Section One: multiple choice questions (45 points)

1. Which of the following are sources of long-term capital for firms?
   a. long-term debt
   b. common stock
   c. Preferred stock
   d. All of the above

2. What does the firm's capital structure represent?
   a. is the mix of debt and equity the firm employs
   b. is the debt the firm employs
   c. is the equity the firm employs
   d. none of the above

3. Which of the following are Flotation costs components?
   a. underwriting fees charged by investment banking firms
   b. administrative expenses (accounting and legal)
   c. cost of goods sold expense
   d. A and B

4. Why is the cost of financing a project with retained earnings less than the cost of financing it with a new issue of common stock?
   a. the firm can avoid flotations costs
   b. receipts lost to underpricing
   c. the firm can avoid flotations costs and receipts lost to underpricing
   d. the firm's average cost of long-term finance

5. The process of evaluating and selecting long-term investments that are consistent with the firm's goal of maximizing owners' wealth. This is referred to:
   a. Cost of capital
   b. Capital budgeting
   c. capital expenditure
   d. operating expenditure

6. Unsystematic risk ________.
   a. does not change
   b. can be eliminated through diversification
   c. cannot be estimated
   d. affects all firms in a market

7. What is the expected market return if the expected return on Asset X is 20 percent, its beta is 1.5, and the risk free rate is 5 percent?
   a. 5.0%
   b. 7.5%
   c. 15.0%
   d. 22.5%

8. Cash flows are unrelated to (or independent of) one another; the acceptance of one project does not eliminate the others from further consideration. This is:
   a. Mutually exclusive projects
   b. Independent projects
   c. unlimited funds
   d. capital rationing

9. ------------ The financial situation in which a firm has only a fixed number of dollars available for capital expenditures, and numerous projects compete for these dollars.
   a. Mutually exclusive projects
   b. Independent projects
   c. unlimited funds
   d. capital rationing

10. the expected return, standard deviation of returns, and coefficient of variation for asset A are ________. (See below.)

Possible Outcomes	Probability	Returns (%)
Pessimistic	0.25	5
Most likely	0.55	10
Optimistic	0.20	13

   a. 10 percent, 8 percent, and 1.25, respectively
   b. 9.33 percent, 8 percent, and 2.15, respectively
   c. 9.35 percent, 4.68 percent, and 2.00, respectively
   d. 9.35 percent, 2.76 percent, and 0.295, respectively

11. A 15-year bond with a face value of $1,000 currently sells for $850. Which of the following statements is CORRECT?
   a. The bond's yield to maturity is greater than its coupon rate
   b. The bond's coupon rate exceeds its current yield
   c. The bond's current yield is equal to its coupon rate
   d. The bond's current yield exceeds its yield to maturity

12. Which of the following are unsecured type of bond?
   a. mortgage bonds
   b. collateral trust
   c. subordinated debentures
   d. equipment trust certificates

13. Secured by real estate or buildings. This is
   a. mortgage bonds
   b. collateral trust
   c. subordinated debentures
   d. equipment trust certificates

14. A bond with a ------------- gives holders the option of converting the bond into a certain number of shares of stock within a certain period of time.
   a. conversion feature
   b. puttable feature
   c. callable feature
   d. extendible feature

15. ---------- give bondholders the right to purchase a certain number of shares of common stock at a specified price.
   a. conversion feature
   b. puttable feature
   c. callable feature
   d. Stock purchase warrants feature

16. __________ Equals a bond's annual Coupon payment divided by its current market price. This is referred to:

   a. Yield to maturity
   b. Discount rate
   c. Current yield
   d. Required rate of return

17. Zhen Yi Computers has an outstanding issue of bond with a par value of $1,000, paying 12 percent coupon rate semi-annually. The bond was issued 25 years ago and has 5 years to maturity. What is the value of the bond assuming 14 percent rate of interest?
   a. $929.76
   b. $1,000
   c. $950.3
   d. $980.63

