Foundations of Investments 1st edition Adair Test Bank

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Name:______________________ Class:_________________ Date:_________

Chapter 2. Types and Attributes of Financial Instruments

1. All of the following are categories of financial instruments EXCEPT
   a. equity securities.
   b. debt securities.
   c. syndicates.
   d. money market securities.

ANSWER: c

2. Which of the following is an organization that regulates publicly traded securities?
   a. IPO
   b. SPAC
   c. SEC
   d. IRS

ANSWER: c

3. The investigation of a contract that a reasonable business makes before entering into an agreement is called
   a. a futures contract.
   b. due diligence.
   c. a preliminary prospectus.
   d. a private placement.

ANSWER: b

4. To determine who rightfully owns a security to ensure investors receive payments from the firm, what is necessary?
   a. Blockchain accounting practices
   b. An initial public offering
   c. Careful tracking of ownership
   d. Preliminary prospectus

ANSWER: c

5. In order to ensure that investors are allowed to exercise their right to control the firm's activities, what is necessary?
   a. Blockchain accounting practices
   b. An initial public offering
   c. Preliminary prospectus
   d. Careful tracking of ownership

ANSWER: d

6. For private equity and debt placements, where the buyer is not expected to resell the instrument, there is
   a. less commodity risk.
   b. greater commodity risk.
   c. no need for careful tracking by the SEC.
   d. a greater need for careful tracking by the SEC.

ANSWER: c

7. The Latin phrase *caveat emptor* that governs private transactions means
   a. "buyer has little risk."

b. "caves are empty."

c. "let the seller beware."

d. "let the buyer beware."

ANSWER: d

8. A direct sale of a security can be facilitated by the offering corporation or

a. the IRS.

b. the U.S. government.

c. an investment bank.

d. the SEC.

ANSWER: c

9. The role of underwriting during the initial sale of stocks or bonds is generally fulfilled by

a. an investment bank.

b. the U.S. government.

c. the SEC.

d. the IRS.

ANSWER: a

10. Sale or purchase of securities by the firm that issued them takes place in

a. the primary market.

b. the secondary market.

c. an ETF.

d. the registration phase.

ANSWER: a

11. A firm that specializes in investing in securities of small, emerging companies is known as a(n)

a. IPO.

b. venture capital firm.

c. SPAC.

d. market participant.

ANSWER: b

12. Venture capital firms generally invest in small firms with emerging technologies. They take on risks that public investors may not take to

a. generate risk-free income.

b. experience exceptional growth.

c. hedge tax protections.

d. avoid due diligence.

ANSWER: b

13. The first sale of common stock to the general public is known as a(n)

a. syndicate.

b. IPO.

c. SPAC.
d. firm commitment.

ANSWER: b

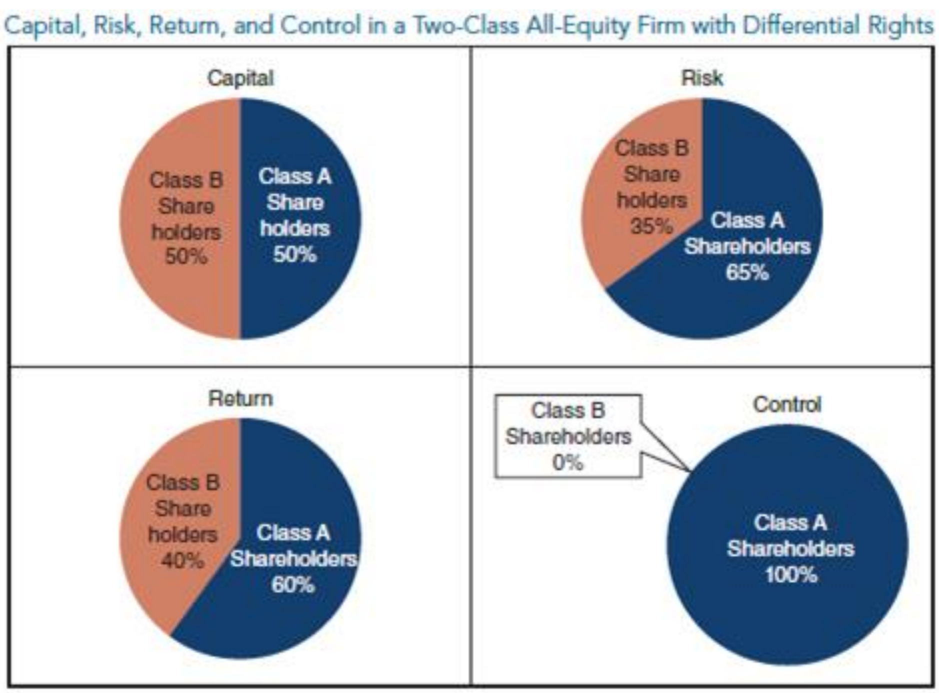
14. All of the following are examples of what an investment bank may advise on EXCEPT
    a. mergers.
    b. privatization.
    c. restructuring.
    d. tax law.

