Chapter 1

**The Financial Environment**

**TRUE-FALSE QUESTIONS**

1. Finance is the study of how individuals, institutions, and businesses acquire, spend and manage money and other financial resources.

Answer: T

Difficulty Level: Easy

Subject Heading: Basic Definitions

L.O. 1.1

2. Business finance is the study of financial planning, asset management and fund raising by businesses and financial institutions.

Answer: T

Difficulty Level: Easy

Subject Heading: Basic Definitions

L.O. 1.1

3. Personal finance is the study of how growth-driven performance-focused, early-stage firms raise financial capital and manage operations and assets.

Answer: F

Difficulty Level: Easy

Subject Heading: Personal Finance

L.O. 1.1

4. Personal finance is the study of how individuals prepare for financial emergencies, protect against premature death and property losses, and accumulate wealth.

Answer: T

Difficulty Level: Easy

Subject Heading: Personal Finance

L.O. 1.1

5. The secondary securities markets are involved in creating and issuing new securities, mortgages, and other claims to wealth.

Answer: F

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

6. While the financial press chooses to highlight examples of unethical behavior, most individuals exhibit sound ethical behavior in their personal and business dealings and practices.

Answer: T

Difficulty Level: Easy

Subject Heading: Business Ethics

L.O. 1.3

7. The six principles of finance include (1) Money has a time value, (2) Higher returns are expected for taking on more risk, (3) Diversification of investments can reduce risk, (4) Financial markets are efficient in pricing securities, (5) Manager and stockholder objectives may differ, and (6) Reputation matters.

Answer: T

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

8. The principle of finance that "money has a time value" implies Money in hand today is worth less than the promise of receiving the same amount in the future because a sum of money today could be invested and grow over time.

Answer: F

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

9. The principle of finance that "lower returns are expected for taking on less risk" implies that rational investors would choose a risky investment only if they feel the expected return is high enough to justify the greater risk.

Answer: T

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

10. The principle of finance that "financial markets are efficient in pricing securities" implies that the prices of securities reflect some information available to the public and that when new information becomes available, prices change over time to reflect that information.

Answer: F

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

11. The principle of finance that "management objectives may differ from owner objectives" implies that owner returns may suffer as a result of manager objectives.

Answer: T

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

12. The principle of finance that "management objectives may differ from owner objectives" can be resolved by increasing manager salaries.

Answer: F

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

13. The principle of finance that "reputation matters" implies that for institutions or businesses to be successful, they must have the trust and confidence of their customers, employees, and owners, as well as the community and society within which they operate.

Answer: T

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

14. The principle of finance that "reputation matters" sometimes is harmed by the different objectives of owners and managers.

Answer: T

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

15. The U.S. Treasury Department is primarily responsible for the amount of money that is created in the U.S. economy.

Answer: F

Difficulty Level: Easy

Subject Heading: Financial System Components and Financial Functions

L.O. 1.4

16. Financial system functions include accumulating savings and lending funds.

Answer: T

Difficulty Level: Easy

Subject Heading: Financial System Components and Financial Functions

L.O. 1.4

17. Three financial system components are the U.S. Treasury, financial institutions, and financial markets.

Answer: F

Difficulty Level: Easy

Subject Heading: Financial System Components and Financial Functions

L.O. 1.4

18. Individuals and businesses hold money for purchases or payments they expect to make in the near future.

Answer: T

Difficulty Level: Easy

Subject Heading: Transferring Money

L.O. 1.4

19. One of the most significant functions of the financial system is the creation of money, which serves as a medium of exchange.

Answer: T

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

20. An effective financial system is a complex mix of government and policy makers, a monetary system, financial institutions, and financial markets that interact to expedite the flow of financial capital from savings into investment.

Answer: T

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

21. The lax oversight by government regulatory agencies and private debt rating agencies helped contribute to the severity of the 2007-2009 financial crisis.

Answer: T

Difficulty Level: Medium

Subject Heading: 2007-2009 Financial Crisis

L.O. 1.4

22. The Economic Stabilization Act of 2008 was passed in response to the financial crisis.

Answer: T

Difficulty Level: Medium

Subject Heading: 2007-2009 Financial Crisis

L.O. 1.4

23. The Troubled Asset Relief Program (TARP), which was passed as part of the Economic Stabilization Act of 1978 enabled the U.S. Treasury to purchase up to $700 billion of troubled assets held by financial institutions.

