Student name:__________

The material wealth of a society is a function of

all financial assets.

all real assets.

all financial and real assets.

all physical assets.

______ are real assets.

Land

Machines

Stocks and bonds

Knowledge

Land, machines, and knowledge

The means by which individuals hold their claims on real assets in a well-developed economy are

investment assets.

depository assets.

derivative assets.

financial assets.

exchange-driven assets.

______ are financial assets.

Bonds

Machines

Stocks

Bonds and stocks

Bonds, machines, and stocks

______ financial asset(s).

Buildings are

Land is a

Derivatives are

Canadian T-Bills are

Derivatives and Canadian bonds are

Financial assets

directly contribute to the country's productive capacity.

indirectly contribute to the country's productive capacity.

contribute to the country's productive capacity, both directly and indirectly.

do not contribute to the country's productive capacity, either directly or indirectly.

are of no value to anyone.

A security that pays a specified cash flow over a specific period is called

fixed income.

stock option.

mutual fund.

real estate.

index.

______ is a commodity.

Money

Forward contract

Oil

A bond

Treasury-bill

Compared to investments in debt securities, equity investments tend to be

equally risky.

riskier.

less risky.

more important.

Which one of the following is not a role of the financial markets?

Consumption timing

Information

Separation of ownership and control

Increasing wealth of the economy

Risk allocation

Holding highly diversified portfolios without spending effort or other resources attempting to improve investment performance through security analysis is a characteristic of

Active management.

Passive management.

Both active and passive management.

Risk-return trade-off.

Efficient markets.

The attempt to improve performance either by identifying mispriced securities or by timing the performance of broad asset classes is a characteristic of:

Active management

Passive management

Both active and passive management

Risk-return trade-off

Efficient markets

A common measure of credit risk in the banking sector is

systemic Risk.

treasury-bill.

TED spread.

LIBOR.

yield curve.

______ is in an insurance contract against the default of one or more borrowers.

Collateralized debt obligation

credit default swap

Freddie Mac

Adjustable-rate mortgage

Fannie Mae

Systemic risk is

credit risk.

an insurance contract against the default of one or more borrowers.

firm-specific risk.

default risk.

the potential breakdown of the financial system when problems in one market spill over and disrupt others.

A fixed-income security pays

a fixed level of income for the life of the owner.

a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

a variable level of income for owners on a fixed income.

a fixed or variable income stream at the option of the owner.

A debt security pays

a fixed level of income for the life of the owner.

a variable level of income for owners on a fixed income.

a fixed or variable income stream at the option of the owner.

a fixed stream of income or a stream of income that is determined according to a specified formula for the life of the security.

Money market securities

are short term.

are highly marketable.

are medium risk.

are highly marketable and are short term.

All of the options.

An example of a derivative security is

a common share of Amazon.

a call option on the S&P500 Index.

A crude oil futures contract.

a call option on S&P500 Index and a crude oil futures contract.

a common share of Amazon and a call option on the S&P500 Index.

The value of a derivative security

depends on the value of the related security.

is unable to be calculated.

is unrelated to the value of the related security.

has been enhanced due to the recent misuse and negative publicity regarding these instruments.

is worthless today.

Although derivatives can be used as speculative instruments, businesses most often use them to

attract customers.

appease stockholders.

offset debt.

hedge risks.

enhance their balance sheets.

Financial assets permit all of the following except

consumption timing.

allocation of risk.

separation of ownership and control.

elimination of risk.

The ______ refers to the potential conflict between management and shareholders.

agency problem

diversification problem

liquidity problem

solvency problem

regulatory problem

A disadvantage of using stock options to compensate managers is that

it encourages managers to undertake projects that will increase stock price.

it encourages managers to engage in empire building.

it can create an incentive for managers to manipulate information to prop up a stock price temporarily, giving them a chance to cash out before the price returns to a level reflective of the firm's true prospects.

All the options are true.

Which of the following are mechanisms that have evolved to mitigate potential agency problems?
I) Using the firm's stock options for compensation
II) Hiring bickering family members as corporate spies
III) Boards of directors protecting the interest of management.

IV) Security analysts monitoring the firm closely
V) Takeover threats

II and V

I, III, and IV

I, IV, and V.

III, IV, and V

I, III, and V

Corporate shareholders are best protected from incompetent management decisions by

the ability to engage in proxy fights.

management's control of pecuniary rewards.

the ability to call shareholder meetings.

the threat of takeover by other firms.

one-share/one-vote election rules.

Theoretically, takeovers should result in

improved management.

increased stock price.

increased benefits to existing management of the taken-over firm.

improved management and increased stock price.

All of the options.

During the period between 2000 and 2002, a large number of scandals were uncovered. Most of these scandals were related to
I) manipulation of financial data to misrepresent the actual condition of the firm.
II) misleading and overly optimistic research reports produced by analysts.

III) allocating IPOs to executives as a quid pro quo for personal favors.
IV) greenmail.

II, III, and IV

I, II, and IV

II and IV

I, III, and IV

I, II, and III

The Sarbanes-Oxley Act

requires corporations to have more independent directors.

requires the firm's CFO to personally vouch for the firm's accounting statements.

prohibits auditing firms from providing other services to clients.

requires corporations to have more independent directors and requires the firm's CFO to personally vouch for the firm's accounting statements.

All of the options are true.

