rs. 8,950 decrease in net fixed assets**
- ▶ Rs. 5,005 decrease in accounts receivable
- ▶ Rs. 10,001 increase in accounts payable
- ▶ Rs. 12,012 decrease in notes payable

Assume a company had Rs.1 billion in free cash flow last year, and it is expected to grow that cash flow at 3% into perpetuity. Assuming a 9% cost of equity, what is the present value of the company?

- ▶ Rs.12.08 billion
- ▶ **Rs.18.15 billion**
- ▶ Rs.14.16 billion
- ▶ Rs.16.67 billion

Formula to be used in this question is

$$PV = \frac{CCF}{(1+g)} \div (r_{CE}-g)$$

$$= 1 \div (1+0.09) \div (0.09-0.03)$$

$$= 18.16667$$

While calculating the stock Beta graphically, y-intercept is known as:

- ▶ Alpha
- ▶ Beta
- ▶ Gamma
- ▶ **None of the given options**

In a market where the SML (Security Market Line) has low slope, most of the investors are:

- ▶ **Risk lover**
- ▶ Risk averse
- ▶ Professional investors
- ▶ None of the given options

What is the assumed value of risk free rate of return in Pakistan?

- ▶ 5%
- ▶ 8%
- ▶ **10%**
- ▶ 12%

In term of diversification, the efficient portfolios must lie on which of the following?

- ▶ **Capital market line**
- ▶ Money market line
- ▶ Security market line
- ▶ None of the given options

Which of the following is/are ideal source(s) of capital for profitable firms because of no transaction costs?

- ▶ Sizeable Cash
- ▶ Retained Earnings
- ▶ **Both Sizeable Cash and Retained Earnings**
- ▶ None of the given options

Which of the following is/are the assumption(s) of MM's (Miller Modigliani) Theory?

- ▶ There are no brokerage costs
- ▶ There are no taxes
- ▶ There are no bankruptcy costs
- ▶ **All of the given options**

How many approaches are used to calculate the required rate of return for common equity?

- ▶ 1
- ▶ **2**
- ▶ 3
- ▶ 5

Which of the following allows to by-pass the errors of forecasting?

- ▶ Capital asset pricing model
- ▶ Gordon's formula
- ▶ Share valuation formula
- ▶ **Standard deviation**

The Impairment of Capital Rule refers to what?

- ▶ Cash Dividends can only be paid from cash
- ▶ **Dividends can not exceed Retained Earnings**

Restricting the dividend payout if earnings are too low to pay interest

- ▶ Investors buy stocks whose dividend policy they like

Question No: 42 (Marks: 1) - Please choose one

Tax Preference Theory suggests that shareholder wealth is maximized by low dividend payout because of which of the following reasons?

Marginal tax rate on dividends is lower than on capital gains

Marginal tax rate on dividends is higher than on capital gains

Marginal tax rate on dividends is equal to capital gains

None of the given options

Company ABC offers its stockholders 10 % stock dividends and Mr. S is one of its stockholders being the owner of 250 stocks. How many shares Mr. S has after availing the stock dividend?

- ▶ 25
- ▶ 50
- ▶ **275**
- ▶ 250

All of the following are considered while computing the working capital of a firm **EXCEPT**:

- ▶ Inventory
- ▶ Accounts Receivables
- ▶ **Accrued expenses**
- ▶ Marketable Securities

Firms increase financial leverage because of the increase in which of the following?

- ▶ Assets
- ▶ **Debt**
- ▶ Equity
- ▶ Expenses

Which of the following is called the father of corporate finance?

- ▶ Prasanna Chandra
- ▶ **Modigliani & Miller**
- ▶ Van Horne & Gittman
- ▶ Robert Alan Hill

Capital structure theory is presented by which of the following?

- ▶ Robert Alan Hill
- ▶ **Modigliani & Miller**
- ▶ Brigham & Houston
- ▶ Van Horne & Gittman

If selling price per unit falls and all other factors remain constant, the operating break-even points (units) will _____.

- ▶ Fall
- ▶ **Rise**
- ▶ Remain the same
- ▶ None of the given options

A car manufacturing company purchases radiators, axles and other parts to be used in manufacturing the car from suppliers rather than making them itself. This refers to which of the following?

- ▶ **Outsourcing**
- ▶ Just in time
- ▶ Aggressive approach
- ▶ Conservative approach

From which of the following, negative net worth of the company is expressed?

- ▶ Experiencing a project failure
- ▶ Competitor's insolvency
- ▶ Experiencing technical insolvency
- ▶ **Experiencing accounting insolvency**

Under which of the following conditions, suppliers may refuse to supply the raw material?

- ▶ **When there is rumor of bankruptcy of the firm**
- ▶ When firms are financed through debt
- ▶ When firms are financed through equity
- ▶ Under uncertain market conditions

Which of the following is not one of the types of merger?

- ▶ Horizontal Merger
- ▶ Vertical Merger
- ▶ **Diagonal Merger**
- ▶ Conglomerate Merger

In which of the following theory the value of the firm increases gradually because of tax savings but with excessive leverage the value starts declining?

- ▶ M&M theory
- ▶ **Trade off theory**
- ▶ Law of diminishing returns
- ▶ Signaling theory

Which of the following statements is true about business risk?

The financial risk of a firm decreases when it takes on a risky project

The financial risk of a firm increases when it takes on more equity

The business risk of a firm increases when it takes on a risky project

The business risk of a firm increases when it takes on more debt

Which of the following type of lease is a long-term lease that is not cancelable and its life often matches the useful life of the asset?

- ▶ **A financial**
- ▶ An operating
- ▶ Both financial & operating lease
- ▶ None of the given options

Which of the following would cause the gross profit margin to remain unchanged, but the net profit margin declined over the same period?

- ▶ Cost of goods sold increased relative to sales
- ▶ Sales increased relative to expenses
- ▶ **Govt. increased the tax rate**
- ▶ Dividends were decreased

The accounting statement of cash flows reports a firm's cash flows segregated into which of the following categorical order?