Answer: T

Difficulty Level: Medium

Subject Heading: 2007-2009 Financial Crisis

L.O. 1.4

24. Financial markets provide the mechanism for allocating financial resources or funds from savers to borrowers.

Answer: T

Difficulty Level: Easy

Subject Heading: Basic Definitions

L.O. 1.5

25. Money markets are the markets where generally short-term assets are traded.

Answer: T

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

26. Capital markets are markets where equity securities and debt securities with maturities of greater than one year are traded.

Answer: T

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

27. Money markets are markets where equity securities and debt securities with maturities of greater than one year are traded.

Answer: F

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

28. Securitization is the process of pooling and packaging mortgage loans into debt securities.

Answer: T

Difficulty Level: Easy

Subject Heading: Mortgages

L.O. 1.5

29. A credit rating indicates the expected likelihood that a borrower will miss interest or principal payments and possibly default on the debt obligation in the form of a loan, mortgage, or bond.

Answer: T

Difficulty Level: Easy

Subject Heading: Credit Ratings

L.O. 1.5

30. Credit ratings are prepared by government organizations on individuals, financial institutions, business firms, and government entities.

Answer: F

Difficulty Level: Easy

Subject Heading: Credit Ratings and Credit Scores

L.O. 1.5

31. A credit score is a number that indicates the creditworthiness or likelihood that a borrower will make loan payments when due

Answer: T

Difficulty Level: Easy

Subject Heading: Credit Ratings and Credit Scores

L.O. 1.5

32. Because the relative values of currencies may change, firms cannot use the currency exchange markets to reduce the risk of holding too much of certain currencies.

Answer: F

Difficulty Level: Easy

Subject Heading: Major Types of Financial Markets

L.O. 1.5

33. During the past couple of decades, generally high fixed-rate mortgage loan interest rates and the desire to extend housing ownership to more individuals in the U.S., the use of adjustable-rate mortgages grew in usage.

Answer: T

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

34. An adjustable-rate mortgage (ARM) has an interest rate that is usually adjusted annually to reflect changes in Treasury bill rates (or other benchmark); ARMs typically have variable interest rates for one to five years with a provision to switch to a fixed-rate over the remaining life of the ARM.

Answer: T

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

35. A mortgage-backed security is an investment created by using a house as collateral for a loan.

Answer: F

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

36. A prime mortgage is a home loan to a borrower with a credit score above 300.

Answer: F

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

37. A sub-prime mortgage is a home loan made to a borrower with a relatively low credit score indicating the likelihood that loan payments might be missed when due.

Answer: T

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

38. Money markets are where debt securities with maturities of one year or more are issued and traded.

Answer: F

Difficulty Level: Medium

Subject Heading: Money and Capital Markets

L.O. 1.5

38. Derivative securities may be used to speculate on the future price direction of the underlying financial assets or to reduce price risk associated with holding the underlying financial assets.

Answer: T

Difficulty Level: Medium

Subject Heading: Major Types of Financial Markets

L.O. 1.5

39. The primary goal of the financial manager in a profit-seeking organization is to maximize the owners’ wealth.

Answer: T

Difficulty Level: Easy

Subject Heading: Goal of Financial Manager

L.O. 1.6

**MULTIPLE-CHOICE QUESTIONS**

40. Finance has its origins in:

a. economics and statistics

b. accounting and sociology

c. accounting and economics

d. psychology and mathematics

Answer: c

Difficulty Level: Easy

Subject Heading: Basic Definitions

L.O. 1.1

41. Finance is:

a. the study of how individuals, institutions, governments, and businesses acquire, spend, and manage money and other financial assets

b. the study of how businesses acquire, spend, and manage money and other financial assets

c. the study of how governments, and businesses acquire, spend, and manage money and other financial assets

d. the study of how money is used to purchase goods and services

Answer: a

Difficulty Level: Medium

Subject Heading: Basic Definitions

L.O. 1.1

42. Finance has its origins in:

a. economics and statistics

b. accounting and mathematics

c. management and operations

d. economics and accounting

Answer: d

Difficulty Level: Medium

Subject Heading: Basic Definitions

L.O. 1.1

43. Economists use a \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ framework to explain how the prices and quantities of goods and services are determined in a free-market economic system.

a. opportunity

b. marginal cost

c. supply-and-demand

d. anti-monopoly

Answer: C

Difficulty Level: Medium

Subject Heading: Basic Definitions

L.O. 1.1

44. Successful businesses typically progress through a series of life-cycle stages—from the idea stage to exiting the business; these five stages include the:

a. development stage, startup stage, survival stage, rapid growth stage, and maturity stage.