18. The three inputs in asset valuation are:
   a. Cash flows—cash received from asset ownership
   b. Timing—time period(s) when cash is receive
   c. Required return—risk-adjusted interest rate used to discount cash flows (i.e., higher risk implies a discount rate).
   d. All of the above

19. What is Nico's portfolio beta if he invests an equal amount in Asset X with a beta of 0.60, Asset Y with a beta of 1.60, and the risk-free asset?
   a. 1.24
   b. 1.00
   c. 0.73
   d. 0.66

20. The preemptive right gives shareholders the right ________.
   a. to caste one vote for each share owned at the annual meeting of the company
   b. to give up their vote to another party if they do not attend the annual meeting
   c. to maintain their proportionate ownership in the corporation when new common stock is issued
   d. to sell their share of stock at a premium in the event of liquidation

21. A firm has the balance sheet accounts, Common Stock and Paid-in Capital in Excess of Par, with values of $40,000 and $500,000, respectively. The firm has 40,000 common shares outstanding. If the firm had a par value of $1, the stock originally sold for ________.
   a. $11.50/share
   b. $12.50/share
   c. $13.50/share
   d. $15.50/share

22. The cost of a long-term debt generally ________ that of a short-term debt.
   a. is less than
   b. is equal to
   c. is greater than
   d. is less than or equal to

23. Deeply discounted bond that pays no coupon interest is a ________.
   a. junk bond
   b. floating rate bond
   c. zero coupon bond
   d. subordinated debenture

41. A firm has determined its cost of each source of capital and optimal capital structure, which is composed of the following sources and target market value proportions:

Source of Capital	Target Market Proportions	After-Tax Cost
Long-term debt	40%	6%
Preferred stock	10	11
Common stock equity	50	15

The weighted average cost of capital is ________.

a. 6 percent
b. 10.7 percent
c. 11 percent
d. 15 percent

42. ________ projects have the same function; the acceptance of one ________ the others from consideration.

a. Capital; eliminates
b. Independent; does not eliminate
c. Mutually exclusive; eliminates
d. Replacement; eliminates

43. The final step in the capital budgeting process is ________.

a. implementation
b. follow-up
c. review and analysis
d. decision making

44. What is the NPV for a project if its cost of capital is 0 percent and its initial after-tax cost is $5,000,000 and it is expected to provide after-tax operating cash inflows of $1,800,000 in year 1, $1,900,000 in year 2, $1,700,000 in year 3, and $1,300,000 in year 4?

a. $1,700,000
b. $371,764
c. $137,053
d. $6,700,000

45. A firm is evaluating three capital projects. The net present values for the projects are as follows:

Project	NPV
1	$100
2	$10
3	-$100

The firm should ________.

a. accept Projects 1 and 2, and reject Project 3
b. accept Projects 1 and 3, and reject Project 2
c. accept Project 3, and reject Projects 1 and 2
d. accept all projects

38. At year end, Tangshan China Company balance sheet showed total assets of $60 million, total liabilities (including preferred stock) of $45 million, and 1,000,000 shares of common stock outstanding. If Tangshan could sell its assets for $52.5 million, Tangshan's liquidation value per share of common stock is ________.

a. $15
b. $7.50
c. $52.50
d. $75

39. Julie's X-Ray Company paid $2.00 per share in common stock dividends last year. The company's policy is to allow its dividend to grow at 5 percent for 4 years and then the rate of growth changes to 3 percent per year from year five and on. What is the value of the stock if the required rate of return is 8 percent?

a. $44.27
b. $40.38
c. $7.46
d. 36.81

40. A firm has common stock with a market price of $100 per share and an expected dividend of $5.61 per share at the end of the coming year. A new issue of stock is expected to be sold for $98, with $2 per share representing the underpricing necessary in the competitive capital market. Flotation costs are expected to total $1 per share. The dividends paid on the outstanding stock over the past five years are as follows:

