Practice Questions Week 7 Day 2

Multiple Choice
Identify the choice that best completes the statement or answers the question.

1. Any long-lasting tool that people use to produce goods and services is called
   a. a product
   b. machinery
   c. capital
   d. equipment
   e. labor assistance

2. The additional revenue a firm obtains from employing one more unit of capital is called the
   a. marginal revenue product of capital
   b. total product of capital
   c. marginal product of capital
   d. production function
   e. marginal product of labor

3. The amount of money that someone would pay today for the right to receive a future payment is called
   a. the present value of the future payment
   b. the determinate value of the future payment
   c. the interest rate
   d. the principal
   e. the time discount

4. Which of the following changes would increase the present value of a future payment?
   a. a decrease in the size of the payment
   b. a decrease in the certainty of the payment actually being received
   c. an increase in the amount of time that elapses before receiving the payment
   d. a decrease in the interest rate
   e. none of the above

5. You have a bond that you can redeem for $10,000 one year from now. The interest rate is 10 percent (0.10) per year. How much is the bond worth today?
   a. $9,090.91
   b. $10,000.00
   c. $8,264.46
   d. $9,523.81
   e. $9,000.00

6. If the interest rate is 5 percent (0.05) per year, what is the present value of $3,000 to be received two years from now?
   a. $2,850.00
   b. $3,000.00
   c. $2,707.50
   d. $2,721.09
   e. $2,857.14
7. A snowplow will generate a net income of $2,000 per year for its owner. After 8 years, the plow will break down and have zero value. The maximum amount of money anyone would pay for the plow is
   a. less than $2,000
   b. $2,000
   c. between $2,000 and $16,000
   d. $16,000
   e. more than $16,000

8. A formalwear shop will earn a net income of $1,500 per year on a tuxedo. A tuxedo is good for two years, after which it will be worn out and worthless. If the interest rate is 10 percent (0.10) per year, what is the present value of a new tuxedo to the shop? (Assume that each year's income is received at the end of the year.)
   a. $148.76
   b. $2,955.30
   c. $2,955.59
   d. $2,603.31
   e. $3,000.00

9. A new computer will generate $1,000 in net revenue for a firm during its first year, $500 during its second year, $250 during its third year, and nothing thereafter. If the interest rate is 10 percent (0.10) per year, what is the present value of the computer to the firm? (The first payment will be received at the end of this year.)
   a. $1,590.91
   b. $1,510.14
   c. $1,750.00
   d. $1,446.28
   e. $1,661.16

10. You have a choice among three options. Option 1: receive $900 immediately. Option 2: receive $1,200 one year from now. Option 3: Receive $2,000 five years from now. The interest rate is 15 percent (0.15) per year. Rank these three options from highest present value to lowest present value.
    a. Option 1, Option 2, Option 3
    b. Option 3, Option 2, Option 1
    c. Option 2, Option 3, Option 1
    d. Option 3, Option 1, Option 2
    e. Option 1, Option 3, Option 2

11. The table below shows the total number of loaves of bread a bakery can bake per year with different numbers of ovens. The market for bread is perfectly competitive, with a market price of $2 per loaf. What is the marginal revenue product of the third oven?

<table>
<thead>
<tr>
<th>Number of Ovens</th>
<th>Total Number of Loaves</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1,000</td>
</tr>
<tr>
<td>2</td>
<td>1,800</td>
</tr>
<tr>
<td>3</td>
<td>2,400</td>
</tr>
<tr>
<td>4</td>
<td>2,800</td>
</tr>
</tbody>
</table>

   a. $1,200
   b. 2,400 loaves of bread
   c. $4,800
   d. 600 loaves of bread
   e. $1,600
12. According to the principle of asset valuation, the value of any asset is equal to
   a. the sum of all the future benefits it generates
   b. the revenue it generates during its first year
   c. the sum of the present values of all the future net benefits it generates
   d. the ratio of its final year's benefits to its price
   e. the sum of all future benefits it generates minus its price

13. A decrease in the interest rate is represented by
   a. a leftward shift of a firm's investment curve
   b. a rightward shift of a firm's investment curve
   c. a movement along a firm's investment curve, upward and to the left
   d. a movement along a firm's investment curve, downward and to the right
   e. a movement along a firm's investment curve, upward and to the right

14. A higher interest rate will lead a firm to purchase less capital because the higher interest rate
   a. lowers the marginal product of capital goods
   b. causes technological change to cease
   c. lowers the present value of capital goods
   d. causes economies of scale to be exhausted
   e. causes the capital market become monopolized

15. The table below shows the present value of beds for a city hospital, at different interest rates. The price of each bed is $800. If the interest rate decreases from 15 percent (0.15) to 5 percent (0.05) per year, how will the hospital's capital expenditure change?

