

Towson University
Fin333.001
Mid-term Exam
Prof. Rhee
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Name: _____
ID#: _____

1. Real assets in the economy include all but which one of the following?

- A. Land
- B. Buildings
- C. Consumer durables
- D. Common stock
- E. Patents

Answer: D

D is a financial asset.

2. Which of the following is not a money market security?

- A. U.S. Treasury bill
- B. Six month maturity CD
- C. Common stock
- D. Banker's acceptance
- E. Commercial Paper

Answer: C

It is a capital market instrument with the maturity is longer than 1 year (in fact, indefinite at least theoretically)

3. Asset allocation refers to the _____.

- A. allocation of the investment portfolio across broad asset classes
- B. analysis of the value of securities
- C. choice of specific assets within each asset class
- D. bottom up method of investing
- E. none of the answers define asset allocation

Answer: A

4. Financial institutions that specialize in assisting corporations in primary market transactions are called?

- A. mutual funds
- B. investment bankers
- C. pension funds
- D. globalization specialists
- E. hedge funds

Answer: B

5. In recent years the greatest dollar amount of securitization occurred for which type loan?

- A. Home mortgages
- B. Credit card debt
- C. Automobile loans
- D. Equipment leasing
- E. Derivative products

Answer: A

6. The price quotations of treasury bonds in the Wall Street Journal show a bid price of 102:12 and an ask price of 102:14. If you sold the bond you expect to receive _____.

- A. \$1,024.75
- B. \$1,024.38
- C. \$1,023.75
- D. \$1,022.50
- E. \$1,021.40

Answer: C

Bid price = $102 + 12/32 = 102 + 0.375 = 102.375\%$ of \$1,000 $\Rightarrow 1023.75$

7. The Dow Jones Industrial Average is _____.

- A. a price weighted average
- B. a value weight and average
- C. an equally weighted average
- D. an unweighted average
- E. a geometric average

Answer: A

8. A bond issued by the State of Alabama is priced to yield 6.25%. If you are in the 28% tax bracket this bond would provide you with an equivalent taxable yield of _____.

- A. 4.50%
- B. 7.25%
- C. 8.68%
- D. 9.21%
- E. 10.03%

Answer: C

$6.25\% / (1 - 0.28) = 8.68\%$

9. June call and put options on King Books Inc are available with exercise prices of \$30, \$35 and \$40. Among the different exercise prices, the call option with the _____ exercise price and the put option with the _____ exercise price will have the greatest value.

- A. \$40; \$30
- B. \$30; \$40
- C. \$35; \$35
- D. \$40; \$40
- E. \$30; \$30

Answer: B

A call with a lower exercise price and a put with a higher exercise price are more valuable as you want to pay less and get paid more.

10. Barnegat Light sold 200,000 shares in an initial public offering. The underwriter's explicit fees were \$90,000. The offering price for the shares was \$35, but immediately upon issue, the share price jumped to \$43. What is the best estimate of the total cost to Barnegat Light of the equity issue?

- A. \$90,000
- B. \$1,290,000
- C. \$2,390,000
- D. \$1,690,000
- E. \$2,190,000

Answer: D

The total cost is comprised of the explicit fee and the under pricing = $\$90k + (\$43 - \$35) * 200,000$

11. The issue process where investors submit bids for a new issue and the shares in an IPO are allocated to the highest bidders until the entire issue is sold is called a

- A. best efforts offer
- B. Dutch auction
- C. secondary offering
- D. firm commitment offer
- E. private placement

Answer: B

12. If an investor places a _____ order the stock will be sold if its price falls to the stipulated level. If an investor places a _____ order the stock will be bought if its price falls to the stipulated level.

- A. stop-loss; stop-loss
- B. market; limit
- C. limit; limit
- D. limit; market
- E. stop-loss; limit

Answer: E

13. A (contingent) deferred sales charge is commonly called a _____.

- A. front-end load
- B. back-end load
- C. 12b-1 charge
- D. top end sales commission
- E. no load fund

Answer: B

14. _____ funds stand ready to redeem or issue shares at their net asset value.

- A. Closed-end
- B. Index
- C. Open-end
- D. Hedge
- E. Unit trust

Answer: C

15. The CAL provided by combinations of one month T-bills and a broad index of common stocks is called the _____.

- A. SML
- B. CAPM
- C. CML
- D. Total Return Line
- E. APT

Answer: C

16. Assume that you have recently purchased 100 shares in an investment company. Upon examining the balance sheet, you note the firm is reporting \$225 million in assets, \$30 million in liabilities, and 10 million shares outstanding. What is the Net Asset Value (NAV) of these shares?

$$(225-30)/10 = \$19.5$$

17. You short-sell 100 shares of ABC Inc. at \$40 per share. What is the total balance of your account if you just satisfy the 50% initial margin requirement? What will be the remaining margin in the account if the price rises to \$50 and the stock has a dividend of \$2 per share? Will you get a margin call if the MMR is 30%? If so, how much money should be added at minimum to be able to keep your short position?

sales proceed = $40 \times 100 = 4,000$. 50% initial margin = 2,000. The total (cash) balance of the account = 6,000. If the stock price rises to \$50, then the remaining margin in the account (including the dividend to be returned to the original owner of the stock shares) = $6,000 - 50 \times 100 - 2 \times 100 = \800 . Since the margin ratio = $800/5,000 = 16\%$, which is less than 30% MMR, you will get a margin call. If you get a margin call, you need to add additional equity to bring the margin ratio back to the initial margin requirement level of 50%. Since 50% of 5,000 = \$2,500 and you have \$800 margin (=equity) already in the account, you need to add \$1,700 ($2,500 - 800$) to be added to the account.

18. A risky portfolio pays 15% rate of return with a probability of 40% or 5% with a probability of 60%. A treasury bill pays 6%. What is the risk premium of the risky portfolio investment?

$$E(R) = .4 \times 15\% + .6 \times 5\% = 9\%. \text{ The risk premium} = 9\% - 6\% = 3\%$$

19. The holding period return on a stock was 32%. Its beginning price was \$25 and its cash dividend was \$1.50. What is its ending price?

$$HPR = (End - Beg + Income)/Beg = (E - 25 + 1.5)/25 = 0.32 \Rightarrow \text{Solving the equation for } E = 25 \times 0.32 + 23.5 = \$31.50$$

20. The return on the risky portfolio is 25%. The risk-free rate is 5%. The standard deviation of return on the risky portfolio is 20%. If the standard deviation on the complete portfolio is 15%, what is the expected return on the complete portfolio? Draw a diagram to indicate where the complete portfolio is located.

$\sigma_c = W_r \times \sigma_r \Rightarrow 15\% = W_r \times 20\% \Rightarrow W_r = 0.75$ and $W_f = 1 - W_r = 0.25$. Now, $E(R_c) = 0.75 \times 25\% + 0.25 \times 5\% = 20\%$. You can identify this point immediately on the CAL connecting f (0, 5%) and r (20%, 25%).

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