ANSWER: d

15. A selling group assembled to market an issue of securities is called a
    a. syndicate.
    b. venture capital firm.
    c. money market fund.
    d. participating bond.

ANSWER: a

16. The following diagram shows that when there are two different classes of stock shares, one class of shares

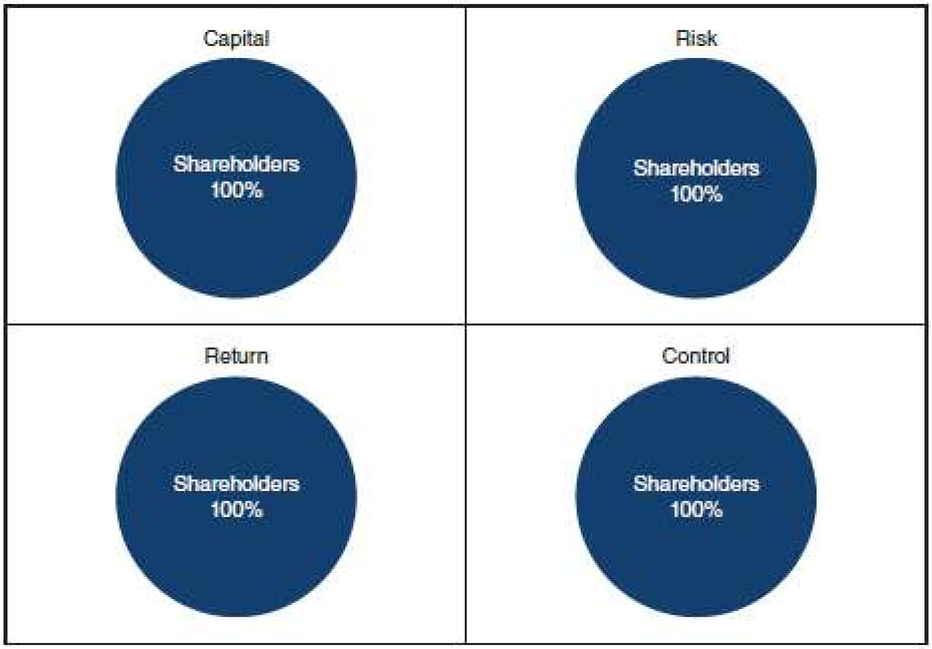


    a. gets less control in exchange for less risk or more return.
    b. gets more control in exchange for less risk or more return.
    c. maintains all the decision-making power.
    d. takes all the risk.

ANSWER: a

17. The following diagram is indicative of what type of stakeholder relationship?

Capital, Risk, Return, and Control in a Firm



a. All equity
b. All debt
c. Some equity and debt
d. Government owned

ANSWER: a

18. The term *residual claimant* refers to
a. leftover payments after promised payments.
b. primary payments.
c. primary debt.
d. leftover debt resolutions.

