

c1

Student: _____

1. The means by which individuals hold their claims on real assets in a well-developed economy are
 - A. investment assets.
 - B. depository assets.
 - C. derivative assets.
 - D. financial assets.
 - E. exchange-driven assets.
2. The material wealth of a society is a function of _____.
 - A. all financial assets
 - B. all real assets
 - C. all financial and real assets
 - D. all physical assets
 - E. all commodities
3. The stage an individual is in his/her life cycle will affect his/her _____.
 - A. return requirements
 - B. risk tolerance
 - C. asset allocation
 - D. **a and b**
 - E. **a, b, and c**
4. Investment objectives
 - A. must be consistent with investment constraints.
 - B. must be in direct contrast with investment constraints.
 - C. and investment constraints determine investment policies.
 - D. **a and b.**
 - E. **a and c.**
5. _____ real asset(s).
 - A. Land is a
 - B. Machines are
 - C. Both stocks and bonds are
 - D. Knowledge is a
 - E. Land, machines and knowledge are

6. _____ financial asset(s).
- A. Buildings are
 - B. Land is a
 - C. Derivatives are
 - D. Canadian government bonds are
 - E. Both derivatives and Canadian government bonds are
7. Investors seeking to diversify are likely to find that their largest investment is in
- A. stocks.
 - B. bonds.
 - C. their job.
 - D. foreign securities.
 - E. cash.
8. _____ of an investment bank.
- A. BMO Nesbitt is an example
 - B. CIBC is an example
 - C. Scotia Capital is an example
 - D. **a** and **b** are examples
 - E. **a** and **c** are examples
9. _____ are financial assets.
- A. Bonds
 - B. Machines
 - C. Stocks
 - D. **a** and **c**
 - E. **a**, **b** and **c**
10. An example of a derivative security is _____.
- A. a common share of Canadian Pacific
 - B. a call option on BMO stock
 - C. a commodity futures contract
 - D. **b** and **c**
 - E. **a** and **b**
11. _____ was the first to introduce mortgage pass-through securities in Canada.
- A. CMHC
 - B. TD Bank
 - C. FNMA
 - D. GNMA
 - E. None of these

12. A bond issue is broken up so that some investors will receive only interest payments while others will receive only principal payments, which is an example of _____.
- A. bundling
 - B. securitization
 - C. unbundling
 - D. financial engineering
 - E. **c and d**
13. An example of a primitive security is _____.
- A. a common share of RBC
 - B. a call option on CIBC stock
 - C. a call option on a stock of a firm based in a Third World country
 - D. a Canada bond
 - E. **a and d.**
14. The _____ refers to the potential conflict between management and shareholders due to management's control of pecuniary rewards as well as the possibility of incompetent performance by managers.
- A. agency problem
 - B. diversification problem
 - C. liquidity problem
 - D. solvency problem
 - E. regulatory problem
15. _____ financial asset(s).
- A. Buildings are
 - B. Land is a
 - C. Derivatives are
 - D. EDC bonds are
 - E. **c and d**
16. The value of a derivative security _____.
- A. depends on the value of the related primitive security
 - B. can only cause increased risk.
 - C. is unrelated to the value of the related primitive security
 - D. has been enhanced due the recent misuse and negative publicity regarding these instruments
 - E. is worthless today
17. _____ are indirect way through which U.S. investors can invest in foreign companies.
- A. ADRs
 - B. RRSPs
 - C. SDRs
 - D. GNMA's
 - E. Krugerrands

18. _____ are examples of financial intermediaries.

- A. Chartered banks
- B. Insurance companies
- C. Investment companies
- D. Credit unions
- E. All of these

19. Financial intermediaries exist because small investors cannot efficiently _____.

- A. diversify their portfolios
- B. gather information
- C. monitor their portfolios
- D. advertise for needed investments
- E. all of these.

20. Financial intermediaries differ from other businesses in that both their assets and their liabilities are mostly

- A. illiquid.
- B. owned by government.
- C. real.
- D. financial.
- E. regulated.