b. idea stage, design stage, operating stage, rebuilding stage, and decline stage

c. development stage, operating stage, rebuilding stage, rapid growth stage, and maturity stage

d. idea stage, startup stage, rapid growth stage, survival stage, and decline stage

Answer: a

Difficulty Level: Medium

Subject Heading: Business Life Cycle

L.O. 1.1

45. Reasons we study finance include all of the following except:

a. To make informed economic decisions

b. To make informed personal and business investment decisions

c. To make informed career decisions based on a basic understanding of business finance

d. To make informed medical decisions

Answer: d

Difficulty Level: Easy

Subject Heading: Basic Concepts

L.O. 1.2

46. \_\_\_\_\_\_\_\_\_\_\_\_\_\_ behavior refers to how an individual or organization treats others legally, fairly, and honestly.

a. Principal-agent

b. Stakeholder

c. Responsible

d. Ethical

e. none of the above

Answer: d

Difficulty Level: Medium

Subject Heading: Business Ethics

L.O. 1.2

47. Programs passed by the federal government in response to the financial crisis of 2007-2009 include which of the following:

a. HIPPA

b. TARP

c. ERISA

d. ADA

Answer: b

Difficulty Level: Medium

Subject Heading: 2007-2009 Financial Crisis

L.O. 1.2

48. The value of money results from

a. its backing

b. rates set by the Federal Reserve

c. its purchasing power

d. its backing by gold

Answer: c

Difficulty Level: Easy

Subject Heading: Basic Concepts

L.O. 1.3

49. If the interest rate is greater than 0%, then a dollar today is worth

a. more than a dollar tomorrow

b. the same as a dollar tomorrow

c. less than a dollar tomorrow

d. there is not sufficient information to tell

Answer: a

Difficulty Level: Easy

Subject Heading: Basic Time Value Concepts

L.O. 1.3

50. If the interest rate is equal to 0%, then a dollar today is worth

a. more than a dollar tomorrow

b. the same as a dollar tomorrow

c. less than a dollar tomorrow

d. there is not sufficient information to tell

Answer: b

Difficulty Level: Easy

Subject Heading: Basic Time Value Concepts

L.O. 1.3

51. The six principles of finance include all of the following except:

a. Money has a time value.

b. Higher returns are expected for taking on more risk

c. Diversification of investments can reduce risk

d. Larger capital amounts are charged higher interest

Answer: d

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

52. Among the six principles of finance, all are included except:

a. All decisions are ultimately financial decisions.

b. Higher returns are expected for taking on more risk

c. Diversification of investments can reduce risk

d. Financial markets are efficient in pricing securities

Answer: a

Difficulty Level: Medium

Subject Heading: Six Principles of Finance

L.O. 1.3

53. $1,000 invested today at 6% interest would be worth \_\_\_\_\_\_\_\_ one year from now

a. $1,600

b. $1,060

c. $1,160

d. $1,006

Answer: b

[$1,000 x .06 = $60, and $1,000 + $60 = $1,060]

Difficulty Level: Medium

Subject Heading: Basic Time Value Concepts

L.O. 1.3

54. Two risky assets can be combined to lower the overall risk of a portfolio. This principle is commonly referred to as

a. blending

b. asset allocation

c. diversification

d. portfolio segmentation

Answer: c

Difficulty Level: Medium

Subject Heading: Risk and Return

L.O. 1.3

55. Rational investors would consider an investment in a risky business venture only if they feel the expected return is high enough to justify the

a. greater risk.

b. higher cost.

c. longer useful life.

d. more complex designs.

Answer: a

Difficulty Level: Medium

Subject Heading: Risk and Return

L.O. 1.3

56. The theory of \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ implies that information is quickly embedded in prices making it difficult for investors to "beat the market."

a. stock investing

b. efficient markets

c. portfolio management

d. asset allocation

Answer: b

Difficulty Level: Medium

Subject Heading: Efficient Markets

L.O. 1.3

57. Which statement best describes the six principles of finance?

a. Money has a time value; Higher returns are expected for taking on more risk; Diversification of investments does not impact risk; Financial markets are efficient in pricing securities; Manager and stockholder objectives may differ; Reputation matters.

b. Money has a time value; Higher returns are expected for taking on more risk; Diversification of investments can reduce risk; Financial markets are efficient in pricing securities; Manager and stockholder objectives may differ; Reputation matters.

c. Money has a time value; Higher returns are expected for taking on more risk; Diversification of investments can reduce risk; Financial markets are inefficient in pricing securities; Manager and stockholder objectives may differ; Reputation matters.

d. Money has a time value; Higher returns are expected for taking on more risk; Diversification of investments can reduce risk; Financial markets are efficient in pricing securities; Manager and stockholder objectives may differ; Reputation doesn’t matter.