ANSWER: a

19. The following diagram is indicative of what type of stakeholder relationship?

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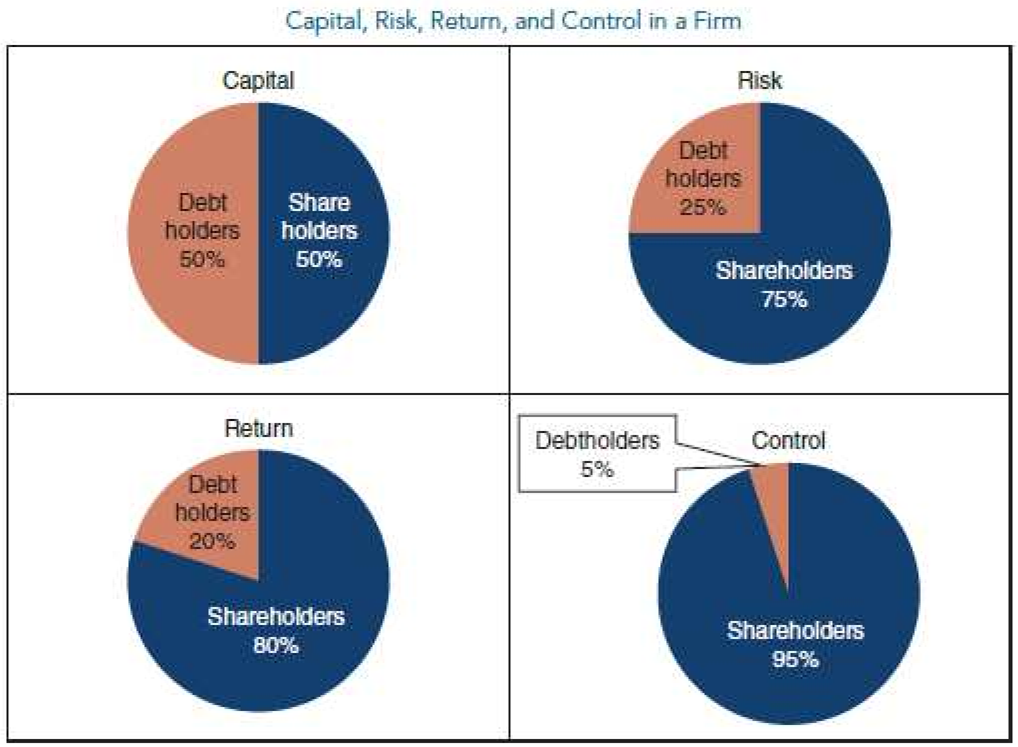
Chapter 2. Types and Attributes of Financial Instruments



a. All equity
b. All debt
c. Some equity and debt
d. Government owned

ANSWER: c

20. A market where securities trade after issuance by the firm is called a
a. primary market.
b. secondary market.
c. money market.
d. syndicate.

ANSWER: b

21. When a syndicate of investment bank brokers an IPO, the firm that manages the sale is known as the
a. underwriter.
b. lead underwriter.
c. derivative instrument.
d. participating organization.

ANSWER: b

22. An agreement with an investment banker who does not guarantee the sale of the security is called a
a. venture capitalist agreement.
b. repurchase agreement.
c. firm commitment.

d. best-efforts agreement.

ANSWER: d

23. An investment banker guaranteeing the sale of securities by agreeing to purchase the entire issue at a specified price is a

a. venture capitalist agreement.
b. repurchase agreement.
c. firm commitment.
d. best-efforts agreement.

ANSWER: c

24. The initial document detailing the financial condition of a firm that is filed with the SEC to register a new issue of securities is called a

a. registration.
b. preliminary prospectus.
c. repurchase agreement.
d. futures contract.

ANSWER: b

25. The process of filing information with the SEC concerning a proposed sale of securities to the public is called a

a. registration.
b. preliminary prospectus.
c. repurchase agreement.
d. futures contract.

ANSWER: a

26. A series of sales presentations to potential investors by an underwriting firm is called a(n)

a. road show.
b. preliminary prospectus.
c. IPO.
d. futures contract.

ANSWER: a

27. Lockup agreements prevent

a. the sale of stock by insiders following an IPO.
b. tax benefits due to public sale of assets.
c. tax benefits due to public trading of common stock.
d. government intervention in an IPO.

ANSWER: a

28. When existing outstanding shares are sold to the public for the first time in a secondary market with no underwriter involvement, this is called

a. an indirect transfer.
b. a direct listing.

c. commercial paper.

d. SPAC.

ANSWER: b

29. An investment vehicle that raises capital in its IPO and then looks for a private company to purchase is called a

a. SPAC.

b. venture capital firm.

c. derivative instrument.

d. repurchase agreement.