- ▶ **Operating, investing, and financing**
- ▶ Investing, operating, and financing
- ▶ Financing, operating and investing
- ▶ Financing, investing, and operating

Managers prefer IRR over net present value because they evaluate investments:

- ▶ In terms of dollars
- ▶ **In terms of Percentages**
- ▶ Intuitively
- ▶ Logically

From which of the following category would be the cash flow received from sales revenue and other income during the life of the project?

- ▶ Cash flow from financing activity
- ▶ Cash flow from operating activity
- ▶ Cash flow from investing activity
- ▶ **All of the given options**

Bond is a type of Direct Claim Security whose value is **NOT** secured by _____.

- ▶ Tangible assets
- ▶ **Intangible assets**
- ▶ Fixed assets
- ▶ Real assets

Which one of the following is the right of the issuer to call back or retire the bond by paying off the bondholders before the maturity date?

- ▶ Call in
- ▶ Call option
- ▶ **Call provision**
- ▶ Put option

Which of the following is designated by the individual investor's optimal portfolio?

- ▶ The point of tangency with the opportunity set and the capital allocation line
- ▶ The point of highest reward to variability ratio in the opportunity set
- ▶ **The point of tangency with the indifference curve and the capital allocation line**
- ▶ The point of the highest reward to variability ratio in the indifference curve

Which of the following is **NOT** the form of cash flow generated by the investments of the shareholders?

- ▶ Dividend
- ▶ Capital gain
- ▶ Interest
- ▶ **Dividend**

- ▶ Income
- ▶ Capital loss
- ▶ Capital gain
- ▶ **Operating income**

You wish to earn a return of 13% on each of two stocks, X and Y. Stock X is expected to pay a dividend of Rs. 3 in the upcoming year while Stock Y is expected to pay a dividend of Rs. 4 in the upcoming year. The expected growth rate of dividends for both stocks is 7%. The intrinsic value of stock X:

- ▶ Will be greater than the intrinsic value of stock Y
- ▶ Will be the same as the intrinsic value of stock Y
- ▶ **Will be less than the intrinsic value of stock Y**

▶ Cannot be calculated without knowing the market rate of return
Which of the following is **CORRECT**, if a firm has a required rate of return equal to the ROE?

The firm can increase market price and P/E by retaining more earnings
The firm can increase market price and P/E by increasing the growth rate

The amount of earnings retained by the firm does not affect market price or the P/E

- ▶ None of the given options

Which of the following is **NOT** a major cause of unsystematic risk.

- ▶ New competitors
- ▶ New product management
- ▶ **Worldwide inflation**
- ▶ Strikes

Assume that the expected returns of the portfolios are the same but their standard deviations are given in the options given below, which of the option represent the most risky portfolio according to standard deviation?

- ▶ 1.5%
- ▶ 2.0%
- ▶ 3.0%
- ▶ **4.0%**

The logic behind _____ is that instead of looking at net cash flows you look at cash inflows and outflows separately for each point in time.

- ▶ IRR
- ▶ **MIRR**
- ▶ PV
- ▶ NPV

In which of the following approach you need to bring all the projects to the same length in time?

- ▶ MIRR approach
- ▶ Going concern approach
- ▶ **Common life approach**
- ▶ Equivalent annual approach

Which of the following is equal to the market risk, beta, of a security?

- ▶ **The covariance between the security's return and the market return divided by the variance of the market's returns**
- ▶ The covariance between the security and market returns divided by the standard deviation of the market's returns
- ▶ The variance of the security's returns divided by the covariance between the security and market returns
- ▶ The variance of the security's returns divided by the variance of the market's returns

If you become more aggressive with your investments, which one of the following is likely to occur?

- ▶ Your risk will decrease

- ▶ **Your risk will increase**
- ▶ Your risk will stay the same
- ▶ Your return will be lower

In efficient market the stock price depends upon the required return which depends upon _____.

- ▶ **Market risk**
- ▶ Total risk
- ▶ Diversified risk
- ▶ Non- Systematic risk

How much return would be offered by the stock whose (risk and return) pair lies above the SML?

- ▶ No return
- ▶ Lower return
- ▶ Average return
- ▶ **Excessive return**

Find the Expected Return on the Market Portfolio given that the Expected Return on Stock is 17%, the Risk-Free Rate is 1.1%, and the Beta for Stock is 1.5.

- ▶ **11.7%**
- ▶ 12.14%
- ▶ 13.23%
- ▶ 13.82%

Which of the following represent all Risk –Return Combinations for the efficient portfolios in the capital market?

- ▶ Parachute graph
- ▶ **CML straight line equation**
- ▶ Security market line
- ▶ All of the given options

Assume the nominal interest rates (annual) in the country of Freedonia and the United States are 6% and 12% respectively. What is the implied 90-day forward rate if the current spot rate is 5 Freedonian marks (FM) per U.S. dollar?

- ▶ 4.732
- ▶ **4.927**
- ▶ 5.074
- ▶ 5.283

Which of the following statements is most correct as it relates to the recording of a capital lease?

- ▶ The capital lease is shown on the lessee's balance sheet as an asset and amortized over the asset's useful life.
 - ▶ **The capital lease is listed as an asset on the lessor's balance sheet and amortized over lease term.**
 - ▶ A capital lease is listed as an asset on the lessee's balance sheet and must be amortized over the lease period.
 - ▶ A capital lease is listed as an asset on the lessee's balance sheet and must be amortized over the asset's useful life.
- The trade terms "1/10, net 45" indicate that _____.
- ▶ **A 45% discount is permitted if payment is made within 10 days**
 - ▶ A 1% discount is permitted if payment is made within 10 days
 - ▶ A 10% discount is permitted if payment is made within 45 days
 - ▶ A 1% discount is permitted if payment is made within 45 days
- When the buyer purchases securities through a brokerage house, it is called as:
- ▶ Dutch-auction operation
 - ▶ **Fixed-price operation**
 - ▶ Open-market operation
 - ▶ Fair-warning operation

The presence of which of the following costs is **NOT** used as a major argument against the M&M arbitrage process?

