

Equity Market

Multiple Choice Problems

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 puttable.
 - 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.

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. Puttable 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.