Question #1 of 42

Question ID: 1458036

Nelson, Inc. has fixed financing costs of $3 million, fixed operating costs of $5 million, and variable costs of $2.00 per unit. If the price of Nelson's product is $4.00, Nelson's operating breakeven quantity of sales is:

A) 1.0 million units.

B) 2.5 million units.

C) 4.0 million units.

Question #2 of 42

Question ID: 1458010

As financial leverage increases, what will be the impact on the expected rate of return and financial risk?

A) Both will rise.

B) One will rise while the other falls.

C) Both will fall.

Question #3 of 42

Question ID: 1458031

Jayco, Inc., sells blue ink for $4.00 a bottle. The ink's variable cost per bottle is $2.00. Ink has fixed cost of $10,000. What is Jayco's breakeven point in units?

A) 6,000.

B) 5,000.

C) 2,500.

Question #4 of 42

Question ID: 1462865

With sales of $45 million, the operating earnings of Poston Industries are $3.8 million. Fixed operating costs are $4.2 million, net profit margin is 4.5%, and unit variable costs are $35.50. At the current level of sales, Poston's degree of operating leverage is *closest* to:

A) 1.2.

B) 1.6.

C) 2.1.

Question #5 of 42

Question ID: 1458019

FCO, Inc. (FCO) is comparing EBIT forecasts to help determine the impact its capital structure has on net income.

	Expected EBIT	EBIT + 10%
EBIT	$80,000	$88,000
Interest expense	15,000	15,000
EBT	65,000	73,000
Taxes	26,000	29,200
Net income	39,000	43,800
Liabilities	200,000	
Shareholder equity	250,000	
Return on equity	15.60%	

FCO's degree of financial leverage is *closest* to:

A) 1.25.

B) 0.80.

C) 0.60.

Question #6 of 42

Question ID: 1462866

For a profitable company, issuing debt in order to retire common stock will *most likely*:

A) decrease both operating income and net income.

B) increase both the level and variability of return on equity.

C) increase both net income and return on equity.

Question #7 of 42

Question ID: 1457997

All else equal, a firm's business risk is higher when:

A) the firm has low operating leverage.

B) fixed costs are the highest portion of its expense.

C) variable costs are the highest portion of its expense.

Question #8 of 42

Question ID: 1458025

Which of the following statements regarding the impact of financial leverage on a company's net income and return on equity (ROE) is *most accurate*?

A) Using financial leverage increases the volatility of ROE for a level of volatility in operating income.

B) If a firm has a positive operating profit margin, using financial leverage will always increase ROE.

C) Increasing financial leverage increases both risk and potential return of existing bondholders.

Question #9 of 42

Question ID: 1458020

Given the following information on the annual operating results for ArtFrames, a producer of quality metal picture frames:

- Sales of $3,500,000.
- Variable costs at 45% of sales.
- Fixed costs of $1,050,000.
- Debt interest payments on $750,000 issued at par with an annual 9.0% coupon; market yield is currently 7.0%.

ArtFrames's degree of operating leverage (DOL) and degree of financial leverage (DFL) are *closest to*:

	DOL	DFL
A)	2.20	1.50
B)	2.20	1.08
C)	3.00	1.50

Question #10 of 42

Question ID: 1462869

In the last period, Foster Insold 20,000 units at $31 per unit. Fixed costs were $180,000 and variable costs were $310,000. In the current period, Foster sold 25,000 units. If Foster's variable cost per unit and fixed costs remained unchanged, it would report income for the current period of:

A) $130,500.

B) $157,000.

C) $207,500.

Question #11 of 42

Question ID: 1458013

The following information reflects the projected operating results for Opstalan, a catalog printer.

- Sales = $5.0 million.
- Variable Costs = 40% of sales.
- Fixed Costs = $1.0 million.
- Interest expense = $105,000.
- Tax Rate = 0.0%.

Opstalan's degree of total leverage (DTL) is *closest* to:

A) 1.41.

B) 2.58.

C) 1.59.

Question #12 of 42

Question ID: 1458018

Which of the following *best* describes a firm with low operating leverage? A large change in:

A) the number of units a firm produces and sells result in a similar change in the firm's earnings before interest and taxes.

B) earnings before interest and taxes result in a small change in net income.

C) sales result in a small change in net income.

Question #13 of 42

Question ID: 1458014

Stromburg Corporation's sales are $75,000,000. Fixed costs, including research and development, are $40,000,000, while variable costs amount to 30% of sales. Stromburg plans an expansion which will generate additional fixed costs of $15,000,000, decrease variable costs to 25% of sales, and permit sales to increase to $100,000,000. What is Stromburg's degree of operating leverage at the new projected sales level?