- ▶ Transaction costs

► Insurance costs

- Bankruptcy costs
- Agency costs

An implicit cost of adding debt to the capital structure is that it:

- Adds interest expense to the operating statement
- Increases the required return on equity
- Reduces the expected return on assets
- Decreases the firm's beta

When financial disaster is looming, why management may borrow to invest in projects having a negative expected NPV?

- The firm's beta is now negative
- Taxes are no longer a concern
- The interest tax shield will cover the loan costs
- The lender bears all the risk

What is difference between shares and bonds?

- Bonds represent ownership whereas shares do not
- Shares represent ownership whereas bonds do not
- Shares and bonds both represent equity
- Bonds represent equity whereas shares do not

What is the present value of Rs.53,000 to be paid at the end of 15 years if the interest rate is 9% compounded annually?

- Rs.25,300
- Rs.34,122
- Rs.14,549
- Rs.11,989

Market portion of risk can be represented through which of the following?

- Standard deviation
- Beta coefficient
- Correlation coefficient
- Variance

The KSE (Karachi Stock Exchange) 100 Index represents what?

- The value of Portfolio of Highest volume stocks
- The value of Portfolio of all Stocks
- The value of Portfolio of lowest volume stocks
- None of the given options

All of the following are used in calculation of required return on a particular stock using SML equation **EXCEPT**:

- Risk free rate
- Market risk premium
- Stock's beta
- Stock's price

What will be the Stock Y's risk premium if the average share of stock Y has a required return of 20% and beta for that stock is 1.0? In addition, treasury bonds yield is 10%?

- 5%
- 10%
- 20%
- 30%

Which of the following represents the tax shield?

- Interest on capital
- Dividends to shareholders
- Retained earnings
- Establishment expenses

Which of the following theory suggests that shareholder wealth is maximized by a low Dividend Payout?

- MM Irrelevance Theory
- Bird in the Hand Theory
- Tax Preference Theory
- Signaling Theory

In residual dividend model, what does the term 'Conservatism' refer?

- Overvaluation of free cash flows
- Underestimation of free cash flows
- Overestimation of free cash flows
- None of the given option

Which of the following states that dividends can not exceed retained earnings which are shown in balance sheet?

- Irrelevance theory
- Impairment of Capital Rule
- Bird-in-the-hand rule
- Tax preference theory

Mr. X is going to purchase the stock of ABC Company. Mr. X should purchase the stock on which date so that he can be entitled to receive the dividend, keeping in mind the ex-dividend date is December 7?

- December 6
- December 7
- December 8
- December 9

Which of the following statement shows the total stand alone risk of a firm?

- Unique risk + Market risk
- Diversified risk + Financial risk
- Business risk + Financial risk
- Business risk + Market risk

Which of the following best matches this statement: "A policy under which relatively large amount of cash, marketable securities, and inventories are carried and under which sales are stimulated by a liberal credit policy, resulting in a high level of receivable"?

- Fat cat working capital policy
- Lean & Mean working capital policy
- Moderate working capital policy
- None of the given options

Calculate the return on equity (ROE) of ABC Company using Du Pont equation and the data given below:

Profit Margin= 30%

Asset Turnover= 50%

Leverage Factor = 60%

- 3.6%
- 9%
- 14%
- 33%

Which of the following is the total cost formula?

- Fixed cost * Quantity + Variable cost
- Variable cost * Quantity - Fixed cost
- Variable cost * Quantity + Fixed cost
- Fixed cost * Quantity - Variable cost

Capital structure theory is presented by which of the following?

- Robert Alan Hill
- Modigliani & Miller
- Brigham & Houston
- Van Horne & Gittman

Which of the following statements is correct regarding an aggressive financing policy for a firm relative to a previous conservative policy?

- The firm will use long-term financing to finance all fixed and current assets
- The firm will see an increase in its expected profits than before
- The firm will see a decline in its overall risk profile

► The firm will need to issue additional common stock this period to finance the assets
Under which of the following conditions, suppliers may refuse to supply the raw material?

► **When there is rumor of bankruptcy of the firm**

- When firms are financed through debt
- When firms are financed through equity
- Under uncertain market conditions

Which of the following is also known as service lease?

- Capital Lease
- Financial Lease
- **Operating Lease**
- Sale & Lease-Back

Company A has to purchase another company. How do Company A pay for buying the other company?

- In Cash
- In Shares
- Bank Borrowing
- **All of the given options**

Two businesses at the same level of production are merging together. It is referred as:

- **Horizontal Merger**
- Vertical Merger
- Congeneric Merger
- Conglomerate Merger

Under pure M&M theory, WACC does not change with

- **Change of debt in capital structure**
- Change in EPS
- Change financial expenses
- Change in business risk

According to the trade off theory, value of the firm rises as a result of

- **Tax saving**
- Increase in EPS
- Increase in EBIT
- Saving in cost of debt

From which of the following equations, net income can be calculated?

- **$NI = (EBIT - x_D r_D) (1 - T_c)$**
- $NI = (EAT - x_D r_D) (1 - T_c)$
- $NI = (EBIT + x_D r_D) (1 - T_c)$
- $NI = (EBIT - x_D r_D) / (1 - T_c)$

Calculate the Forward Rate for Rupee using Interest Rate Parity if the interest on 1 Year Maturity in Pakistan is 10% and on Euro is 6% and the forward rate is Rs.124/ EUR.

- Rs. 6 per EUR
- Rs. 120 per EUR
- **Rs. 124 per EUR**
- Rs. 1240 per EUR

Which of the following is known as selling price for currency?

- **Bid rate**
- Ask rate
- Forward rate
- Spot rate

What is the long-run objective of financial management?

- **Maximize earnings per share**
- Maximize the value of the firm's common stock
- Maximize return on investment
- Maximize market share

Which of the following statement (in general) is correct?