21. Firms that specialize in helping companies raise capital by selling securities are called _____.

- A. chartered banks
- B. investment banks
- C. trust companies
- D. credit unions
- E. all of these.

22. In what roles do investment bankers perform?

- A. design securities with desirable properties
- B. market new stock and bond issues for firms
- C. provide advice to the firms as to market conditions, price, etc.
- D. none of these
- E. all of these

23. Financial assets _____.

- A. directly contribute to the country's productive capacity
- B. indirectly contribute to the country's productive capacity
- C. contribute to the country's productive capacity both directly and indirectly
- D. do not contribute to the country's productive capacity either directly or indirectly
- E. are of no value to anyone

24. The sale of a mortgage portfolio by setting up mortgage pass-through securities is an example of _____.
- A. call options
 - B. securitization
 - C. unbundling
 - D. derivatives
 - E. none of these
25. Corporate shareholders are best protected from incompetent management decisions by
- A. the ability to engage in proxy fights.
 - B. management's control of pecuniary rewards.
 - C. the ability to call shareholder meetings.
 - D. the threat of takeover by other firms.
 - E. one-share/one-vote election rules.
26. Theoretically, takeovers should result in _____.
- A. improved management
 - B. increased stock price
 - C. increased benefits to existing management of taken over firm
 - D. **a** and **b**
 - E. **a**, **b**, and **c**
27. Collateralized mortgage obligations were created to
- A. aggregate individual mortgages into relatively homogeneous pools.
 - B. meet the demand for mortgage-backed securities with a range of maturities.
 - C. rebundle separate branches into a single unit.
 - D. circumvent the requirements of Regulation Q.
 - E. provide government insurance for mortgages.
28. Derivative securities are
- A. potentially dangerous because they are highly leveraged
 - B. an effective tool to better manage business returns and risk
 - C. always structured as option contracts
 - D. both **a** and **b** are true
 - E. all of these are true
29. Important trends changing the contemporary investment environment are
- A. globalization
 - B. securitization
 - C. bundling and unbundling
 - D. financial engineering
 - E. all of these

30. The term "human capital" refers to

- A. the total amount of capital owned by humans.
- B. the value of the earnings potential of the workforce.
- C. the value of a firm's management personnel.
- D. the value of a firm's blue-collar workers.
- E. the value of equipment that is operated by company personnel.

31. What are the objectives of businesses issuing securities to the public?

- A. To get the best possible price for their securities.
- B. To market the issues to the public at the lowest cost.
- C. To issue fairly simple securities requiring little incremental analysis.
- D. All of these are true.
- E. None of these is true.

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

- A. investment assets.
- B. depository assets.
- C. derivative assets
- D. financial assets.
- E. exchange-driven assets

33. Which of the following are mechanisms that have evolved to mitigate potential agency problems?

- I. compensation in the form of the firm's stock options
- II. hiring bickering family members as corporate spies
- III. underperforming management teams being forced out by boards of directors
- IV. security analysts monitoring the firm closely
- V. takeover threats

- A. II and V
- B. I, III, and IV
- C. I, III, IV, and V
- D. III, IV, and V
- E. I, III, and V

34. Until 1999, the _____ Act(s) prohibited banks in the United States from both accepting deposits and underwriting securities.

- A. Sarbanes-Oxley
- B. Glass-Steagall
- C. SEC
- D. Sarbanes-Oxley and SEC
- E. None of the options

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

- A. attract customers.
- B. appease stockholders.
- C. offset debt.
- D. hedge.
- E. enhance their balance sheets.

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

- A. The Government of Canada
- B. EDC
- C. The Bank of Canada
- D. CMHC
- E. EDC and CMHC

37. 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 continue to service them.

- A. II, III, and IV
- B. I, II, and IV
- C. II and IV
- D. I, III, and IV
- E. I, II, III, and IV

38. Discuss the agency problem in detail.

39. Discuss the various types of securities markets. Distinguish between initial sale of the assets and subsequent sales. Also distinguish between the middlemen in the different markets.