Answer: b

Difficulty Level: Hard

Subject Heading: Six Principles of Finance

L.O. 1.3

58. An area of finance that involves the sale or marketing of securities, the analysis of securities, and the management of investment risk through portfolio diversification is referred to as

a. financial management

b. investments

c. financial institutions

d. financial markets

Answer: b

Difficulty Level: Easy

Subject Heading: Investments

L.O. 1.4

59. Intermediaries that help the financial system operate efficiently and transfer funds from savers and investors to individuals, businesses, and governments that seek to spend or invest the funds are known as:

a. financial markets

b. financial institutions

c. securities markets

d. government organizations

Answer: b

Difficulty Level: Easy

Subject Heading: Financial Institutions

L.O. 1.4

60. The financial environment:

a. encompasses the financial markets and global interactions that contribute to an efficiently operating economy.

b. encompasses the financial institutions and financial markets that contribute to an efficiently operating economy.

c. encompasses the financial system, financial institutions, financial markets, business firms, individuals, and global interactions that contribute to an efficiently operating economy.

d. encompasses the trade in goods and services by financial instruments.

Answer: c

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

61. An effective financial system must have:

a. several sets of policy makers who pass laws and make decisions relating to fiscal and monetary policies

b. an efficient system for buying goods and services

c. gold reserves equal to the amount of money in circulation

d. free trade in financial instruments with foreign nations

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

62. An area of finance that involves financial planning, asset management and fund-raising decisions to enhance the value of businesses is called:

a. financial management

b. investments

c. financial institutions

d. financial markets

Answer: a

Difficulty Level: Medium

Subject Heading: Financial Management

L.O. 1.4

63. An area of finance that involves the study of organizations or intermediaries that help the financial system operate efficiently and transfer funds from savers and investors to individuals, businesses, and governments that seek to spend or invest the funds in physical assets (inventories, buildings, and equipment) is called:

a. financial management

b. investments

c. financial institutions

d. financial markets

Answer: c

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.4

64. The \_\_\_\_\_\_\_\_\_\_\_\_\_\_ is a term used to describe the financial system, institutions, markets, businesses, individuals, and global interactions that help the economy operate efficiently

a. financial environment

b. regulatory environment

c. international environment

d. operating environment

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

65. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ provide the record-keeping mechanism for showing ownership of the financial instruments used in the flow of financial funds between savers and borrowers and record revenues, expenses, and profitability of organizations that produce and exchange goods and services.

a. Financial Managers

b. Accountants

c. Operations Managers

d. Statisticians

Answer: b

Difficulty Level: Medium

Subject Heading: Relationship between Accounting and Finance

L.O. 1.4

66. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ are intermediaries, such as banks, insurance companies, and investment companies that engage in financial activities to aid the flow of funds from savers to borrowers or investors.

a. Financial Institutions

b. Financial market organizations

c. Federal agencies

d. International financial organizations

Answer: a

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.4

67. An effective financial system needs which of the following:

a. an efficient monetary system

b. to be able to trade with other nations

c. markets in which to buy and sell goods and services

d. physical locations for markets

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

68. Crucial elements of well-developed financial systems include all of the following except:

a. government control of the economy

b. financial intermediaries

c. financial markets

d. an efficient monetary system

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

69. Financial functions in the U.S. financial system include all of these except:

a. transferring financial assets

b. creating money

c. accumulating savings

d. barter of goods and services

Answer: d

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

70. A basic requirement for an effective financial system is a monetary system that performs which of the following financial functions?