- A low receivables turnover is desirable

► **The lower the total debt-to-equity ratio, the lower the financial risk for a firm**

► An increase in net profit margin with no change in sales or assets means a weaker ROI

► The higher the tax rate for a firm, the lower the interest coverage ratio

What is the present value of a Rs.1,000 ordinary annuity that earns 8% annually for an infinite number of periods?

- Rs.80
- Rs.800
- Rs.1,000
- **Rs.12,500**

Companies and individuals running different types of businesses have to make the choices of the asset according to which of the following?

- Life span of the project
- Validity of the project
- Cost of the capital
- **Return on asset**

What is the advantage of a longer life of the asset?

- Cash flows from the asset becomes non-predictable
- **Cash flows from the asset becomes more predictable**
- Cash inflows from the asset becomes more predictable
- Cash outflows from the asset becomes more predictable

Consider two bonds, A and B. Both bonds presently are selling at their par value of Rs. 1,000. Each pays interest of Rs. 120 annually. Bond A will mature in 5 years while bond B will mature in 6 years. If the yields to maturity on the two bonds change from 12% to 10%, ► Both bonds will increase in value, but bond A will increase more than bond B

► **Both bonds will increase in value, but bond B will increase more than bond A**

► Both bonds will decrease in value, but bond A will decrease more than bond B

► Both bonds will decrease in value, but bond B will decrease more than bond A

Given no change in required returns, the price of a stock whose dividend is constant will _____.

- **Remain unchanged**
- Decrease over time at a rate of $r\%$
- Increase over time at a rate of $r\%$
- Decrease over time at a rate equal to the dividend growth rate

For most firms, P/E ratios and risk _____.

- **Will be directly related**
- Will have an inverse relationship
- Will be unrelated
- Will both increase as inflation increases

Which of the following statement about portfolio statistics is **CORRECT**?

► **A portfolio's expected return is a simple weighted average of expected returns of the individual securities comprising the portfolio.**

► A portfolio's standard deviation of return is a simple weighted average of individual security return standard deviations.

► The square root of a portfolio's standard deviation of return equals its variance.

► The square root of a portfolio's standard deviation of return equals its coefficient of variation.

Which of the following is simply the weighted average of the possible returns, with the weights being the probabilities of occurrence?

- A probability distribution

- **The expected return**
- The standard deviation
- Coefficient of variation

The square of the standard deviation is known as the _____.

- Beta
- Expected return
- Coefficient of variation
- **Variance**

Why companies invest in projects with negative NPV?

- **Because there is hidden value in each project**
- Because they have chance of rapid growth
- Because they have invested a lot
- All of the given options

An investor was expecting a 18% return on his portfolio with beta of 1.25 before the market risk premium increased from 8% to 10%.

Based on this change, what return will now be expected on the portfolio?

- **22.5%**
- 20.0%
- 20.5%
- 26.0%

Which of the following is the characteristic of a well diversified portfolio?

- Its market risk is negligible
- **Its unsystematic risk is negligible**
- Its systematic risk is negligible
- All of the given options

How the beta of a stock can be calculated?

- By monitoring price of the stock
- By monitoring rate of return of the stock
- **By comparing the changes in the stock market price to the changes in the stock market index**

- All of the given options

Which of the following formula relates beta of the stock to the standard deviation?

- Covariance of stock with market * variance of the market
- **Covariance of stock with market / variance of the market**
- Variance of the market / Covariance of stock with market
- Slope of the regression line

A beta greater than 1 for a stock shows:

- Stock is relatively more risky than the market

► If the market moves up by 10% the stock will move up by 12%

- As the market moves the stock will move in the same direction

- **All of the given options**

If risk and return combination of any stock is above the SML, what does it mean?

It is offering lower rate of return as compared to the efficient stock

It is offering higher rate of return as compared to the efficient stock

► Its rate of return is zero as compared to the efficient stock

An arbitrage opportunity exists if an investor can construct a _____ investment portfolio that will yield a sure profit.

- **Positive**
- Negative
- Zero
- All of the given options

Which of the following factors might affect stock returns?

- The business cycle
- Interest rate fluctuations
- Inflation rates

- **All of the given options**

If arbitrage opportunities are to be ruled out, what would be the expected excess return of each well-diversified portfolio?

- Inversely proportional to the risk-free rate
- **Inversely proportional to its standard deviation**
- Proportional to its standard deviation
- Proportional to its beta coefficient

Which of the following represent all Risk –Return Combinations for the efficient portfolios in the capital market?

- **Parachute graph**
- CML straight line equation
- Security market line
- All of the given options

Which of the following best describes the statement; “The value of an asset is preserved regardless of the nature of the claims against it”?

- Law of diminishing marginal returns
- Law of conservation of value
- Law of return on equity
- **Law of return on assets**

Firm ABC has Rs.5 million in outstanding debt, currently has 200,000 shares outstanding priced at Rs.60 a share, and has a borrowing rate of 10%. If the firm's return on equity is 15%, what is the firm's WACC?

- 5.00%
- **3.23%**
- 4.25%
- 2.16%

Which of the following statements regarding the M&M Propositions without taxes is true?

► The total value of the firm depends on how cash flows are divided up between stockholders and bondholders, under M&M Proposition I.

- The firm's capital structure is relevant under M&M Proposition I.

I.

► The cost of equity depends on the firm's business risk but not its financial risk, under M&M Proposition II.

► **The cost of equity rises as the firm increases its use of debt financing under M&M Proposition II.**

Which one of the following is correct for the spot exchange rate?

► This is the rate today for exchanging one currency for another for immediate delivery

► **This is the rate today for exchanging one currency for another at a specific future date**

► This is the rate today for exchanging one currency for another at a specific location on a specific future date

► This is the rate today for exchanging one currency for another at a specific location for immediate delivery

The restructuring of a firm should be undertaken, when:

► **The restructuring is expected to create value for shareholders**

► The restructuring is expected to increase earnings per share next year

► The restructuring is expected to increase the firm's market share power in industry

► The current employees will receive additional stock options to align employee interest

Which of the following term is used when the firm can independently control considerable assets with a very limited amount of equity?