<table>
<thead>
<tr>
<th>Bed</th>
<th>Total PV of Net Income at 5% interest Rate</th>
<th>Total PV of Net Income at 15% Interest Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st</td>
<td>$1,818.38</td>
<td>$1,541.99</td>
</tr>
<tr>
<td>2nd</td>
<td>$1,363.78</td>
<td>$1,250.96</td>
</tr>
<tr>
<td>3rd</td>
<td>$ 909.19</td>
<td>$ 771.00</td>
</tr>
<tr>
<td>4th</td>
<td>$ 454.59</td>
<td>$ 385.49</td>
</tr>
<tr>
<td>5th</td>
<td>$ 227.29</td>
<td>$ 192.75</td>
</tr>
</tbody>
</table>

   a. decrease by $138.19
   b. increase by $276.39
   c. increase by $800
   d. increase by $631.04
   e. decrease by $1,600
Practice Questions Week 7 Day 2
Answer Section

MULTIPLE CHOICE

1. C
2. A
3. A
4. D
5. A
6. D
7. C
8. D
9. E
10. C
11. A
12. C
13. D
14. C
15. C
Practice Questions Week 7 Day 3

Multiple Choice
Identify the choice that best completes the statement or answers the question.

1. A financial asset is
   a. a unit of physical capital with a positive market value
   b. any asset that generates a stream of income
   c. a share in the ownership of a productive enterprise
   d. a form of money
   e. a promise to pay future income in some form

2. A bond with a face value of $10,000 (and no coupon payments) is always worth
   a. $10,000
   b. less than $10,000 before the maturity date
   c. more than $10,000 if the interest rate is high enough
   d. $10,000 on the date of purchase
   e. $9,090.91 two years before the maturity date

3. What is the value of a newly issued 10-year bond with face value of $10,000 and no coupon payments? Assume the interest rate is 7 percent (0.07) per year.
   a. $0
   b. $5,083.49
   c. $10,000
   d. $95,632.41
   e. $100,000.00

4. You are thinking of purchasing a 5-year bond, with a face value of $8,000, on the secondary bond market. The bond was issued three years ago, so it will mature two years from today. If the interest rate is 10 percent (0.10) per year, what is the value of the bond?
   a. $6,611.57
   b. $8,000.00
   c. $4,967.37
   d. $6,010.52
   e. $7,272.73

5. Your aunt gives you a PepsiCo bond with face value of $5,000. It will mature in two years. Currently, the interest rate is 10 percent (0.10) per year. How will the value of the bond change if the interest rate falls to 5 percent tomorrow morning?
   a. It will rise by $413.22.
   b. It will rise by $402.90.
   c. It will rise by $432.90.
   d. It will fall by $432.90.
   e. It will fall by $402.92.

6. You have two bonds, both with a face value of $7,000. One of them matures one year from today, while the other matures one year after that. If the interest rate is 8 percent (0.08) per year, what is the difference in value between the two bonds?
   a. $480.11
   b. $578.52
   c. $317.46
   d. zero
   e. $925.92
7. Microsoft issues a 2-year bond with a face value of $5,000. In addition to the principal paid at maturity, the bond has 2 annual coupon payments of $500 each, to be received at the end of the first and second year respectively. If the interest rate is 10 percent (0.10) per year, what is the value of the newly issued bond?
   a. $5,000.00
   b. $6,000.00
   c. $5,886.68
   d. $4,901.48
   e. $41.32

8. A newly issued bond with a face value of $12,000 and no coupon payments is priced at $9,000. The bond will mature in one year. What is the yield on this bond?
   a. 33.3 percent
   b. 25 percent
   c. $3,000
   d. $1,909.09
   e. It depends on the interest rate

9. Which of the following states the relationship between a bond's price and its yield?
   a. As the price falls, the yield falls.
   b. Price and yield are usually independent of each other.
   c. As the price rises, the yield rises.
   d. As the price rises, the yield falls.
   e. As the yield rises, so does the price.