Year	Dividend
1	$4.00
2	4.28
3	4.58
4	4.90
5	5.24

The cost of this new issue of common stock is ________.

a. 5.8 percent
b. 7.7 percent
c. 10.8 percent
d. 12.8 percent

34. The cost of common stock equity may be estimated by using the ________.

a. yield curve
b. break-even analysis
c. Gordon model
d. DuPont analysis

35. Aunt Tilly's Fur Company has been experiencing several years of financial difficulty and, thus, has considered maintaining its dividend payment at $2.50 indefinitely. What is the value of its common stock if the required rate of return is 8.5 percent?

a. $29.41
b. $2.30
c. $27.50
d. $33.33

36. At year end, Tangshan China Company balance sheet showed total assets of $60 million, total liabilities (including preferred stock) of $45 million, and 1,000,000 shares of common stock outstanding. Based on this information, Tangshan's book value per share of common stock is ________.

a. $105
b. $10.50
c. $15
d. $150

37. B Company is considering the purchase of a piece of equipment that costs $23,000. Projected net annual cash flows over the project's life are:

Year	Net Annual Cash Flow
1	$3,000
2	8,000
3	15,000
4	9,000

The cash payback period is:

e. 2.63 years.
f. 2.80 years.
g. 2.37 years.
h. 2.20 years.

28. Based on the above information what is the firm's cost of Debt before tax?
   a. 4.4 percent
   b. 3.7 percent
   c. 7.3 percent
   d. 3.8 percent
   e. 7.6 percent

29. Based on the above information what is the firm's cost of Debt After tax?
   a. 1.44 percent
   b. 2.44 percent
   c. 1.26 percent
   d. 1.5 percent
   e. 2.22 percent

30. Based on the above information what is the Market Value of the firm's Common Stocks?
   a. $700,000
   b. $7,000,000
   c. $625,000
   d. $7,500,000
   e. Insufficient information

31. Based on the above information what is the market Value of the firm's bonds?
   a. $7,000,000
   b. $7,350,000
   c. $6,860,000
   d. $7,500,000
   e. Cannot be determine

32. Based on the above information what is the weights of the firm's debt and equity respectively?
   a. 70% debt, 30% equity
   b. 51.2% debt, 48.8% equity
   c. 50% debt, 50% equity
   d. 48.8% debt, 51.2% equity

33. Based on the above information What is the firm's weighted average cost of capital?
   a. 5.4 percent
   b. 6.2 percent
   c. 4.9 percent
   d. 8.5 percent

24. If the coupon rate of a bond is equal to its required rate of return, then ________.

a. the current value is not equal to par value
b. the current value is equal to par value
c. the maturity value is equal to par value
d. the current value is equal to maturity value

25. The common stock of Metal Molds has a negative growth rate of 1.5 percent and a required return of 18 percent. The current stock price is $11.40. What was the amount of the last dividend paid?

a. $2.07
b. $2.11
c. $2.19
d. $2.22
e. $2.26

26. Highway Express has paid annual dividends of $1.16, $1.20, $1.25, $1.10, and $0.95 over the past five years respectively. What is the average dividend growth rate?

a. -4.51 percent
b. -3.60 percent
c. 2.28 percent
d. 2.47 percent
e. 4.39 percent

R.S. Green has 250,000 shares of common stock outstanding at a market price of $28 a share. Next year's annual dividend is expected to be $1.55 a share. The dividend growth rate is 2 percent. The firm also has 7,500 bonds outstanding with a face value of $1,000 per bond. The bonds carry a 7 percent coupon, pay interest semiannually, and mature in 7.5 years. the bonds are selling at 98% of face Value. The company's tax rate is 34 percent.

27. Based on the above information what is the firm's cost of common stock?

a. 25.9 percent
b. 7.5 percent
c. 7.9 percent
d. 8.5 percent
e. 9.6 percent