A) 3.50.

B) 3.75.

C) 4.20.

Question #14 of 42

Question ID: 1458030

Annual fixed costs at King Mattress amount to $325,000. The variable cost of raw materials and labor is $120 for the typical mattress. Sales prices for mattresses average $160. How many units must King Mattress sell to break even?

A) 8,125.

B) 2,708.

C) 40.

Question #15 of 42

Question ID: 1458028

Jayco, Inc. has a division that makes red ink for the accounting industry. The unit has fixed costs of $10,000 per month, and is expected to sell 40,000 bottles of ink per month. If the variable cost per bottle is $2.00 what price must the division charge in order to breakeven?

A) $2.25.

B) $2.50.

C) $2.75.

Question #16 of 42

Question ID: 1458027

Wanton's San Y'isidro Co. manufactures custom door knobs for international clients. Average Revenue is $35 per unit, variable costs are $15 per unit, and total costs are $200,000. If sales are 10,000 units, what is the firm's breakeven sales quantity?

A) 1,750 units.

B) 2,500 units.

C) 3,000 units.

Question #17 of 42

Question ID: 1462864

Business risk is *best* described as resulting from the combined effects of a firm's:

A) financial risk and sales risk.

B) sales risk and operating risk.

C) operating risk and financial risk.

Question #18 of 42

Question ID: 1458003

The two major types of risk affecting a firm are *best* described as:

A) business risk and collection risk.

B) business risk and financial risk.

C) financial risk and cash flow risk.

Question #19 of 42

Question ID: 1458006

Myron Jackson is a private equity fund manager specializing in distressed companies. His investment philosophy is based on the principle that capital structure problems can be fixed, but industry characteristics dictate business models. Jackson would *most likely* be interested in distressed firms with which of the following characteristics?

A) High financial risk and low operating risk.

B) High operating risk and low financial risk.

C) High operating risk and high financial risk.

Question #20 of 42

Question ID: 1458022

Additional debt should be used in the firm's capital structure if it increases:

A) firm earnings.

B) earnings per share.

C) the value of the firm.

Question #21 of 42

Question ID: 1458037

Steven's Bakery produces snack cakes and bread. Listed below are the operating costs for the snack cakes division and the bread division.

	Snack cakes	Bread
Price per package	$2.00	$2.50
Variable cost per package	$1.00	$1.30
Fixed operating costs	$25,000	$30,000
Fixed financing costs	$10,000	$10,000

Compared to the snack cakes division, the operating breakeven quantity for the bread division is:

A) less.

B) greater.

C) the same.

Question #22 of 42

Question ID: 1458001

Hughes Continental is assessing its business risk. Which of the following factors would *least likely* be considered in the analysis?

A) Debt-equity ratio.

B) Input price variability.

C) Unit sales levels.

Question #23 of 42

Question ID: 1458004

The additional risk a firm's common shareholders must bear when a firm uses fixed cost financing is *best* described as:

A) financial risk.

B) business risk.

C) operating risk.

Question #24 of 42

Question ID: 1457999

Variability in a firm's operating income is *most closely* related to its:

A) financial risk.

B) internal risk.

C) business risk.

Question #25 of 42

Question ID: 1458012

Which of the following statements about leverage is *most accurate*?

A) If the company has no debt outstanding, then its degree of total leverage equals its degree of operating leverage.

B) An increase in fixed costs (holding sales and variable costs constant) will reduce the company's degree of operating leverage.

C) A decrease in interest expense will increase the company's degree of total leverage.

Question #26 of 42

Question ID: 1458000

Which of the following factors is *least likely* to affect business risk?

A) Operating leverage.

B) Demand variability.

C) Interest rate variability.

Question #27 of 42

Question ID: 1458024

Which of the following is a key determinant of operating leverage?

A) Level and cost of debt.

B) The tradeoff between fixed and variable costs.

C) The competitive nature of the business.

Question #28 of 42

Question ID: 1458016

All else equal, which of the following statements about operating leverage is *least* accurate?

A) Firms with high operating leverage experience greater variance in operating income.

B) Lower operating leverage generally results in a higher expected rate of return.

C) Operating leverage reflects the tradeoff between variable costs and fixed costs.

Question #29 of 42

Question ID: 1458002

Which of the following sources of financing is *least likely* to increase a firm's financial risk?

A) Common equity.

B) Operating leases.

C) Fixed-rate debt.

Question #30 of 42

Question ID: 1458023

Financial leverage magnifies:

A) taxes.

B) earnings per share variability.

C) operating income variability.