- Joint venture
- **Leveraged buyout (LBO)**
- Spin-off

- Consolidation

What is the economic order quantity for an automobile dealer selling 2,000 cars per year, at a cost of Rs.750 per order, and a carrying cost of Rs.300 per automobile?

- 40 cars
- 71 cars
- **100 cars**
- 126 cars

As the amount of _____ increases the present value of net tax-shield benefits of debt increases.

- **Debt**
- Common equity
- Preferred equity
- Assets

Why the present value of the costs of financial distress increases with increases in the debt ratio?

- Expected return on assets increases
- Present value of the interest tax shield is greater
- Equity tax shield is depleted
- **Probability of default and/or bankruptcy is greater**

Who determines the market price of a share of common stock?

- **Individuals buying and selling the stock**
- The board of directors of the firm
- The stock exchange on which the stock is listed
- The president of the company

Which of the following would cause the gross profit margin to remain unchanged, but the net profit margin declined over the same period?

- Cost of goods sold increased relative to sales
- Sales increased relative to expenses
- **Govt. increased the tax rate**
- Dividends were decreased

Which of the following make the calculation of NPV difficult?

- Estimated cash flows
- Discount rate
- **Anticipated life of the business**
- All of the given options

Who is responsible for the decisions relating capital budgeting and capital rationing?

- Chief executive officer
- Junior management
- Division heads
- **All of the given option**

Mortgage bonds are secured by real property whose value is generally _____ than that of the value of the bonds issue?.

- **Higher**
- Lower
- Equal
- Higher or lower

The value of direct claim security is derived from which of the following?

- Fundamental analysis
- **Underlying real asset**
- Supply and demand of securities in the market
- All of the given options

Which of the following would tend to reduce a firm's P/E ratio?

- The firm significantly decreases financial leverage
- The firm increases return on equity for the long term

► **The level of inflation is expected to increase to double-digit levels**

- The rate of return on Treasury bills decreases

How the beta of a stock can be calculated?

- By monitoring price of the stock
- By monitoring rate of return of the stock

► **By comparing the changes in the stock market price to the changes in the stock market index**

- All of the given options

Where the stock points will lie, if a stock is a part of totally diversified portfolio?

- It will lie below the regression line
- It will line above the regression line
- **It will line exactly on the regression line**
- It will be tangent to the regression line

Why debt is a less costly source of fund?

- **Because additional interest creates a new form of tax shield**
- Because additional money creates a new form of tax shield
- Because banks extend loan at lower interest rates
- None of the given options

When a firm can acquire another firm?

- Only by purchasing the assets of the target firm
- Only by purchasing the common stock of the target firm

► **By either purchasing the assets or the common equity of the target firm**

- None of the given options

What is the economic order quantity for an automobile dealer selling 2,000 cars per year, at a cost of Rs.750 per order, and a carrying cost of Rs.300 per automobile?

- 40 cars
- 71 cars
- 100 cars
- 126 cars

The stock in your portfolio was selling for Rs. 40 per share yesterday, but has today declared a three for two stock split. Which of the following statements seems to be true?

- There will be two-thirds as many shares outstanding, and they will sell for Rs.60.00 each
- There will be four times as many shares outstanding, and they will sell for Rs.160.00 each
- **There will be 50 percent more shares outstanding and they will sell for Rs.26.67 each**
- There will be one-and-one-half times as many shares outstanding, and they will sell for Rs.60.00 each

Which of the following's existence on the balance sheet generates tax advantages that directly influence the capital structure of the firm?

- Long-term debt
- Retained earnings
- All of the given answers are correct
- A large proportion of fixed assets

Which of the following is an example of restructuring the firm?

- Dividends are increased from Rs.1 to Rs.2 per share
- A new investment increases the firm's business risk
- New equity is issued and the proceeds repay debt
- **A new Board of Directors is elected to the firm**

While calculating the Stock Portfolio Risk using 3x3 Matrix Approach, the terms shown in Boxes on Diagonal are called:

- Covariance
- **Variance**
- Coefficient
- Correlation

What is the basis of CAPM which describes how the expected return of a stock or portfolio is correlated to the return of the financial market as a whole?

- ▶ Correlation
- ▶ Beta
- ▶ NPV
- ▶ Cash flow

Ahmad is a 40-year-old employee and he wants to invest his money. He should put how much money in stocks?

▶ The amount to be invested is a matter of personal preference, based on the Ahmad's goal for his money

▶ The amount is a matter of personal preference, based on the investment's risk only

▶ The rule of thumb suggests that 40% of his assets be in cash/bonds and the remaining 60% in stocks

▶ The rule of thumb suggests that 60% of his assets be in cash/bonds and the remaining 40% in stocks

If a stock is part of totally diversified portfolio then which of the following is TRUE for that stock?

- ▶ Stock's total Risk = Company Risk
- ▶ Stock's total Risk = Market Risk
- ▶ Stock's total Risk = Market Risk + Company Risk
- ▶ All of the given options

Which of the following is the characteristic of Arbitrage Pricing Model that offers the greatest potential advantage over the Capital Asset Pricing Model?

▶ It gives the variability of coefficients of sensitivity for a given asset over time

▶ It provides accurate measurement of the risk-free rate of return over historical time periods

▶ It uses several factors instead of a single market index to enlighten the risk-return relationship

▶ It identifies the anticipated changes in production, inflation and term structure as key factors in explaining the risk-return relationship

Which of the following is true about the security market line (SML) derived from the Arbitrage pricing model?

▶ The benchmark portfolio for the Security market line may be any well-diversified portfolio

▶ The Security market line for the Arbitrage pricing model has an intercept equal to the expected return on the market portfolio

▶ The Security market line for the Arbitrage pricing model shows expected return in relation to portfolio standard deviation

▶ The Security market line has a downward slope

What should be used to calculate the proportional amount of equity financing employed by a firm?

