CB3044: Mock Exam

Due in class, **Monday 21 November 2022 2:45PM**

EXPLAIN your answer, whenever relevant – you will not be penalized for a well-explained answer, whether or not it's correct.

1. (I) Prices of longer-maturity bonds respond more dramatically to changes in interest rates.

   (II) Prices and returns for long-term bonds are less volatile than those for short-term bonds.

A) (I) is true, (II) false.

B) (I) is false, (II) true.

C) Both are true.

D) Both are false.

2. The duration of a portfolio of securities is the _____ average of the durations of the individual securities.

A) geometric

B) weighted

C) simple

D) arithmetic

3. _____ bonds are the most liquid of all long-term bonds.

A) Callable

B) Municipal

C) Corporate Aaa

D) U.S. Treasury

4. Typically, yield curves are

A) gently upward-sloping.

B) gently downward-sloping.

C) flat.

D) bowl shaped.

E) mound shaped.

5. To say that stock prices follow a "random walk" is to argue that

A) stock prices rise, then fall.

B) stock prices rise, then fall in a predictable fashion.

C) stock prices tend to follow trends.

D) stock prices are, for all practical purposes, unpredictable.

6. Which of the following is NOT an implication of the strong view of market efficiency in an efficient market?

A) One investment is as good as any other because the securities' prices are correct.

B) Security prices will reflect all relevant information about a securities price: past, present, and future.

C) A security's price reflects all available information about the intrinsic value of the security.

D) Security prices can be used by managers of both financial and nonfinancial firms to assess their cost of capital (cost of financing their investments) accurately.

7. A conflict of interest occurs when

A) a financial firm sells a service to its customers for a price that exceeds the cost of producing the service.

B) lenders prefer higher interest rates and borrowers prefer lower interest rates.

C) riskier borrowers are the ones who are more likely to apply for loans.

D) people expected to provide reliable information to the public have incentives not to do so.

8. Since firms issuing new securities pay to have these securities rated, the credit-rating agencies have incentive to _____ to attract more business.

A) give favorable ratings

B) give impartial ratings

C) lower the fees they charge

D) practice spinning

9. Treasury bills do not

A) pay interest.

B) have a maturity date.

C) have a face amount.

D) have an active secondary market.

10. If the Fed wants to lower the federal funds interest rate, it will _____ the banking system by _____ securities.

A) add reserves to; selling

B) add reserves to; buying

C) remove reserves from; selling

D) remove reserves from; buying

11. (I) To sell an old bond when interest rates have risen, the holder will have to discount the bond until the yield to the buyer is the same as the market rate. (II) The risk that the value of a bond will fall when market interest rates rise is called interest-rate risk.

A) (I) is true, (II) false.

B) (I) is false, (II) true.

C) Both are true.

D) Both are false.

12. A change in the current yield _____ signals a change in the same direction of the yield to maturity.

A) never

B) rarely

C) always

D) often

13. According to the Gordon growth model, what is an investor's valuation of a stock whose current dividend is $1.00 per year if dividends are expected to grow at a constant rate of 10 percent over a long period of time and the investor's required return is 15 percent?

A) $20

B) $11

C) $22

D) $7.33

E) $4.40

14. The PE ratio approach to valuing stock is especially useful for valuing

A) publicly held corporations.

B) firms that regularly pay dividends.

C) both A and B of the above.

D) neither A nor B of the above.

15. Which of the following are true of mortgages?

A) A mortgage is a long-term loan secured by real estate.

B) Borrowers pay off mortgages over time in some combination of principal and interest payments that result in full payment of the debt by maturity.

C) Less than 65 percent of mortgage loans finance residential home purchases.

D) All of the above are true of mortgages.

E) Only A and B of the above are true of mortgages.

16. _____ issues participation certificates, and _____ provides federal insurance for participation certificates.

A) Freddie Mac; Freddie Mac

B) Freddie Mac; Ginnie Mae

C) Ginnie Mae; Freddie Mac

D) Ginnie Mae; Ginnie Mae

E) Freddie Mac; no one

17. _____ intermediation means that small investors can pool their funds with other investors to purchase high face value securities.

A) Liquidity

B) Financial

C) Denomination

D) Share

18. "Stripping" a Treasury bond

A) means selling each of its future payments as a separate zero-coupon bond.

B) decreases the total present discounted value of future payments.

C) both A and B.

D) none of the above.

19. Financial derivatives include

A) stocks.

B) bonds.

C) forward contracts.

D) both A and B.

20. By selling short a futures contract of $100,000 at a price of 96, you are agreeing to deliver _____ face value securities for _____.