ANSWER: a

30. Which type of investment receives dividends first?

a. Common stock

b. Debt securities

c. Preferred stock

d. Money market bonds

ANSWER: c

31. What type of equity security receives dividend payments and has debt features?

a. Preferred stock

b. Common stock

c. Corporate bonds

d. Government bonds

ANSWER: a

32. The maximum amount that an equity investor can lose should a public corporation default on its obligations is the

a. amount of the investment.

b. assets held by the investor.

c. amount of the investment plus taxes.

d. amount of the debt held.

ANSWER: a

33. The maximum amount that an investor can lose who pledged personal assets to secure a loan should the corporation default on its obligations is the

a. amount of the investment the personal assets pledged.

b. assets held by the investor.

c. amount of the investment plus taxes.

d. amount of the debt held.

ANSWER: a

34. The legal status where an investor's liability is limited to their investment in a firm is called

a. due diligence.

b. repurchase agreement.

c. liability minimization.

d. limited liability.

ANSWER: d

35. Shareholders of an organization have the right to
    a. vote the shares and participate in hiring the firm's management.
    b. vote the shares and elect a board of directors.
    c. participate in hiring the firm's management and elect a board of directors.
    d. participate in hiring the firm's management and comply with government regulations.

ANSWER: b

36. Which of the following is entitled to a firm's earnings?
    a. Investment banks
    b. Creditors
    c. Stockholders
    d. Debtholders

ANSWER: c

37. Which of the following gets paid last if a firm goes bankrupt?
    a. Bondholders
    b. Stockholders
    c. Creditors
    d. Debtholders

ANSWER: b

38. Fixed-income bonds are least likely to be issued by
    a. large corporations.
    b. federal governments.
    c. municipal governments.
    d. smaller corporations.

ANSWER: d

39. Risk assumed by the lender in which the borrower might fail to pay interest or principal repayments is called
    a. inherent risk.
    b. interest rate risk.
    c. purchasing power risk.
    d. default risk.

ANSWER: d

40. The potential return on a bond is known as
    a. maturity.
    b. coupon.
    c. yield.
    d. interest.

ANSWER: c

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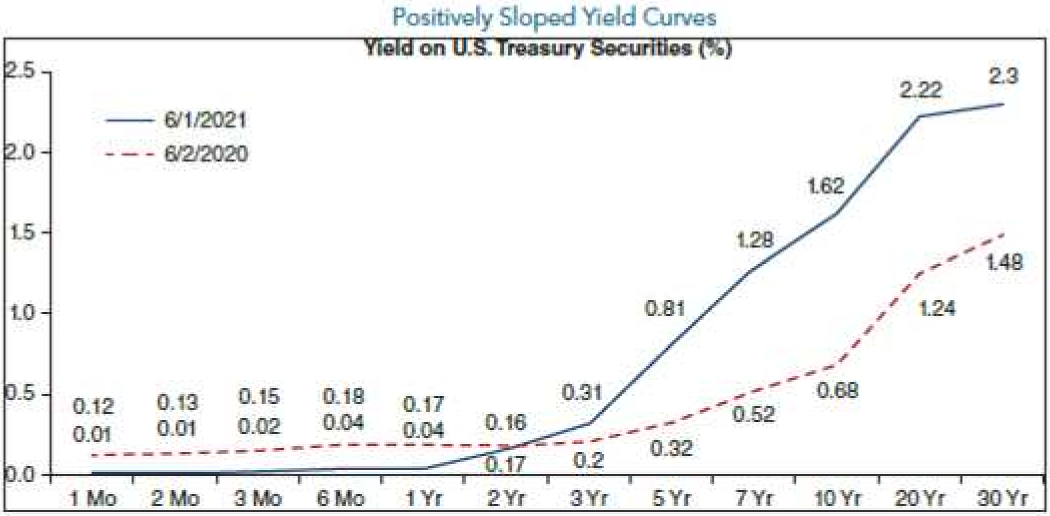
41. The estimated annual rate of return for a bond, assuming the investor holds the asset to its maturity date, is known as
    a. coupon yield.
    b. interest yield.
    c. yield to maturity.
    d. yield.