- ▶ The book value of the firm

The sum of common stock and preferred stock on the balance sheet

▶ The current market price per share of common stock times the number of shares outstanding

- ▶ The common stock equity account on the firm's balance sheet

In the WACC equation ($r_D x_D + r_E x_E + r_P x_P$), x_E represents which of the following?

Weight or Fraction of Total Capital value raised from bonds

Weight or Fraction of Total Capital value raised from preferred stock

Weight or Fraction of Total Capital value raised from common stock

Weight or Fraction of Total Capital value raised from debentures

The Impairment of Capital Rule refers to what?

Cash Dividends can only be paid from cash

Dividends can not exceed Retained Earnings

Restricting the dividend payout if earnings are too low to pay interest

Investors buy stocks whose dividend policy they like

Bird-in-the-hand dividend theory was proposed by which of the following?

- ▶ Miller Modigliani
- ▶ Myron Gordon and John Lintner
- ▶ Henry Fayol
- ▶ William John and Lehman

The date on which the right to the current dividend no longer accompanies a stock is termed as:

- ▶ Declaration Date
- ▶ Holder-of-record Date
- ▶ Ex-Dividend Date
- ▶ Payment Date

Which of the following industry is not the example of high leveraged firm?

- ▶ Textile industry
- ▶ Cement plant
- ▶ Education sector
- ▶ I.T industry

Which of the following current asset investment policy leads firm to maintain small amount of current assets?

- ▶ Fat cat working capital policy
- ▶ Lean & Mean working capital policy
- ▶ Moderate working capital policy
- ▶ All of the given options

Which of the following industries is considered as capital intensive?

- ▶ Pharmaceutical industry
- ▶ Textile industry
- ▶ Information technology
- ▶ Automobile industry

If total assets of the firm are equal to Rs. 2,000 and debt is Rs. 1,000 then the financial leverage of the firm is equal to which of the following? ($FL = \text{Debt} / (\text{Debt} + \text{Equity})$)

- ▶ 40%
- ▶ 50%
- ▶ 60%
- ▶ 65%

Which of the following is called the father of corporate finance?

- ▶ Prasanna Chandra
- ▶ Modigliani & Miller
- ▶ Van Horne & Gittman
- ▶ Robert Alan Hill

XYZ Company is financing its seasonal requirements of current assets with short-term debt and permanent requirement of current assets with long term debt. The firm is using which of the following approach to finance its working capital?

- ▶ Aggressive approach
- ▶ Conservative approach
- ▶ Moderate approach
- ▶ Hybrid approach

NM Corporation is financing its seasonal as well as permanent requirements of current assets with long term debt. The firm is using which of the following approaches to finance its working capital?

- ▶ Aggressive approach
- ▶ Conservative approach
- ▶ Moderate approach
- ▶ Hybrid approach

Mr. A, a sole proprietor has purchased the raw material on credit; this transaction has generated which of the following?

- ▶ Permanent Financing
- ▶ Spontaneous Financing
- ▶ Short-term Loan
- ▶ All of the given options

Which of the following is **NOT** a source of spontaneous financing?

- ▶ Trade credits
- ▶ **Short term loans**
- ▶ Accrued taxes
- ▶ Wages payable

Optimal debt/ equity ratio lies between which of the following range?

- ▶ **20/80 to 70/30**
- ▶ 30/70 to 50/50
- ▶ 40/60 to 60/40
- ▶ 20/80 to 60/40

Company A and Company B merged together in such a way that the combined value and performance of both these companies is greater than the sum of their separate individual parts. This phenomenon is referred as:

- ▶ **Synergy**
- ▶ Acquisition
- ▶ Leveraged buy-out
- ▶ Hostile merger

Which of the following is not one of the types of merger?

- ▶ Horizontal Merger
- ▶ Vertical Merger
- ▶ **Diagonal Merger**
- ▶ Conglomerate Merger

A target firm does not want to be acquired. That's why it has taken an excessive short-term debt to appear unhealthy for the acquiring firm.

This phenomenon is referred as:

- ▶ White Knight
- ▶ **Poison Pill**
- ▶ Leveraged Buy-Outs
- ▶ White squire

Under efficient market, the effect of debt on WACC can be represented with the help of which of the following?

- ▶ **Straight line**
- ▶ U shaped curve
- ▶ Concave
- ▶ Time to time fluctuation

With the increased rate of total risk of the firm, which of the following will be greatly affected?

- ▶ Required rate of return
- ▶ **Expected rate of return**
- ▶ Multiple rate of return
- ▶ Internal rate of return

Which of the following is called as spontaneous financing?

- ▶ Current assets
- ▶ Fixed assets
- ▶ **Current liabilities**
- ▶ Fixed liabilities

Which of the following is NOT the interest rate used for discounting calculation?

- ▶ **Benchmark interest rate**
- ▶ Effective interest rate
- ▶ Periodic interest rate
- ▶ Nominal interest rate

Which of the following is true about payback period?

The regular payback method recognizes all cash flows over a project's life

It recognizes all cash flows over a project's life, and it also adjusts these cash flows to account for the time value of money

It is useful as an indicator of a project's liquidity as it gives an idea that how long it will take to recover the funds invested in a project

The regular payback method was widely used, but virtually no companies even calculate the payback today

Which of the following describes a set of projects where only one project can be selected?

- ▶ Mutually exclusive projects
- ▶ Supplementary projects
- ▶ Complementary projects
- ▶ Independent projects

Risk can be measured with which of the following statistical tool?

- ▶ **Standard deviation**
- ▶ Range
- ▶ T- test
- ▶ Mean, median and mode

Which is the best measure for an asset held in a diversified portfolio?

- ▶ **Beta**
- ▶ Variance
- ▶ Standard deviation
- ▶ Coefficient of variation

Which of the following type of lease is a long-term lease that is not cancelable and its life often matches the useful life of the asset?

