

Name _____ Section _____ ID # _____

AP/ADMS 3530 3.00 Finance

Midterm Exam – Fall 2016

Saturday October 22nd., 2016; 6:30pm – 9:00pm

Version “X”

Instructors and Sections

Kwok Ho	Section A, Fridays, 11:30am-2:30pm, SLH E Section E, Wednesdays, 11:30am-2:30pm, SLH E
Orlando Lopez	Section B, Tuesdays, 7pm-10 pm, SLH E
Irvin Pestano	Section D, Thursdays, 4pm -7pm, SLH E
Samuel Alagurajah	Section C, Wednesdays, 4pm-7pm, R N203 Section F, Tuesdays 4pm-7pm, VH C
Lois King	Section G, Internet (online)

This exam consists of 40 multiple choice questions and carries a total of 40 marks. Choose the response that best answers each question. Circle your answers below, and fill in your answers on the bubble sheet. *Only the bubble sheet is used to determine your exam score.* Please do not forget to write your name and ID # both at the top of this cover page and on the bubble sheet. Also please write the type of your exam (X or Y) on the bubble sheet.

Please note the following points:

- 1) **Read the questions carefully and use your time efficiently.**
- 2) Choose the answers that are **closest** to yours, because of possible rounding.
- 3) Keep at least **4** decimal places in your calculations and at least **2** in your final answers and at least **6** for the interest rates.
- 4) *Unless otherwise stated*, interest rates are **annual**, and bonds pay **semi-annual coupons** and have a face value (or par value) of **\$1,000**.
- 5) You may use the back of the exam paper as your scrap paper.
- 6) Instructors and invigilators will not answer questions during the exam.

CONCEPTUAL QUESTIONS

28. An investor who purchases stock in a firm cannot realize a positive return on that investment if the firm pays no dividends. This statement is:
- A) False. The investor will still receive interest payments from the investment
 - B) True. The investor does not receive any cash flows therefore, the investment return is zero
 - C) False. The investor may realize a capital gain from the appreciation of the stock price.
 - D) False: Firms have an obligation to pay investors dividends.
 - E) None of the above.

Solution: C

29. A bond which, at the option of the holder, can be swapped for a fixed number of shares of common stock at any time prior to the bond's maturity is called a _____ bond.
- A) Zero coupon
 - B) Callable C) Perpetual D) Convertible E) Junk

Solution: D

30. A stream of equal cash payments lasting forever with the first payment occurring at the end of the first year is termed as:
- A) a delayed annuity
 - B) a delayed perpetuity
 - C) an installment plan.
 - D) a regular perpetuity
 - E) an annuity due

Solution: D

31. Which one of the following will increase the present value of an annuity, other things equal?
- A) increasing the interest rate
 - B) decreasing the interest rate
 - C) decreasing the number of payments
 - D) decreasing the amount of the payment
 - E) increasing the inflation rate

Solution: B

32. If interest is paid m times per year, then the per-period interest rate equals the: A) effective annual rate divided by m .
B) compound interest rate multiplied by m . C) effective annual rate plus m
D) annual percentage rate divided by m .
E) annual percentage rate multiplied by m .

Solution: D - Example: if $m=12$, $i_m = APR/12$

33. Cash flows occurring in different periods should not be compared unless: A) interest rates are expected to be stable.
B) the cash flows occur no more than one year from each other. C) high rates of interest can be earned on the cash flows.
D) the cash flows have been discounted to a common date. E) the inflation rate is zero.

Solution: D

34. Corporations that annually retire a set portion of their long-term debt are said to be using:
A) indexed bonds. B) convertible debt. C) sinking funds.
D) secured debt. E) retractable funds

Solution C

35. A convertible bond can be described as
A) a combination of a bond and a preferred share
B) a combination of a bond and a warrant
C) a bond whose coupon floats with inflation
D) a bond whose coupon is converted into another currency
E) a bond which can be converted to cash by the holder

Solution: B

36. Common stocks can be valued using the perpetuity valuation formula if the: A) Discount rate is expected to grow at a constant rate
B) Dividends are not expected to grow but will remain the same amount
C) Growth rate in dividends is not constant
D) Investor does not intend to sell the stock
E) Discount rate is higher than the growth rate

Solution: B (e.g. If dividends are the same amount, the formula $P_0 = DIV/r$ can be used)

37. A takeover attempt in which outsiders compete with management for shareholders' votes is called:
- A) a proxy contest
 - B) a sinking boat meeting
 - C) a governance contest
 - D) a widely-held contest
 - E) a vulture meeting

Solution: A

38. Agency theory best addresses which of the following....
- A) The potential conflict between shareholders of company A & company B if company A were to attempt to take over company B.
 - B) The potential conflict between management and suppliers to the company who have not delivered on their contractual obligation.
 - C) The potential conflict between a corporation and government due to the regulations that a corporation has to follow.
 - D) The potential conflict between shareholders and management as they may have conflicting objectives for the corporation.
 - E) The potential conflict between shareholders and government over laws that restrict a company's ability to maximize shareholder wealth.

Solution: D

39. If the rate of interest increases, which of the following statement is false?
- A) Future value will increase.
 - B) Future value of an annuity due will increase.
 - C) Present value of a growth annuity will increase.
 - D) Future value of a growth annuity will increase.
 - E) Present value of perpetuity will decrease.

Solution: C

40. Which of the following is a false statement?
- A) Effective Annual Rate depends on how long you hold an investment.
 - B) Future value of your investment increases with APR.
 - C) On biweekly compounded loans, the EAR will exceed the APR.
 - D) The real rate of interest can be positive or negative.
 - E) The nominal rate of interest can be positive or negative

Solution: A