40. Discuss the euro in relation to its impact on globalization. How is it currently used and what are the plans for its future use?
41. Discuss the similarities and differences between real and financial assets.
42. Discuss securitization as it relates to the field of investments.

c1 KEY

1. The means by which individuals hold their claims on real assets in a well-developed economy are
- A. investment assets.
 - B. depository assets.
 - C. derivative assets.
 - D.** financial assets.
 - E. exchange-driven assets.

Financial assets allocate the wealth of the economy. Example: it is easier for an individual to own shares of an auto company than to own an auto company directly.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #1
Difficulty: Basic

2. The material wealth of a society is a function of _____.
- A. all financial assets
 - B.** all real assets
 - C. all financial and real assets
 - D. all physical assets
 - E. all commodities

The material wealth of a society is a function of all real assets (i.e. land, buildings, machines, knowledge, workers and their skills). Other assets, per se, do not represent society's wealth.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #2
Difficulty: Basic

3. The stage an individual is in his/her life cycle will affect his/her _____.
- A. return requirements
 - B. risk tolerance
 - C. asset allocation
 - D. **a and b**
 - E.** **a, b, and c**

See section on 'Individuals and Financial Objectives'

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #3
Difficulty: Moderate

4. Investment objectives

- A. must be consistent with investment constraints.
- B. must be in direct contrast with investment constraints.
- C. and investment constraints determine investment policies.
- D. **a** and **b**.
- E. **a** and **c**.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #4
Difficulty: Basic

5. _____ real asset(s).

- A. Land is a
- B. Machines are
- C. Both stocks and bonds are
- D. Knowledge is a
- E. Land, machines and knowledge are

Land, machines and knowledge are real assets; stocks and bonds are financial assets.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #5
Difficulty: Basic

6. _____ financial asset(s).

- A. Buildings are
- B. Land is a
- C. Derivatives are
- D. Canadian government bonds are
- E. Both derivatives and Canadian government bonds are

Buildings and land are real assets.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #6
Difficulty: Basic

7. Investors seeking to diversify are likely to find that their largest investment is in

- A. stocks.
- B. bonds.
- C. their job.
- D. foreign securities.
- E. cash.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #7
Difficulty: Moderate

8. _____ of an investment bank.

- A. BMO Nesbitt is an example
- B. CIBC is an example
- C. Scotia Capital is an example
- D. **a** and **b** are examples
- E. **a** and **c** are examples

See section on 'Investment Banking and Brokerage Services' in text.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #8
Difficulty: Basic

9. _____ are financial assets.

- A. Bonds
- B. Machines
- C. Stocks
- D. **a** and **c**
- E. **a**, **b** and **c**

Machines are real assets; stocks and bonds are financial assets.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #9
Difficulty: Basic

10. An example of a derivative security is _____.

- A. a common share of Canadian Pacific
- B. a call option on BMO stock
- C. a commodity futures contract
- D. **b** and **c**
- E. **a** and **b**

The values of **b** and **c** are derived from that of an underlying financial asset; the value of **a** is based on the value of the firm only.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #10
Difficulty: Basic

11. _____ was the first to introduce mortgage pass-through securities in Canada.

- A.** CMHC
- B. TD Bank
- C. FNMA
- D. GNMA
- E. None of these

See section on 'Financial Engineering'.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #11
Difficulty: Basic

12. A bond issue is broken up so that some investors will receive only interest payments while others will receive only principal payments, which is an example of _____.

- A. bundling
- B. securitization
- C. unbundling
- D. financial engineering
- E. c and d**

Unbundling is one of many examples of financial engineering that offer more alternatives to the investor.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #12
Difficulty: Basic

13. An example of a primitive security is _____.

- A. a common share of RBC
- B. a call option on CIBC stock
- C. a call option on a stock of a firm based in a Third World country
- D. a Canada bond
- E. a and d.**

A primitive security's return is based only upon the earning power of the issuing agency, such as stock in Inco and the Canadian government.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #13
Difficulty: Basic

14. The _____ refers to the potential conflict between management and shareholders due to management's control of pecuniary rewards as well as the possibility of incompetent performance by managers.

