Overview of Equity Securities

PROBLEMS

1. Which of the following is *not* a characteristic of common equity?
   A. It represents an ownership interest in the company.
   B. Shareholders participate in the decision-making process.
   C. The company is obligated to make periodic dividend payments.
2. The type of equity voting right that grants one vote for each share of equity owned is referred to as:
   A. Proxy voting.
   B. Statutory voting.
   C. Cumulative voting.
3. All of the following are characteristics of preference shares *except*:
   A. They are either callable or putable.
   B. They generally do not have voting rights.
   C. They do not share in the operating performance of the company.
4. Participating preference shares entitle shareholders to:
   A. Participate in the decision-making process of the company.
   B. Convert their shares into a specified number of common shares.
   C. Receive an additional dividend if the company's profits exceed a predetermined level.
5. Which of the following statements about private equity securities is *incorrect*?
   A. They cannot be sold on secondary markets.
   B. They have market-determined quoted prices.
   C. They are primarily issued to institutional investors.
6. Venture capital investments:
   A. Can be publicly traded.
   B. Do not require a long-term commitment of funds.
   C. Provide mezzanine financing to early-stage companies.
7. Which of the following statements *most accurately* describes one difference between private and public equity firms?
   A. Private equity firms are focused more on short-term results than public firms.
   B. Private equity firms' regulatory and investor relations operations are less costly than those of public firms.
   C. Private equity firms are incentivized to be more open with investors about governance and compensation than public firms.
8. Emerging markets have benefited from recent trends in international markets. Which of the following has *not* been a benefit of these trends?
   A. Emerging market companies do not have to worry about a lack of liquidity in their home equity markets.
   B. Emerging market companies have found it easier to raise capital in the markets of developed countries.
   C. Emerging market companies have benefited from the stability of foreign exchange markets.

12. Calculate the total return on a share of equity using the following data:
Purchase price: $50
Sale price: $42
Dividend paid during holding period: $2

A. −12.0%
B. −14.3%
C. −16.0%

13. If a U.S.-based investor purchases a euro-denominated ETF and the euro subsequently depreciates in value relative to the dollar, the investor will have a total return that is:

A. Lower than the ETF's total return.
B. Higher than the ETF's total return.
C. The same as the ETF's total return.

14. Which of the following is *incorrect* about the risk of an equity security? The risk of an equity security is:

A. Based on the uncertainty of its cash flows.
B. Based on the uncertainty of its future price.
C. Measured using the standard deviation of its dividends.

15. From an investor's point of view, which of the following equity securities is the *least* risky?

A. Putable preference shares.
B. Callable preference shares.
C. Noncallable preference shares.

16. Which of the following is *least likely* to be a reason for a company to issue equity securities on the primary market?

A. To raise capital.
B. To increase liquidity.
C. To increase return on equity.

17. Which of the following is *not* a primary goal of raising equity capital?

A. To finance the purchase of long-lived assets.
B. To finance the company's revenue-generating activities.
C. To ensure that the company continues as a going concern.

18. Which of the following statements is *most accurate* in describing a company's book value?

A. Book value increases when a company retains its net income.
B. Book value is usually equal to the company's market value.
C. The ultimate goal of management is to maximize book value.

19. Calculate the book value of a company using the following information:

Number of shares outstanding	100,000
Price per share	€52
Total assets	€12,000,000
Total liabilities	€7,500,000
Net Income	€2,000,000

A. €4,500,000
B. €5,200,000
C. €6,500,000

20. Which of the following statements is *least accurate* in describing a company's market value?

A. Management's decisions do not influence the company's market value.
B. Increases in book value may not be reflected in the company's market value.
C. Market value reflects the collective and differing expectations of investors.

21. Calculate the 2009 return on equity (ROE) of a stable company using the following data:

Total sales	£2,500,000
Net income	£2,000,000
Beginning of year total assets	£50,000,000
Beginning of year total liabilities	£35,000,000
Number of shares outstanding at the end of 2009	1,000,000
Price per share at the end of 2009	£20

A. 10.0%
B. 13.3%
C. 16.7%

22. Holding all other factors constant, which of the following situations will *most likely* lead to an increase in a company's return on equity?

A. The market price of the company's shares increases.
B. Net income increases at a slower rate than shareholders' equity.
C. The company issues debt to repurchase outstanding shares of equity.

23. Which of the following measures is the *most difficult* to estimate?

A. The cost of debt.
B. The cost of equity.
C. Investors' required rate of return on debt.

24. A company's cost of equity is often used as a proxy for investors':

A. Average required rate of return.
B. Minimum required rate of return.
C. Maximum required rate of return.