a. formation and transferring of money

b. storing gold and silver to back up money

c. creating jobs

d. transferring real assets

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

71. In the United States, most money is created by:

a. depository institutions

b. the United States Treasury

c. capital markets

d. None of the above

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

72. Checks:

a. are orders to depository institutions to transfer money to the party who received the check

b. may be safely sent in the mail

c. provide a record of payment

d. all of the above

Answer: d

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.4

73. A basic requirement of an effective financial system includes:

a. storing money

b. transferring money

c. designing money

d. all of the above

Answer: b

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

74. The basic requirements for an effective financial system in a developed economy include:

a. a store of gold reserves

b. markets for the sale of godds and services

c. markets for the transfer of financial assets

d. a freely elected government to oversee markets

Answer: c

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

75. The saving-investment process involves which of the following financial functions:

a. creating and transferring money

b. accumulating savings and lending and investing money

c. marketing and transferring financial assets

d. selling non-financial assets

Answer: b

Difficulty Level: Medium

Subject Heading: Savings-Investment Process

L.O. 1.4

76. An economy’s \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ is the interaction of policy makers, a monetary system, financial institutions, and financial markets to expedite the flow of financial capital from savings into investment:

a. banking system

b. stock market

c. capital market

d. financial system

Answer: d

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

77. An efficient \_\_\_\_\_\_\_\_\_\_\_\_\_\_ that is comprised of a central bank and a banking system that is able to create and transfer a stable medium of exchange called money.

a. allocation system

b. banking system

c. monetary system

d. market system

Answer: c

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

78. The \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ is primarily responsible for the amount of money that is created, although most of the money is actually created by depository institutions.

a. Securities Exchange Commission

b. Federal Treasury

c. Federal Reserve System

d. Financial Asset Oversight Board

Answer: b

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

79. Functions of the monetary system include which of the following:

a. creating money

b. designing money

c. storing money

d. exchanging money for goods and services

Answer: a

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.4

80. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ are crucial elements of the financial environment and well-developed financial systems.

a. Businesses and the federal government

b. International organizations such as the World Bank and International Monetary Fund

c. Well-developed barter systems

d. Financial institutions, financial markets, and investment and financial management

Answer: d

Difficulty Level: Hard

Subject Heading: Financial System

L.O. 1.4

81. The issuing of new securities, mortgages, and other claims to wealth takes place in the:

a. secondary market

b. money market

c. primary market

d. securities market

Answer: c

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

82. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ facilitate the transfer of financial assets among individuals, institutions, businesses, and governments.

a. Financial markets

b. Government institutions

c. Regulatory authorities

d. Individual investors

Answer: a

Difficulty Level: Easy

Subject Heading: Financial Markets

L.O. 1.5

83. Financial markets encourage investment by:

a. providing capital at lower rates than provided by banks

b. providing electronic execution of transactions which are faster and cheaper than other methods

c. providing the means for savers to easily and quickly convert financial assets into cash when needed

d. encouraging people not to buy goods and services

Answer: c

Difficulty Level: Medium

Subject Heading: Financial Markets

L.O. 1.5

84. The primary securities markets are

a. the markets for previously issued securities such as the New York Stock Exchange

b. the markets where financial assets such as stocks and bonds are initially issued

c. the three most important financial markets in any economy

d. the markets for stocks and bonds only

Answer: b

Difficulty Level: Medium

Subject Heading: Financial Markets

L.O. 1.5

85. Which of the following financial institutions market “seasoned” instruments and securities?

a. brokerage firms

b. finance companies

c. mortgage lenders

d. commercial banks

Answer: a

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.5

86. Brokerage firms do not perform which of the following functions?

a. handle shares of ownership

b. create money

c. market existing securities

d. transfer shares of ownership

Answer: b

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.5

87. The possible conflict between managers and owners is sometimes called the

a. principal-subordinate problem

b. principal-agent problem

c. boss-subordinate problem

d. boss-agent problem

Answer: b

Difficulty Level: Medium

Subject Heading: Agency Costs

L.O. 1.5

88. Creditworthiness reflects:

a. an individual borrower’s capacity to pay

b. where a borrower lives

c. how old a borrow is

d. the gender of a borrower

Answer: a

Difficulty Level: Medium

Subject Heading: Financial Institutions

L.O. 1.5

89. Major participants in the secondary mortgage markets include which of the following:

a. personal loan companies

b. Agricultural co-ops

c. Freddie Mae

d. Fannie Mae

Answer: d

Difficulty Level: Medium

Subject Heading: Mortgages

L.O. 1.5

90. The financial crisis of 2007-2009 resulted from a number of negative economic and financial trends including:

a. an increase in housing prices

b. an increase in stock prices

c. more credit cards

d. high debt levels

Answer: d

Difficulty Level: Medium

Subject Heading: 2007-2009 Financial Crisis

L.O. 1.5

91. Which of the following statements is most correct?

a. Capital markets include short-term and long-term debt securities such as Treasury bills, notes, and bonds.

b. Money market instruments include commercial paper, federal funds, repurchase agreements, and Treasury notes.

c. Real estate mortgages are money market instruments.

d. Federal agencies, and state and local governments, generally issue longer-term financial claims which trade in the capital market.

