# Module 1 Practice Quiz 1

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Correct

1 / 1 points

1. A merger was announced today in the financial press. According to financial analysts and investors, this merger will add significant value to the acquirer. What should happen to the acquirer's stock price in the first day after the merger announcement?

1. It should go down since announcement returns are typically negative for acquirers.
2. Nothing since the merger has not yet happened.
3. **It should go up since investors believe the merger will increase company value.**

**Correct Response**

Even though the merger hasn't happened, the stock price incorporates the market's expectation that the merger will increase value.

1. Nothing, the stock price is determined by future dividends and should not be affected by investors' reaction to a merger.

Correct

1 / 1 points

2. A company just announced quarterly earnings. The company's CFO expects earnings-per-share to decrease by 5% next year. However, the market reacted positively to the earnings announcement and the company's stock price increased. Which of the following statements is most likely to be true?

1. The company's CFO is probably lying about next year's EPS.
2. **Despite next year's decrease in EPS, the market's expectation about future cash flows went up, and this is the reason why stock prices increased.**

**Correct Response**

The news about EPS is certainly relevant, but stock prices depend on all future cash flows not just next year's EPS. The increase in stock prices means that future cash flows are expected to be higher.

1. The market's reaction to the announcement shows that the stock market is inefficient.
2. Next year's decrease in EPS is irrelevant, and thus, it is not surprising that stock prices went up.

Correct

1 / 1 points

3. U.S. multinationals keep a significant amount of cash in foreign countries because

1. **repatriating cash will increase taxes and thus reduce shareholder wealth.**

**Correct Response**

Since the U.S. corporate tax rate is high, bringing cash back to the U.S. will force the company to pay additional taxes and thus reduce shareholder wealth.

1. the U.S. government forbids the companies to bring the cash back into the U.S.
2. U.S. multinationals have no alternative use for these cash balances.
3. U.S. multinationals are poorly managed.

Correct

1 / 1 points

4. Which of the following is not an example of an agency problem?

1. The CFO manipulated last quarter earnings to increase earnings per share and thus increase her bonus (which is tied to an EPS target).
2. A divisional manager is using the company's airplane for personal reasons.
3. **A company decided to invest in a technology that is harmful to the environment.**

**Correct Response**

A company investing in a technology that is harmful to the environment is an example of a conflict between shareholder value and other stakeholders. Agency problems refer to conflicts between managers and shareholders.

1. The CEO decides to employ her son as a divisional manager without searching for alternatives in the labor market.