Asset allocation refers to

choosing which securities to hold based on their valuation.

investing only in "safe" securities.

the allocation of assets into broad asset classes.

bottom-up analysis.

Security selection refers to

choosing which securities to hold based on their valuation.

investing only in "safe" securities.

the allocation of assets into broad asset classes.

top-down analysis.

Which of the following portfolio construction methods starts with security analysis?

Top-down

Bottom-up

Middle-out

Buy and hold

Asset allocation

Which of the following portfolio construction methods starts with asset allocation?

Top-down

Bottom-up

Middle-out

Buy and hold

Asset allocation

______ are examples of financial intermediaries.

Commercial banks

Insurance companies

Investment companies

Credit unions

All of the options

Financial intermediaries exist because small investors cannot efficiently

diversify their portfolios.

assess credit risk of borrowers.

advertise for needed investments.

diversify their portfolios and assess credit risk of borrowers.

All of the options.

______ specialize in helping companies raise capital by selling securities.

Commercial bankers

Investment bankers

Investment issuers

Credit raters

Commercial banks differ from other businesses in that both their assets and their liabilities are mostly

illiquid.

financial.

real.

owned by the government.

regulated.

… Is an insurance contract against the default of one or more borrowers.

Credit default swap.

Collateralized debt obligation.

LIBOR.

Subprime mortgage.

The application of technology to financial markets, that has changed many aspects of the financial landscape is called:

Decentralized finance.

Fintech.

Peer-to-peer lending.

Robo Advice

The S&P/TSX Total return Index fell by almost … from its peak during the Financial Crisis of 2008-2009.

50%.

20%.

70%.

All factors below contributed to the ranking of Canada's banks the soundest among 134 countries by the World Economic Forum, except:

Canadian banks were better capitalized.

Canadian banks had more conservative lending practices.

Deposits were used to finance lending.

widespread securitization or mortgages.

Prior to 1970, most U.S. mortgage loans would come from:

Fannie Mae (FNMA, or Federal National Mortgage Association),

Freddie Mac (FHLMC, or Federal Home Loan Mortgage Corporation)

a local lender such as a neighbourhood savings bank or credit union, Mortgage-backed securities.

Prior to the 2008-2009 financial crisis, the following financial instruments presence exploded in the market:

CDO’s,

CDS’s,

ARM’s.

All of the above.

Which country was the hardest hit by the spread of the 2008-2009 financial crisis around the world?

Canada,

China.

Grece,

Germany

New issues of securities are sold in the ______ market(s).

primary

secondary

over-the-counter

primary and secondary

Investors trade previously issued securities in the ______ market(s).

primary

secondary

primary and secondary

derivatives

Investment bankers perform which of the following role(s)?

Market new stock and bond issues for firms

Provide advice to the firms as to market conditions, price, etc.

Design securities with desirable properties

All of the options

None of the options

Prior to the 2008-2009 financial crisis, the combination of ____and an apparently stable economy fed a historic boom in the housing market.

dramatically reduced interest rates,

increased unemployment,

increased inflation,

low yields on a wide variety of investments

The spread between the LIBOR and the Treasury-bill rate is called the

term spread.

T-bill spread.

LIBOR spread.

TED spread.

Mortgage-backed securities were created when _______ began buying mortgage loans from originators and bundling them into large pools that could be traded like any other financial asset.

GNMA

FNMA

FHLMC

FNMA and FHLMC

GNMA and FNMA

The sale of a mortgage portfolio by setting up mortgage pass-through securities is an example of

credit enhancement.

credit swap.

unbundling.

derivatives.

Which of the following is true about mortgage-backed securities?
I) They aggregate individual home mortgages into homogeneous pools.
II) The purchaser receives monthly interest and principal payments received from payments made on the pool.
III) The banks that originated the mortgages maintain ownership of them.
IV) The banks that originated the mortgages may continue to service them.

II, III, and IV

I, II, and IV

II and IV

I, III, and IV

I, II, III, and IV

_______ were designed to concentrate the credit risk of a bundle of loans on one class of investor, leaving the other investors in the pool relatively protected from that risk.

Stocks

Bonds

Derivatives

Collateralized debt obligations

All of the options

_______ are, in essence, an insurance contract against the default of one or more borrowers.

Credit default swaps

CMOs

ETFs

Collateralized debt obligations

All of the options

What fueled the stock market rally that took hold in April 2020 during the COVID-19 Pandemic?

Massive vaccinations across the world

Indication from central banks that interest rates would remain low

Expectations of a strong recovery in economic growth

Indications that rates would remain low and the expectation of strong economic recovery

All of the options

The Canadian equity market, with its relatively high weight in resource stocks, tends to perform well in ______

An inflationary environment.

A financial crisis.

A global pandemic.

A deflationary environment.

All of the options

Most venture capital funds are set up as

An insurance company

Sole Proprietorships.

Corporations.

Limited partnerships.

None of the options

The so-called Volcker Rule, named after former chair of the Federal Reserve Paul Volcker, prohibits banks from trading for their own accounts and restricts their investments in _____.

hedge funds and equity funds

private equity or mutual funds

mutual funds or hedge funds

equity funds and mutual funds

hedge funds or private equity

Mortgage-backed securities

aggregate individual home mortgages into homogeneous pools

Are owned by the banks that originated the mortgages maintain ownership of them.

Are derivatives

insurance contract against the default of one or more borrowers

Answer Key

Test name: Ch1_Investments_11e

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