Module 4 Quiz

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# Module 4 Quiz

12 questions

*1 point*

1. True or False: Valuing a firm using discounted cash flow techniques (i.e., the income approach) involves adding projected cash flows over a forecast period (such as 5 to 10 years into the future) to an estimated terminal value of the firm at the end of the forecast period and appropriately discounting both to reflect a value today.

* **True**
* False

*1 point*

1. Which of the following is NOT part of the formula for the required return for equity (assuming you are using a CAPM model)?

* **Beta of the stock**
* Market risk premium
* Risk-free rate
* Volatility of the stock

*1 point*

1. Suppose debt is 20% of a firm’s capital structure and equity is 80%. The required return on the firm’s debt is 5%, and the required return on the firm’s equity is 12%. Suppose there is zero corporate tax. What is the firm’s weighted average cost of capital (WACC)?

* 5%
* **5.6%**
* 8.5%
* 10%
* 10.6%
* 12%

*1 point*

1. True or False: Empirical research suggests that there is strong persistence in the earnings growth rates of U.S. firms.

* **True**
* False

*1 point*

1. An asset can have a high price-to-earnings ratio because:

* It is expected to have a high growth rate in cash flows.
* **It is viewed as having low risk (i.e., has a low discount rate).**
* Both are possible reasons for an asset having a high price-to-earnings ratio.
* Neither are possible reasons for an asset having a high price-to-earnings ratio.

*1 point*

1. Suppose an asset provides annual risk-free cash flows of $200 at the end of each year in perpetuity. The risk-free rate is 5%. What is the value of this perpetuity?

* $200
* $1,000
* **$2,000**
* $4,000
* $8,000
* $10,000
* $20,000

*1 point*

1. An increase in the financial or operating leverage of a firm should:

* Increase the CAPM beta of the firm’s stock
* **Have no effect on the CAPM beta of the firm’s stock**
* Decrease the CAPM beta of the firm’s stock

*1 point*

1. Market multiple techniques to value a firm:

* Use ratios like price-to-earnings or market-to-book from a competitor to value a firm
* Are useful to obtain an estimate of the potential market value of a private company before its initial public offering (IPO)
* **Are only as good as is the match between the firm to value and its comparison firm**
* Can result in biased valuation estimates if firms have different accounting conventions
* All of these responses are true.
* None of these responses are true.

*1 point*

1. True or False: The accounting deduction for depreciation represents actual cash flow leaving the firm.

* **True**
* False

*1 point*

1. Future liabilities or revenues tied to fixed quantities that are known in advance should be discounted at a:

* **Low discount rate**
* High discount rate

*1 point*

1. The stock betas of individual industries estimated over a five-year period are:

* **Positively related to what the industry betas were five years earlier, but not perfectly so (i.e., the betas change somewhat over time)**
* Exactly the same as those estimated five years earlier (i.e., don’t change over time)
* Unrelated to what the industry betas were five years earlier

*1 point*

1. Suppose an asset provides annual risk-free cash flows at the end of each year in perpetuity. The risk-free rate is 5%. The first cash flow is $200, and the cash flows grow at 4% per year. What is the value of this perpetuity?

* $200
* **$1,000**
* $2,000
* $4,000
* $8,000
* $10,000
* $20,000