- A. agency problem
- B. diversification problem
- C. liquidity problem
- D. solvency problem
- E. regulatory problem

The agency problem describes potential conflict between management and shareholders. The other problems identified above are those of firm management only.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #14
Difficulty: Basic*

15. _____ financial asset(s).

- A. Buildings are
- B. Land is a
- C. Derivatives are
- D. EDC bonds are
- E. c and d

Land and buildings are real assets.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #15
Difficulty: Basic*

16. The value of a derivative security _____.

- A. depends on the value of the related primitive security
- B. can only cause increased risk.
- C. is unrelated to the value of the related primitive security
- D. has been enhanced due the recent misuse and negative publicity regarding these instruments
- E. is worthless today

Of the factors cited above, only **a** affects the value of the derivative and/or is a true statement.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #16
Difficulty: Basic*

17. _____ are indirect way through which U.S. investors can invest in foreign companies.

- A. ADRs
- B. RRSPs
- C. SDRs
- D. GNMAAs
- E. Krugerrands

Only ADRs represent an indirect investment in a foreign company.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #17
Difficulty: Basic

18. _____ are examples of financial intermediaries.

- A. Chartered banks
- B. Insurance companies
- C. Investment companies
- D. Credit unions
- E. All of these

All are financial institutions that bring borrowers and lenders together.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #18
Difficulty: Basic

19. Financial intermediaries exist because small investors cannot efficiently _____.

- A. diversify their portfolios
- B. gather information
- C. monitor their portfolios
- D. advertise for needed investments
- E. all of these.

The individual investor cannot efficiently and effectively perform any of the tasks above without more time and knowledge than that available to most individual investors.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #19
Difficulty: Basic

20. Financial intermediaries differ from other businesses in that both their assets and their liabilities are mostly

- A. illiquid.
- B. owned by government.
- C. real.
- D. financial.**
- E. regulated.

Financial intermediaries sell their liabilities to raise funds that are used to purchase liabilities of other corporations. Therefore, both their assets and liabilities are mostly financial.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #20
Difficulty: Basic*

21. Firms that specialize in helping companies raise capital by selling securities are called _____.

- A. chartered banks
- B. investment banks**
- C. trust companies
- D. credit unions
- E. all of these.

An important role of investment banks is to act as middle men in helping firms place new issues in the market.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #21
Difficulty: Basic*

22. In what roles do investment bankers perform?

- A. design securities with desirable properties
- B. market new stock and bond issues for firms
- C. provide advice to the firms as to market conditions, price, etc.
- D. none of these
- E. all of these**

All these are roles performed by investment banks as described in the "Financial intermediaries" section.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #22
Difficulty: Basic*

23. Financial assets _____.

- A. directly contribute to the country's productive capacity
- B. indirectly contribute to the country's productive capacity**
- C. contribute to the country's productive capacity both directly and indirectly
- D. do not contribute to the country's productive capacity either directly or indirectly
- E. are of no value to anyone

Financial assets indirectly contribute to the country's productive capacity because these assets permit individuals to invest in firms and governments. This in turn allows firms and governments to increase productive capacity.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #23
Difficulty: Basic

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

- A. call options
- B. securitization**
- C. unbundling
- D. derivatives
- E. none of these

The financial asset is secured by the mortgages backing the instrument.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #24
Difficulty: Basic

25. Corporate shareholders are best protected from incompetent management decisions by

- A. the ability to engage in proxy fights.
- B. management's control of pecuniary rewards.
- C. the ability to call shareholder meetings.
- D. the threat of takeover by other firms.**
- E. one-share/one-vote election rules.