- ▶ **A financial**
- ▶ An operating
- ▶ Both financial & operating lease
- ▶ None of the given options

What is potentially the biggest advantage of a small partnership over a sole proprietorship?

- ▶ Unlimited liability
- ▶ Single tax filing
- ▶ Difficult ownership resale

▶ **Raising capital**

What is the present value of a Rs.1,000 ordinary annuity that earns 8% annually for an infinite number of periods?

- ▶ Rs.80
- ▶ Rs.800
- ▶ Rs.1,000

▶ **Rs.12,500**

1000/ .08

As interest rates go up, the present value of a stream of fixed cash flows _____.

- ▶ **Goes down**
- ▶ Goes up
- ▶ Stays the same
- ▶ Can not be found

A capital budgeting technique through which discount rate equates the present value of the future net cash flows from an investment project with the project's initial cash outflow is known as:

- ▶ Payback period
- ▶ **Internal rate of return**
- ▶ Net present value
- ▶ Profitability index

Which of the following has "Beta" as a measure of risk?

- ▶ Firm specific risk
- ▶ Diversifiable risk
- ▶ Unique risk
- ▶ **Market risk**

Which of the following risk can be diversified away?

- ▶ **Un systematic risk** pg94
- ▶ Beta risk
- ▶ Firm specific risk

- ▶ Market risk

_____ is equal to (common shareholders' equity/common shares outstanding).

- ▶ Book value per share

- ▶ Liquidation value per share
- ▶ Market value per share
- ▶ None of the above

Which of the following is the variability of return on stocks or portfolios not explained by general market movements. It is avoidable through diversification?

- ▶ Systematic risk
- ▶ Standard deviation
- ▶ Unsystematic risk
- ▶ Financial risk

The Higher the Risk of a Share, the _____ its Rate of Return and the _____ its Market Price.

- ▶ Higher; Lower
- ▶ Lower; Higher
- ▶ Higher; Higher
- ▶ Lower; Lower

Which of the following is NOT a major cause of systematic risk.

- ▶ A worldwide recession
- ▶ A world war
- ▶ World energy supply
- ▶ Company management change

Capital budgeting is a decentralized function assigned to:

- ▶ Individuals
- ▶ Departments
- ▶ Teams
- ▶ All of the give

Market risk is measured in terms of the _____ of the market portfolio or index.

- ▶ Variance
- ▶ Covariance
- ▶ Standard deviation
- ▶ Correlation coefficient

Why market values are often used in computing the weighted average cost of capital?

- ▶ This is the simplest way to do the calculation
- This is consistent with the goal of maximizing shareholder value
This is required in the U.S. by the Securities and Exchange Commission

- ▶ None of the given options

Calculate the break-even (quantity) point given the following information. The firm has Rs.1, 000,000 in fixed costs. The firm produces only one product and anticipates selling each unit for Rs.25 with variable costs of Rs.5 per unit.

- ▶ 200,000
- ▶ 50,000
- ▶ 40,000
- ▶ There is not sufficient information provided to calculate the sales break-even point.

Which of the following costs would be considered a fixed cost?

- ▶ Raw materials
- ▶ Depreciation
- ▶ Bad-debt losses
- ▶ Production labor

In the context of operating leverage break-even analysis, if selling price per unit falls and all other variables remain constant, what will be the effect on the operating break-even point in units?

- ▶ Fall

- ▶ Rise

- ▶ Stay the same
- ▶ Incomplete information

Which of the following represents financial leverage?

- ▶ Use of more debt capital to increase profit
- ▶ Debt is not used in capital to increase profit
- ▶ High degree of solvency
- ▶ Low degree of solvency

Which of the following is NOT a reason for international investment?

To provide an expected risk-adjusted return in excess of that required

- ▶ To gain access to important raw materials
- ▶ To produce products and/or services more efficiently than possible domestically
- ▶ International investments have less political risk than domestic investments

Assuming that the firm can either hold cash paying no interest or invest in marketable securities, which of the following might induce the manager to hold higher cash balances?

- ▶ The cost of borrowing is high relative to interest rates on marketable securities

- ▶ Future cash flows are relatively predictable
- ▶ The cost of cash balances is relatively high
- ▶ Bank interest rates are expected to increase

The stock in your portfolio was selling for Rs. 40 per share yesterday, but has today declared a three for two stock split. Which of the following statements seems to be true?

- ▶ There will be two-thirds as many shares outstanding, and they will sell for Rs.60.00 each

- ▶ There will be four times as many shares outstanding, and they will sell for Rs.160.00 each

- ▶ There will be 50 percent more shares outstanding and they will sell for Rs.26.67 each

- ▶ There will be one-and-one-half times as many shares outstanding, and they will sell for Rs.60.00 each

After the payment of a 25% stock dividend, an investor has 500 shares of stock and Rs. 400 total value. What did the investor have prior to the stock dividend?

- ▶ 375 shares of stock and Rs. 375 total value
- ▶ 400 shares of stock and Rs. 400 total value
- ▶ 400 shares of stock and Rs. 500 total value
- ▶ 625 shares of stock and Rs. 400 total value

Which term would most likely be associated with the phrase "actions speak louder than words?"

- ▶ Incentive signaling
- ▶ Shareholder wealth maximization
- ▶ Financial signaling
- ▶ Optimal capital structure

The KSE (Karachi Stock Exchange) 100 Index represents what?

- ▶ The value of Portfolio of Highest volume stocks
- ▶ The value of Portfolio of all Stocks
- ▶ The value of Portfolio of lowest volume stocks
- ▶ None of the given options

While calculating the stock Beta graphically, y-intercept refers to:

- ▶ Market risk
- ▶ Systematic risk
- ▶ Company's specific risk
- ▶ Non-diversifiable risk

Which of the following helps you to reduce your portfolio's risk?