ANSWER: c

42. The following graph implies that as the term to maturity of a bond increases, the investors



    a. require additional compensation.
    b. require less compensation.
    c. can tolerate less risk.
    d. can tolerate more risk.

ANSWER: a

43. The stated legal document for a debt agreement is known as the
    a. indenture.
    b. debenture.
    c. yield spread.
    d. registration.

ANSWER: a

44. According to the following graph, the large yield spread of Treasury Bills and Treasury Bonds appears over time to

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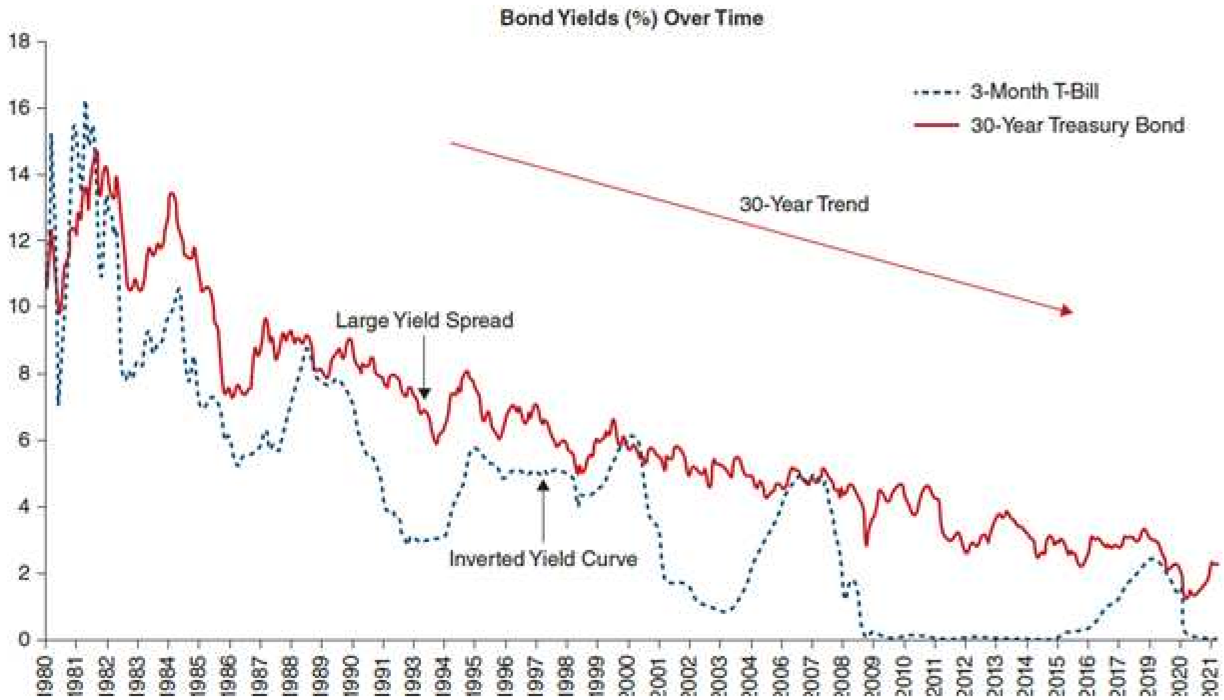

a. increase.

b. remain relatively stable.

c. decrease.

d. decrease in risk.

ANSWER: c

45. All of the following are debt agreement terms that debtors must meet included in the indenture EXCEPT

a. coupon rate.

b. yield.

c. date of maturity.

d. date of issuance.

ANSWER: b

46. Property that a borrower must offer to secure a loan is known as

a. the yield.

b. an asset.

c. a T-bill.

d. collateral.

ANSWER: d

47. An agent appointed to act in the interest of the bondholders is known as

a. a fiduciary.

b. an investment bank.

c. a trustee.

d. the SEC.

ANSWER: c

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48. Out of the bonds in the following table, which is the least risky?

Ratings for Selected Bonds Maturing in 2025

Issuer	Coupon Rate of Interest	S&P Rating	Moody's Rating
Apple	2.500%	AA+	A2
Bank of America	4.000	BBB+	Baa3
FedEx	3.200	BBB	Baa1
General Motors Financing	4.000	BBB	Ba1
Merck	2.750	AA	A2
Waste Management	3.125	A	Baa2

a. Waste Management
b. Merck
c. Apple
d. Bank of America

ANSWER: c

49. A diversified bond portfolio can protect an investor against
a. interest rate risk.
b. reinvestment risk.
c. purchasing power risk.
d. default risk.