Proxy fights are expensive and seldom successful, and management may often control the board or own significant shares. It is the threat of takeover of underperforming firms that has the strongest ability to keep management on their toes.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #25
Difficulty: Moderate

26. Theoretically, takeovers should result in _____.

- A. improved management
- B. increased stock price
- C. increased benefits to existing management of taken over firm
- D. a and b**
- E. a, b, and c

Theoretically, when firms are taken over, better managers come in and thus increase the price of the stock; existing management often must either leave the firm, be demoted, or suffer a loss of existing benefits.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #26
Difficulty: Basic

27. Collateralized mortgage obligations were created to

- A. aggregate individual mortgages into relatively homogeneous pools.
- B. meet the demand for mortgage-backed securities with a range of maturities.**
- C. rebundle separate branches into a single unit.
- D. circumvent the requirements of Regulation Q.
- E. provide government insurance for mortgages.

CMOs were created unbundling pools of mortgages to meet investor demand for mortgage-backed securities with a range of maturities.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #27
Difficulty: Basic

28. Derivative securities are

- A. potentially dangerous because they are highly leveraged
- B. an effective tool to better manage business returns and risk
- C. always structured as option contracts
- D. both a and b are true**
- E. all of these are true

Derivative securities were created to allow the transfer of risk from one party to another. They can be used to effectively reduce risk, or, because of leverage effects, to greatly increase risk.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #28
Difficulty: Moderate

29. Important trends changing the contemporary investment environment are

- A. globalization
- B. securitization
- C. bundling and unbundling
- D. financial engineering
- E. all of these**

All of these are examples of important trends in the contemporary investment environment.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #29
Difficulty: Basic*

30. The term "human capital" refers to

- A. the total amount of capital owned by humans.
- B. the value of the earnings potential of the workforce.**
- C. the value of a firm's management personnel.
- D. the value of a firm's blue-collar workers.
- E. the value of equipment that is operated by company personnel.

See section on "Individuals and Financial Objectives" in text

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #30
Difficulty: Basic*

31. What are the objectives of businesses issuing securities to the public?

- A. To get the best possible price for their securities.
- B. To market the issues to the public at the lowest cost.
- C. To issue fairly simple securities requiring little incremental analysis.
- D. All of these are true.**
- E. None of these is true.

Business-sector security issuers prefer simplicity and uniformity. This has created a demand for middlemen who transform simple securities into complex issues to suit particular market niches.

*Accessibility: Keyboard Navigation
Bodie - Chapter 01 #31
Difficulty: Basic*

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

- A. investment assets.
- B. depository assets.
- C. derivative assets
- D. financial assets.**
- E. exchange-driven assets

Financial assets allocate the wealth of the economy. Book example: it is easier for an individual to own shares of an auto company than to own an auto company directly.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #32
Difficulty: Basic

33. Which of the following are mechanisms that have evolved to mitigate potential agency problems?

- I. compensation in the form of the firm's stock options
 - II. hiring bickering family members as corporate spies
 - III. underperforming management teams being forced out by boards of directors
 - IV. security analysts monitoring the firm closely
 - V. takeover threats
- A. II and V
 - B. I, III, and IV
 - C. I, III, IV, and V**
 - D. III, IV, and V
 - E. I, III, and V

All but the second option have been used to try to limit agency problems.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #33
Difficulty: Moderate

34. Until 1999, the _____ Act(s) prohibited banks in the United States from both accepting deposits and underwriting securities.

- A. Sarbanes-Oxley
- B. Glass-Steagall**
- C. SEC
- D. Sarbanes-Oxley and SEC
- E. None of the options

Until 1999, the Glass-Steagall Act prohibited banks in the United States from both accepting deposits and underwriting securities.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #34
Difficulty: Basic

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

- A. attract customers.
- B. appease stockholders.
- C. offset debt.
- D. hedge.**
- E. enhance their balance sheets.

Firms may use forward contracts and futures to protect against currency fluctuations or changes in commodity prices. Interest-rate options help companies control financing costs.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #35
Difficulty: Basic

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

- A. The Government of Canada
- B. EDC
- C. The Bank of Canada
- D. CMHC**
- E. EDC and CMHC

Mortgage-backed securities were created in the U.S. by FNMA and FHLMC, but later in Canada when CMHC began buying mortgage loans and bundling them into large pools that could be traded like any other financial asset.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #36
Difficulty: Basic

37. 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 continue to service them.