- ▶ Own more than 20 securities

- ▶ Own a basket of securities that don't behave alike
- ▶ Own a bunch of stocks from the same industry
- ▶ Own less risky securities only

If a stock is part of totally diversified portfolio then which of the following is TRUE for that stock?

- ▶ Stock's total Risk = Company Risk
- ▶ Stock's total Risk = Market Risk
- ▶ **Stock's total Risk = Market Risk + Company Risk**
- ▶ All of the given options

If the Market Risk of a stock is 25% and Stock's Beta is 2.0, then what is the Relevant Market Risk Component of that stock?

- ▶ 30%
- ▶ 40%
- ▶ **50%**
- ▶ 60%

If the Market Risk of a stock is 15% and Stock's Beta is 2.5 then what is the Relevant Market Risk Component of that stock?

- ▶ 30%
- ▶ 34%
- ▶ **38%**
- ▶ 42%

Which of the following is the main feature to adopt the Arbitrage Pricing Model?

- ▶ Risk need not to be considered

It has covered all the shortfalls of the Capital Asset Pricing Model

- ▶ The model requires a specific benchmark market portfolio
- ▶ **The model provides specific guidance concerning the determination of the risk premiums on the factor portfolios**

What should be used to calculate the proportional amount of equity financing employed by a firm?

The book value of the firm

The sum of common stock and preferred stock on the balance sheet

- ▶ **The current market price per share of common stock times the number of shares outstanding** DOUBTED

- ▶ The common stock equity account on the firm's balance sheet

Tax Preference Theory suggests that shareholder wealth is maximized by low dividend payout because of which of the following reasons?

- ▶ Marginal tax rate on dividends is lower than on capital gains
- ▶ **Marginal tax rate on dividends is higher than on capital gains**
- ▶ Marginal tax rate on dividends is equal to capital gains
- ▶ None of the given options

Bird-in-the-hand dividend theory was proposed by which of the following?

- ▶ Miller Modigliani
- ▶ **Myron Gordon and John Lintner**
- ▶ Henry Fayol
- ▶ William John and Lehman

The date on which the names of stockholders in the Stock Transfer Register of firm are documented is referred as:

- ▶ Declaration Date
- ▶ **Holder-of-record Date**
- ▶ Ex-Dividend Date
- ▶ Payment Date

XYZ Corporation has offered its shareholders the option that their dividends will be used to purchase additional shares of this corporation. This offer of XYZ Corporation is referred as:

- ▶ Stock repurchases
- ▶ **Dividend reinvestment**
- ▶ Stock dividends

- ▶ Stock splits

Calculate the return on equity (ROE) of ABC Company using Du Pont equation and the data given below:

Profit Margin= 30%

Asset Turnover= 50%

Leverage Factor = 60%

- ▶ 3.6%

- ▶ **9%**

- ▶ 14%

- ▶ 33%

= Profit Margin x Asset Turnover x Leverage Factor (or Equity Multiplier)

= (Net Income/Sales) x (Sales/Assets) x (Total Assets/Equity)

= Net Income / Equity

Business risk stems from operations and the _____ of the firm.

- ▶ Liability

- ▶ **Asset**

- ▶ Capital

- ▶ Revenue

Which of the following statements is TRUE about an aggressive approach to finance working capital?

- ▶ **Financing seasonal requirements of current assets with short-term debt and permanent requirement of current assets with long term debt**

- ▶ Financing permanent requirements of current assets with short-term debt and seasonal requirement of current assets with long term debt

- ▶ Financing seasonal as well as permanent requirements of current assets with short-term debt

- ▶ Financing seasonal as well as permanent requirements of current assets with long term debt

Every firm strives to achieve which of the following?

To keep Return on Equity (ROE) lower than Expected return (rE)

To keep Return on Equity (ROE) equal to Expected return (rE)

To keep Return on Equity (ROE) higher than Expected return (rE)

All of the given option

Capital structure theory is presented by which of the following?

- ▶ **Modigliani & Miller**

- ▶ Brigham & Houston

- ▶ Van Horne & Gittman

- ▶ Robert Alan Hill

Which of the following is (are) the characteristics of operating lease?

- ▶ Lessor maintains and finances the Asset

- ▶ It is not fully amortized

- ▶ It is cancelable

- ▶ **All of the given options**

When market value of another similar firm is less than the cost of replacing the assets of your own firm, it is better to buy another firm.

It is known as:

- ▶ **Cherry picking**

- ▶ Divestiture

- ▶ Spin-off

- ▶ Asset stripping

Most of the firms wish to maintain their capital structure in the form of which of the following?

- ▶ 100% equity

- ▶ **100% debt**

- ▶ Mix of debt and equity

- ▶ 100% from the personal

Calculate the Forward Rate for Rupee using Interest Rate Parity if the interest on 1 Year Maturity in Pakistan is 10% and on Euro is 6% and the forward rate is Rs.124/ EUR.

- ▶ Rs. 6 per EUR
- ▶ Rs. 120 per EUR
- ▶ Rs. 124 per EUR
- ▶ Rs. 1240 per EUR

If Return on Equity (ROE) is higher than the Expected Return (ROE $> r_E$), then which of the following is better for the firm to pursue?

- ▶ To plough the retained earnings back into the business
- ▶ To pay out the dividend this will raise the share price
- ▶ To finance short-term needs with long-term debt
- ▶ To finance seasonal needs with long-term funds

Which of the following is a bond that could be defined as “a bond bearing a yield that may rise or fall according to the fluctuations in the market”?

- ▶ High yield bond
- ▶ Floating rate bond
- ▶ Low coupon bond
- ▶ Euro bond

Which of the following can be used as measure of return?

- ▶ Forecasted selling price
- ▶ Forecasted purchase price
- ▶ Forecasted dividend
- ▶ Forecasted time span of project

When $\rho_{AB} = 0$ it means that:

- ▶ Investments are not correlated
- ▶ Investments are perfectly positively correlated
- ▶ Investments are perfectly negatively correlated
- ▶ None of the given options