10. The key difference between the primary and secondary bond markets is that __________ bonds are traded on the primary market, while __________ bonds are traded on the secondary market.
    a. newly issued; previously issued
    b. government; corporate
    c. more valuable; less valuable
    d. low risk; high risk
    e. high yield; low yield

11. The interest rate on U.S. government securities is often called the
    a. prime rate
    b. public discount
    c. riskless rate
    d. superior rate
    e. universal discount

12. Which of the following will lower the present value of a bond?
    a. a fall in the interest rate
    b. an increase in the principal
    c. a shorter time to maturity
    d. an increased risk of default
    e. none of the above

13. Which of the following is a correct statement about bond prices, other things equal?
    a. a lower face value leads to a higher bond price
    b. a higher risk of default leads to a higher bond price
    c. a higher risk of default leads to a lower yield
    d. fewer coupon payments lead to a higher bond price
    e. a higher price leads to a lower yield
14. When the market estimate of a company’s riskiness decreases the market adjusts by
   a. having the supply of that bond increase.
   b. having the supply of that bond decrease.
   c. having the demand for that bond increase.
   d. having the demand for that bond decrease.

15. When the demand for alternative investments increases, the market for a particular bond adjusts by
   a. having the supply of that bond increase.
   b. having the supply of that bond decrease.
   c. having the demand for that bond increase.
   d. having the demand for that bond decrease.
Practice Questions Week 7 Day 3
Answer Section

MULTIPLE CHOICE

1. E
2. B
3. B
4. A
5. B
6. A
7. A
8. A
9. D
10. A
11. C
12. D
13. E
14. C
15. D
Multiple Choice
Identify the choice that best completes the statement or answers the question.

1. The key difference between a share of stock and a bond is that
   a. a share of stock is a riskless asset
   b. the holder of a bond receives only one future payment
   c. the holder of a share stock has a share in the ownership of a firm
   d. bonds are issued only by the government, while stock is issued only by corporations
   e. there are secondary markets for stocks, but not for bonds

2. On a secondary stock market, such as the New York Stock Exchange,
   a. firms sell new issues of stock
   b. firms make initial public offerings
   c. previously issued bonds are sold and resold
   d. previously issued shares of corporations are sold and resold
   e. firms sell newly issued bonds

3. A corporation that specializes in owning shares of stock in other corporations is called a
   a. secondary market
   b. mutual fund
   c. stock broker
   d. second hander
   e. day trader

4. The payments made to shareholders from a firm's profits are called
   a. owner subsidies
   b. principal
   c. coupon payments
   d. retained earnings
   e. dividends

5. The total value of dividends paid out to shareholders by a firm is equal to
   a. its total after-tax profits
   b. its total after-tax profits minus its retained earnings
   c. its total after-tax profits minus its bond payments
   d. its total after-tax profits plus its retained earnings
   e. the present value of the firm

6. Which of the following would increase the value of a firm's stock?
   a. a decrease in the firm's present profit
   b. a decrease in the anticipated growth rate of future profits
   c. an increase in the perceived riskiness of future profits
   d. a fall in the interest rate
   e. an anticipated increase in the interest rate

7. The price/earnings (PE) ratio of a stock is found by
   a. dividing the most recent year's dividend by the current stock price
   b. dividing the current stock price by the after-tax profit per share
   c. dividing the most recent year's dividend by retained earnings
   d. dividing the current stock price by the Dow Jones Industrial Average
   e. dividing the current stock price by the present value of the firm
8. Which of the following would be most likely to cause a rightward shift of the demand for shares of Planet X, Inc.'s stock?
   a. the appearance of a strong competitor in Planet X's market
   b. a ban on Planet X's product in a large export market
   c. the announcement of a profitable new product line from Planet X
   d. news of a labor strike against Planet X
   e. the announcement of a new public offering of Planet X stock

9. If you carefully research the products, technologies, patents, and management of firms, the efficient markets theory of stock prices, predicts that
   a. you will probably reap significant gains
   b. you will actually decrease your odds of doing better than the average investor
   c. you will probably do about as well as someone who did no research
   d. you will lose money unless you failed to consider historical stock price patterns
   e. both b and d

10. The efficient markets theory of stock prices, says that new information
    a. is quickly and completely incorporated into stock prices
    b. is incorporated into stock prices only when discovered by fundamental analysis
    c. causes stock prices to increase
    d. has little impact on stock prices
    e. is incorporated into stock prices with a time lag of a few days
Practice Questions Week 7 Day 4
Answer Section

MULTIPLE CHOICE

1. C
2. D
3. B
4. E
5. B
6. D
7. B
8. C
9. C
10. A