**Investment Principles**

**Homework 2**

Following are 30 Multiple Choice questions, each worth 3.3 points, Select the answer that you think is most appropriate for the question.

***Equity Research***

1) Investors who conduct industry analyses typically favor companies with strong market positions over companies with less secure market positions because firms with strong market positions tend to

I. be price leaders.

II. benefit more from economies of scale.

III. have better R&D programs.

IV. have lower production costs.

A) II and IV only.

B) I, II and IV only.

C) I, II and III only

D) I, II, III and IV

2) The consumer electronics would be most significantly affected by

A) developments in technology.

B) interest rates and inflation.

C) labor relations.

D) government regulations.

3) The stage in an industry's growth cycle in which product acceptance is spreading, investors can foresee the industry's future, and overall economic variables have little to do with the industry's overall performance, is known as the

A) initial development stage.

B) rapid expansion stage.

C) mature growth stage.

D) stability or decline stage.

4) Which of the following are considered in the company analysis phase of a fundamental analysis of a firm?

I. the composition and growth in sales

II. the capital structure of the firm

III. the outlook of the national economy

IV. the composition and liquidity of the company's assets

A) I and II only

B) I, II and IV only

C) II and IV only

D) I, II, III and IV

5) Which one of the following statements concerning accounting reports is correct?

A) The income statement reflects the position of a firm as of a single point in time.

B) The total equity of a firm is equal to the total assets plus the total liabilities.

C) The statement of cash flows identifies both the sources and the uses of cash.

D) The income statement reflects the amount of cash available for investment and financing activities.

6) Cash flow from operations

A) represents the amount of cash generated by the company.

B) is the least important section of the Statement of Cash Flows.

C) is the amount of cash acquired from the borrowing activities of the firm.

D) represents the cash flows from the purchase and sale of long-term assets.

7) Which of the following would be typical of a Statement of Cash Flows for a healthy firm in a sustainable business?

A) Cash flow from operations is negative, cash flows from investment activities and financing activities are positive.

B) Cash flow from operations , investment activities and financing activities must all be positive.

C) Cash flow from operations is positive, cash flows from investment activities and financing activities are negative.

D) If the Statement shows a net increase in cash, the source is unimportant.

8) Which of the following measures excludes non-cash charges against income.

A) operating expenses

B) EBIT

C) net income before taxes

D) EBITDA

9) Which of the following would be found on a company's income statement?

I. cost of goods sold

II. interest expense

III. cash flow from operations

IV. earnings before taxes

A) I an IV only

B) I, II and III only

C) I, II and IV only

D) I, II, III and IV

10) Which of the following would be found on a company's balance sheet?

I. Accounts receivable

II. Interest expense

III. Property plant and equipment

IV. Total stockholders' equity

A) I an IV only

B) I, II and III only

C) I, II and IV only

D) I, III and IV only

**Efficient Markets**

1) An efficient market reflects

A) only historical information.

B) only the information related to events that have already occurred.

C) all publicly known information related to past events and announced future events.

D) all information including predictions about future information.

2) A type of mutual fund with particular appeal to investors who accept the efficient market hypothesis is

A) index fund.

B) asset allocation fund.

C) growth opportunities fund.

D) emerging markets fund.

3) In an efficient market, prices appear to move randomly because

A) investors do not process new information correctly.

B) only new information affects stock prices.

C) insider trading has an unpredictable effect on stock prices.

D) the number of investors who can forecast prices correctly is too small to have any effect.

4) The efficient market hypothesis rests on which of the following assumptions?

I. Information is widely available to all investors almost simultaneously.

II. Investors react quickly to new information.

III. Investors correctly interpret all available information.

IV. Events which affect the market occur randomly.

A) I and II only

B) I, II and III only

C) I, III and IV only

D) I, II, III and IV

5) Which one of the following best describes the term "efficient market"?

A) The commissions on large transactions are smaller than the commissions on small transactions.

B) New information is quickly reflected in security prices.

C) Little time and effort are spent on marketing securities to the public.

D) The cost of receiving, processing, executing, and reporting securities orders is small.

6) Based on the semi-strong form of the efficient market theory, an investor reacting immediately to a news flash on the television generally

A) can make an abnormal profit.

B) is guaranteed to make a reasonable profit.

C) is too late to make an exceptional profit.

D) will suffer a loss.

7) Followers of the random walk hypothesis believe that

A) security analysis is the best tool to utilize when investing in the stock market.

B) the price movements of stocks are unpredictable, and therefore security analysis will not help to predict future market behavior.

C) that traders can earn higher than normal returns by exploiting market anomalies such as the small-firm effect.

D) support levels and resistance lines, when combined with basic chart formations, yield both buy and sell signals.

8) Which one of the following statements concerning the random walk hypothesis is correct?

A) Stock price movements are predictable but only over short periods of time.

B) Random price movements support the weak form efficient market hypothesis.

C) Stock prices in general follow repetitive patterns but the actions of individual investors are random in nature.

D) Random price movements indicate that investors can earn abnormal profits on a routine basis.

9) Which of the following is true?

A) Historically, high P/E or growth stocks have outperformed low P/E or value stocks.

B) Historically, low P/E or value stocks have outperformed high P/E or growth stocks.

C) After adjusting for risk, high P/E or growth stocks and low P/E or value stocks have performed about the same over time.

D) the P/E effect is limited to U.S. stocks.

10) Investor overconfidence leads to

A) too little trading.

B) an overestimation of risk.

C) overly optimistic predictions.

D) narrow framing.

**Fixed-Income Securities**

1) Which of the following are advantages of owning bonds?

I. diversification properties

II. higher long-term returns than equity holdings

III. current income

IV. relatively low risk

A) I and II only

B) I, III and IV only

C) I, II and III only

D) I, II, III and IV

2) When bonds are initially added to an all-equity portfolio the

A) level of risk of the portfolio is impacted more than the rate of return.

B) rate of return on the portfolio is impacted more than the level of risk.

C) level of risk and the rate of return are equally impacted.

D) rate of return is not impacted but the level of risk is lowered.

3) The phenomenon known as "flight to quality" causes yields on government bond and corporate bonds

A) to rise in tandem.

B) to fall in tandem.

C) to move in opposite directions.

D) to become less volatile.

4) Which of the following types of risk affect bonds?

I. call risk

II. business risk

III. purchasing power risk

IV. liquidity risk

A) III and IV only

B) II, III and IV only

C) I, III and IV only

D) I, II, III and IV

5) The bond market is considered bearish when

A) market interest rates are low or falling.

B) market interest rates are high or rising.

C) the risk-free rate of return exceeds the required rate of return.

D) more bonds are called than issued over a given period of time.

6) When interest rates are falling, most of the return on bonds will come from

A) inflation gains.

B) interest income.

C) capital gains.

D) risk premiums.

7) Which type of risk is based on the financial integrity of a bond issuer?

A) liquidity risk

B) call risk

C) default risk

D) interest rate risk

8) Under normal economic conditions, the major source of risk faced by investors who purchase investment grade bonds is

A) purchasing power risk.

B) interest rate risk.

C) liquidity risk.

D) default risk.

9) In a severe recession, the major source of risk faced by investors who purchase corporate bonds is

A) purchasing power risk.

B) interest rate risk.

C) liquidity risk.

D) default risk.

10) A single bond issue with multiple maturity dates is called a

A) callable bond.

B) premium bond.

C) serial bond.

D) term bond.