Question #31 of 42

Question #31 of 42

Question ID: 1462867

Daley Company sells its output for $15 per unit. Daley's variable costs, including taxes, are $10 per unit and its breakeven quantity of sales is 30,000 units. Daley's annual fixed costs are $50,000 for interest and $100,000 for rent. If Daley sells 35,000 units in a year, its net income will be:

A) $25,000.

B) $15,000.

C) $35,000.

Question #32 of 42

Question ID: 1458029

Annah Korotkin is the sole proprietor of CoverMeUp, a business that designs and sews outdoor clothing for dogs. Each year, she rents a booth at the regional Pet Expo and sells only blankets. Korotkin views the Expo as primarily a marketing tool and is happy to breakeven (that is, cover her booth rental). For the last 3 years, she has sold exactly enough blankets to cover the $750 booth rental fee. This year, she decided to make all blankets for the Expo out of high-tech waterproof/breathable material that is more expensive to produce, but that she believes she can sell for a higher profit margin. Information on the two types of blankets is as follows:

Per Unit	Last Year's (Basic) Blanket	This Year's (New) Blanket
Sales Price	$25	$40
Variable Cost	$20	$33

Assuming that Korotkin remains most interested in covering the booth cost (which has increased to $840), how many more or fewer blankets (new style) does she need to sell to cover the booth cost? To cover this year's booth costs, Korotkin needs to sell:

A) 30 fewer blankets than last year.

B) 42 fewer blankets than last year.

C) 42 more blankets than last year.

Question #33 of 42

Question ID: 1457998

Which of the following statements about business risk and financial risk is *least accurate*?

A) Business risk is the riskiness of the company's assets if it uses no debt.

B) The greater a company's business risk, the higher its optimal debt ratio.

C) Factors that affect business risk are demand, sales price, and input price variability.

Question #34 of 42

Question ID: 1458035

Yangtze Delta High Technology produces multimedia-enabled wireless phones. The factory incurs rent, depreciation, salary, and other fixed costs totaling RMB 10 million per year. Also, the company incurs annual interest of RMB 3 million on debt. Each phone sold by Yangtze Delta sells for RMB 200. The variable cost per phone is RMB 150. Yangtze Delta's operating breakeven quantity of sales is *closest to*:

A) 65,000.

B) 260,000.

C) 200,000.

Question #35 of 42

Question ID: 1462870

Gordon Castparts has fixed operating costs of $1.2 million and fixed financing costs of $400,000. If the price per unit is $39 and variable costs are $22 per unit, Gordon's operating breakeven quantity of sales is *closest* to:

A) 54,500.

B) 70,600.

C) 94,100.

Question #36 of 42

Question ID: 1462863

Operating risk is *most likely* to increase as a result of:

A) an increase in fixed production costs.

B) an increase in sales risk.

C) increased variability of costs.

Question #37 of 42

Question ID: 1458005

Business risk is *most* accurately described as:

A) another term for sales risk.

B) another term for operating risk.

C) consisting of both sales risk and operating risk.

Question #38 of 42

Question ID: 1458017

An analyst has gathered the following expenditure information for three different firms, each of which has a sales level of $4 million.

Costs for firms under consideration (in millions)			
	Firm A	**Firm B**	**Firm C**
Variable Costs	$2.00	$2.60	$2.40
Fixed Costs	$1.00	$1.30	$1.40
Interest Expense	$0.20	$0.00	$0.20

Which firm has the *highest* degree of operating leverage (DOL)?

A) Firm B.

B) Firm A.

C) Firm C.

Question #39 of 42

Question ID: 1458015

Which of the following statements regarding leverage is *most accurate*?

A) A firm with low operating leverage has a small proportion of its total costs in fixed costs.

B) A firm with high business risk is more likely to increase its use of financial leverage than a firm with low business risk.

C) High levels of financial leverage increase business risk while high levels of operating leverage will decrease business risk.

Question #40 of 42

Question ID: 1462868

First Choice, Inc., sold 40,000 units during its most recent quarter; had fixed operating costs of $70,000, total variable costs of $140,000, and interest expense of $80,000; and charged a price of $7.75 per unit. First Choice's breakeven level of sales, based on these values, is *closest* to:

A) 16,500.

B) 28,000.

C) 35,000.

Question #41 of 42

Question ID: 1458009

During a period of expansion in the economy, compared to firms with lower operating leverage, earnings growth for firms with high operating leverage will be:

A) lower.

B) higher.

C) unaffected.

Question #42 of 42

Question ID: 1458011

If a 10% increase in sales causes earnings per share to increase from $1.00 to $1.50, and if the firm has no debt, then what is its degree of operating leverage?

A) 4.2.

B) 5.0.

C) 4.7.