ANSWER: d

50. A factor of debt that partially compensates for the risk of price fluctuations is
a. that the debt ultimately matures.
b. risk tends to lessen over time.
c. the bond market evens out over the life of the loan.
d. bonds have less risk than stocks.

ANSWER: a

51. The likelihood that future cash flows won't be worth as much because of inflation is known as
a. purchasing power risk.
b. inflation rate risk.
c. interest rate risk.
d. default risk.

ANSWER: a

52. When an investor acquires bonds in a foreign currency, there is a type of risk known as
a. purchasing power risk.
b. interest rate risk.
c. default risk.
d. foreign exchange risk.

ANSWER: d

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53. The safest short-term security that typically has a maturity of less than one year is known as
    a. commercial paper.
    b. a CD.
    c. a T-bill.
    d. a repurchase agreement.

ANSWER: c

54. The sale of a security where a seller agrees to buy back the security at a specified price at a specified date is called
    a. commercial paper.
    b. a CD.
    c. a T-bill.
    d. a repurchase agreement.

ANSWER: d

55. Short-term debt issued by a corporation that matures in 270 days or less is known as
    a. commercial paper.
    b. a CD.
    c. a T-bill.
    d. a repurchase agreement.

ANSWER: a

56. In which type of instrument does an investor know precisely how much will be made on the investment?
    a. Commercial paper
    b. CD
    c. T-bill
    d. Repurchase agreement

ANSWER: d

57. What instrument is a short-term promissory note that a bank guarantees?
    a. Tax anticipation note
    b. CD
    c. Banker's acceptance
    d. Repurchase agreement

ANSWER: c

58. A debt issued by a state and to be repaid from future tax revenues is called a
    a. CD.
    b. T-bill.
    c. tax anticipation note.
    d. repurchase agreement.

ANSWER: c

59. Yield on money market funds compared to other mutual funds tends to be

a. much higher.
b. much lower.
c. much riskier.
d. more likely to follow the S&P 500.

ANSWER: b

60. Risk associated with money market funds compared to other mutual funds tends to be
a. much lower.
b. much higher.
c. more likely to improve with time.
d. more likely to follow the S&P 500.

ANSWER: a

61. A contract that derives its value from an underlying asset or factor is known as a
a. financial instrument.
b. registration.
c. derivative instrument.
d. commodity.

ANSWER: c

62. A form of insurance that investors take against risk is known as a
a. muni.
b. T-bill.
c. hedge.
d. commodity.

ANSWER: c

63. A basic good used in commerce that is interchangeable with other goods of a similar type is known as a
a. commodity.
b. T-bill.
c. hedge.
d. muni.

ANSWER: a

64. A formal agreement to buy or sell a commodity at a specified price is known as a(n)
a. option.
b. futures contract.
c. hedge.
d. muni.

ANSWER: b

65. A transaction where an individual does not purchase but rather enters into a contract to buy or sell is known as a(n)
a. option.
b. T-bill.

c. hedge.
d. futures contract.

ANSWER: d

66. The primary appeal of commodity contracts to speculators is the potential
a. to diversify a portfolio.
b. to hedge against upside risk.
c. to hedge against downside risk.
d. for a large return on the investment.

ANSWER: d

67. An investment defined as the non-binding right to buy or sell a stock at a specified price for a specified length of time is a(n)
a. hedge.
b. futures contract.
c. commodity.
d. option.

ANSWER: d

68. Leverage exists in futures contracts because the
a. contract may become null and void if conditions are not met.
b. contract controls a large amount of the underlying asset and costs little money.
c. value is inherent in the underlying asset.
d. value of the underlying asset changes predictably.

ANSWER: b

69. Which investing market is the largest in the world?
a. Stock market
b. Bond market
c. Foreign exchange market
d. Primary market

ANSWER: c

70. Speculating in foreign markets is thought to be
a. risk averse.
b. not very risky.
c. level in terms of risk.
d. very risky.

ANSWER: d