- A. II, III, and IV
- B. I, II, and IV**
- C. II and IV
- D. I, III, and IV
- E. I, II, III, and IV

III is not correct because the bank no longer owns the mortgage investments.

Accessibility: Keyboard Navigation
Bodie - Chapter 01 #37
Difficulty: Moderate

38. Discuss the agency problem in detail.

Managers are the agents of the shareholders, and should act on their behalf to maximize shareholder wealth (the value of the stock). A conflict (the agency conflict) arises when managers take self-interested actions to the detriment of shareholders. The roles of the board of directors selected by the shareholders are to oversee management and to minimize agency problems. However, often these boards are figureheads, and individual shareholders do not own large enough blocks of the shares to override management actions. One potential resolution of an agency problem occurs when inefficient management actions cause the price of the stock to be depressed. The firm may then become a takeover target. If the acquisition is successful, managers may be replaced and potentially, stockholders benefit.

Feedback: The question is designed to ascertain that the student understands the corporate relationship between shareholders, management, and the board of directors. In addition, this problem has been addressed extensively in recent years, both in the popular financial press during the mergers and acquisitions mania of the 1980s, and in the academic literature as agency theory.

*Bodie - Chapter 01 #38
Difficulty: Moderate*

39. Discuss the various types of securities markets. Distinguish between initial sale of the assets and subsequent sales. Also distinguish between the middlemen in the different markets.

Real assets represent the productive capacity of the firm, and appear as assets on the firm's balance sheet. Financial assets are claims against the firm, and thus appear as liabilities on the firm's balance sheet. On the other hand, financial assets are listed on the asset side of the balance sheet of the individuals who own them. Thus, when financial statements are aggregated across the economy, the financial assets cancel out, leaving only the real assets, which directly contribute to the productive capacity of the economy. Financial assets contribute indirectly only.

Feedback: The purpose of this question is to ascertain if the student understands the difference between real and financial assets, both in the aggregate balance sheet context and the relative contribution of the two types of assets to the productive capacity of the economy.

*Bodie - Chapter 01 #39
Difficulty: Moderate*

40. Discuss the euro in relation to its impact on globalization. How is it currently used and what are the plans for its future use?

The euro was introduced in 1999 as a new currency for eleven European countries and it is used with the countries' own currencies for the time being. The goal is for the euro to replace the currencies so there will be one common European currency in the participating countries. A common currency is expected to facilitate global trade and encourage the integration of markets across national boundaries.

Feedback: The introduction of the Euro was discussed in the section on Globalization. Students should be aware of the existence and purpose of the Euro and how it is used in international finance. They should also appreciate its current centrality to world finance and also European politics.

*Bodie - Chapter 01 #40
Difficulty: Moderate*

41. Discuss the similarities and differences between real and financial assets.

Real assets represent the productive capacity of the firm and appear as assets on the firm's balance sheet. Financial assets are claims against the firm and thus appear as liabilities on the firm's balance sheet. On the other hand, financial assets are listed on the asset side of the balance sheet of the individuals who own them. Thus, when financial statements are aggregated across the economy, the financial assets cancel out, leaving only the real assets, which directly contribute to the productive capacity of the economy. Financial assets contribute indirectly only.

Feedback: The purpose of this question is to ascertain if the student understands the difference between real and financial assets, both in the aggregate balance sheet context and the relative contribution of the two types of assets to the productive capacity of the economy.

*Bodie - Chapter 01 #41
Difficulty: Moderate*

42. Discuss securitization as it relates to the field of investments.

Securitization refers to aggregating underlying financial assets, such as mortgages, into pools and then offering a security that represents a claim on these underlying assets. An example is mortgage-backed securities. Securitization allows investors to hold partial ownership in financial assets that would otherwise be beyond their reach (e.g., mortgages).

Financial engineering involves bundling or unbundling. Bundling involves combining separate securities.

Feedback: The purpose of this question is to ascertain if the student understands the importance of securitization and the impact it has on the field of investments.

*Bodie - Chapter 01 #42
Difficulty: Moderate*

c1 Summary

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