1. Which of the following events would make it more likely that a company would choose to call its outstanding callable bonds?
    a. A reduction in market interest rates.
    b. The company's bonds are downgraded.
    c. An increase in the call premium.
    d. Answers a and b are both correct.
    e. Answers a, b, and c are all correct.

2. Of the following provisions that might be found in a bond indenture, which would tend to *reduce* the coupon interest rate on the bond in question?
    a. A subordination clause in a debenture.
    b. A call provision.
    c. A convertible feature.
    d. Having relatively few restrictive covenants.
    e. All of the above.

3. The terms and conditions to which a bond is subject are set forth in its
    a. Debenture.
    b. Underwriting agreement.
    c. Indenture.
    d. Restrictive covenants.
    e. Call provision.

4. Common equity refers to the sum of which of the following balance sheet accounts?
    a. Common stock and retained earnings
    b. Book value, retained earnings, and common stock
    c. Common stock, additional paid-in capital, retained earnings
    d. Either answer a or c above could be correct depending on whether the firm has "par" or "no par" stock.
    e. Both b and c are correct since additional paid-in capital is equivalent to book value.

5. An option which gives the holder the right to sell a stock at a specified price at some time in the future is called a(n)
    a. Call option.
    b. Put option.
    c. Out-of-the-money option.
    d. Naked option.
    e. Covered option.

6. Your Aunt Agatha purchased a call option a few months ago. Today is the expiration date, so she must decide whether to exercise the option. Which of the following statements is correct? Do not consider brokers' commissions in your answer.
    a. Aunt Agatha doesn't need to make a decision about exercising the option today; in fact, it would be better if she waited until after the option expires.

b. Aunt Agatha should exercise the option if the price of the stock is less than the exercise, or strike, price.
c. Aunt Agatha should exercise the option if the price of the stock is greater than the exercise, or strike, price.
d. Aunt Agatha should exercise the option, regardless of the current stock price.
e. None of the above.

8. Which of the following are generally considered advantages of term loans over publicly issued bonds?
a. Lower flotation costs.
b. Speed, or how long it takes to bring the issue to market.
c. Flexibility, or the ability to adjust the bond's terms after it has been issued.
d. All of the above.
e. Only answers b and c above.

9. Eurodebt is the term used to designate
a. Debt sold by a foreign borrower that is denominated in the currency of the country where it is sold.
b. European bank loans that are denominated in the new Euro currency.
c. Debt that is denominated in a currency that is different than the currency of the country in which it is sold.
d. Equity instruments of one country that are sold in another country.
e. The certificates that represent ownership in foreign companies that are sold in the United States.

10. An American Depository Receipt (ADR) represents
a. Debt sold by a foreign borrower that is denominated in the currency of the country where it is sold.
b. Stock of foreign companies that is sold directly to investors in the United States.
c. Equity instruments of one country that are sold in another country.
d. The certificates that represent ownership in foreign companies that are sold in the United States.
e. Certificates representing ownership in stocks of foreign companies that are held in trust by a bank located in the country the stock is traded.

11. Assume the securities are all issued by the same firm. From the *investor's* standpoint, rank the following securities in order of increasing risk (the number of the least risky security is placed first, or to the left, in the answer set).

(1) Preferred stock.
(2) Income bonds.
(3) Convertible preferred stock.
(4) Mortgage bonds.

a. 1, 2, 3, 4
b. 4, 1, 2, 3
c. 4, 1, 3, 2
d. 4, 2, 1, 3
e. 4, 2, 3, 1

12. The sale of new common stock at a price greater than par value will affect which balance sheet accounts? (Choose the most complete answer.)

a. Common stock, paid-in capital, retained earnings.
b. Assets, common stock, paid-in capital.
c. Liabilities, common equity.
d. Common stock, retained earnings.
e. Common stock, paid-in capital.

13. Rollincoast Incorporated issued BBB bonds two years ago that provided a yield to maturity of 11.5 percent. Long-term risk-free government bonds were yielding 8.7 percent at that time. The current risk premium on BBB bonds versus government bonds is half what it was two years ago. If the risk-free long-term governments are currently yielding 7.8 percent, then at what rate should Rollincoast expect to issue new bonds?
a. 7.8%
b. 8.7%
c. 9.2%
d. 10.2%
e. 12.9%

14. B & O Railroad's convertible debentures were issued at their $1,000 par value in 2008. At any time prior to maturity on February 1, 2028, a debenture holder can exchange a bond for 25 shares of common stock. What is the conversion price, $P_c$?
a. $25
b. $1,000
c. $40
d. $1,025
e. $50

15. An investor purchased a call option that allows her to purchase 100 shares of Dell Computer common stock for $45 per share any time during the next six months. The price she paid for the option was $2.50 per share, or $250 total, and the current market price of Dell's stock is $42.50. If the price of Dell increases to $50 and the investor decides to exercise it, what will be the gain or loss that results from the option position that was held? Ignore taxes and commissions.
a. $500 gain
b. $250 loss
c. $750 gain
d. $250 gain
e. None of the above.

16. Sharon has a convertible bond with a face value of $1,000 that can be converted into 40 shares of common stock of Mountain Ice Corporation. If the current price of the stock is $20, what is the conversion price of the bond?
a. $20
b. $50
c. $800
d. $500
e. None of the above.

17. A(n) ____ is generally obtained from a bank or insurance company and the borrower agrees to make a series of payments consisting of interest and principal.
    a. putable bond
    b. bankers acceptance
    c. income bond
    d. term loan
    e. certificate of deposit

18. A(n) ____ is a bond that pays no annual interest but is sold at a discount below par, thus providing compensation to investors in the form of capital appreciation.
    a. coupon bond
    b. income bond
    c. convertible bond
    d. zero coupon bond
    e. callable bond

19. Which of the following is **NOT** a type of debt?
    a. commercial paper
    b. certificate of deposit
    c. term loan
    d. preferred stock

20. Bond ratings of ____ and higher are considered investment grade.
    a. AAA
    b. AA
    c. A
    d. BBB