Answer: d

Difficulty Level: Hard

Subject Heading: Financial Markets

L.O. 1.5

92. Which of the following statements is true?

a. During the past couple of decades, generally high fixed-rate mortgage loan interest rates and the desire to extend housing ownership to more individuals in the U.S., saw the use of adjustable-rate mortgages decline.

b. An adjustable-rate mortgage (ARM) has an interest rate that does not change or variety over time with market-determined interest rates on a U.S. treasury bill or other debt security.

c. The interest rate on an ARM is often adjusted daily to reflect changes in treasury bill rates (or other interest rate benchmark).

d. Lenders typically offer ARMs with variable interest rates for one to five years with a provision to switch to a fixed-rate over the remaining life of the ARM.

Answer: d

Difficulty Level: Hard

Subject Heading: Mortgages

L.O. 1.5

93. Which of the following is true regarding mortgage backed securities?

a. A mortgage-backed security is a debt security created by pooling together a group of mortgage loans whose periodic payments belong to the holders of the security.

b. Mortgage-backed securities never “pass through” the interest and principal payments to the owners of the securities.

c. Payments on the underlying mortgages are made to the financial institution that created the mortgage-backed security, and the institution, in turn, pays or passes through the payments to the investors or owners of the securities annually.

d. Inmortgage-backed securities, issuers never separate or “strips” the interest and principal payment streams into separate securities.

Answer: a

Difficulty Level: Hard

Subject Heading: Mortgages

L.O. 1.5

94. The primary goal of the financial manager of a profit-seeking organization is to:

a. maximize market share

b. maximize the owners’ wealth

c. increase sales and profit

d. have healthy cash flow

Answer: b

Difficulty Level: Easy

Subject Heading: Basic Definitions

L.O. 1.6

95. Which of the following is a crucial element of the financial environment and a well-developed financial system?

a. financial institutions

b. markets for goods and services

c. storage facilities for gold and silver

d. trade with foreign nations

Answer: a

Difficulty Level: Easy

Subject Heading: Financial System

L.O. 1.6

96. Career opportunities in finance involving both treasury and control functions are generally associated with:

a. business financial management

b. financial intermediaries

c. securities markets

d. government organizations

Answer: a

Difficulty Level: Easy

Subject Heading: Career Opportunities

L.O. 1.6

97. An area of finance that refers to the physical locations or electronic forums that facilitate the flow of funds among investors, businesses, and governments is called:

a. financial management

b. investments

c. financial institutions

d. financial markets

Answer: d

Difficulty Level: Medium

Subject Heading: Financial Markets

L.O. 1.6

98. An area of finance that involves the evaluating of credit applications and collecting amounts owed by credit customers is called:

a. financial management

b. credit analysis

c. financial institutions

d. financial markets

Answer: e

Difficulty Level: Medium

Subject Heading: Financial System

L.O. 1.6

99. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ involves making decisions relating to issuing and investing in stocks and bonds.

a. Financial economics

b. Financial management

c. Investment management

d. Asset allocation

Answer: c

Difficulty Level: Medium

Subject Heading: Investments

L.O. 1.6

100. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ in business involves making decisions relating to the efficient use of financial resources in the production and sale of goods and services.

a. Financial management

b. Financial economics

c. Investment management

d. Asset allocation

Answer: a

Difficulty Level: Medium

Subject Heading: Financial Management

L.O. 1.6

101. Maximizing \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ is accomplished through effective financial planning and analysis, asset management, and the acquisition of financial capital.

a. the value of perquisites.

b. the owners’ wealth.

c. the firm's profits

d. the firm's earnings

Answer: b

Difficulty Level: Medium

Subject Heading: Shareholder Wealth

L.O. 1.6

102. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ is the study of how growth-driven, performance-focused, early-stage (from development through early rapid growth) firms raise financial capital and manage their operations and assets.

a. Personal finance

b. Corporate finance

c. Entrepreneurial finance

d. Investment banking

Answer: c

Difficulty Level: Medium

Subject Heading: Small Business and Personal Finance

L.O. 1.6

103. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ is the study of how individuals prepare for financial emergencies, protect against premature death and the loss of property, and accumulate wealth over time.

a. Personal finance

b. Corporate finance

c. Entrepreneurial finance

d. Investment banking

Answer: a

Difficulty Level: Medium

Subject Heading: Small Business and Personal Finance

L.O. 1.6