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Finance

268



Module 3 Honors Quiz

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1. Which of the following did Eugen von Böhm-Bawerk NOT believe caused the interest rate to be a small positive number?

1 / 1 point

- ☐ There are advantages to roundaboutness.
- ☐ People value money more today than they do in a year.
- ☒ Financial knowledge and expertise accumulates at a societal level at approximately this rate.
- ☐ This is approximately the rate of technological progress.



Correct

2. If you put \$1000 into an account with a 20% interest rate, how much money will you have at the end of the year if interest is compounded CONTINUOUSLY?

1 / 1 point

(When inputting your answer, enter your rounded answer without decimal precision and do not type in the \$ dollar sign)

1221

✓ Correct

3. Suppose that a consol has a promised payment of 6 pounds per 100 pounds notional. This consol is now traded at 150 pounds. What is the current yield to maturity of the consol?

1 / 1 point

- ☐ 1%
- ☐ 2%
- ☐ 3%
- ☒ 4%

✓ Correct

The yield to maturity of a consol is the coupon payment divided by the price of the security, that is $(6\%) \times 100 / 150 = 4\%$.

4. You observe that on today's yield curve, the one year rate is $R_1=6\%$ and the two year rate is $R_2=6.5\%$. What is the one year forward rate one year from now?

1 / 1 point

- ☐ 6%
- ☐ 6.5%
- ☒ 7%
- ☐ 5%

✓ Correct

$$(1+R_2)^2 / (1+R_1) - 1$$

5. A tech company can make a 3% real return on an investment. It can borrow funds to finance the investment at a nominal rate of 6% and the inflation rate is 1%. Hence:

1 / 1 point

- ☐ The investment will be profitable.
- ☒ The investment will be unprofitable.
- ☐ The real rate of interest is 2%.
- ☐ The real rate of interest is 3%.

✓ Correct

The real rate of interest is 5%. Since the company can only earn 3% in real terms, the project will be unprofitable.

be unprofitable.

6. If expected inflation is less than actual inflation, then wealth will be redistributed from:

1 / 1 point

- ☐ The government to consumers.
- ☐ The consumers to the government.
- ☒ Lenders to borrowers.
- ☐ Borrowers to lenders.

✓ **Correct**

More inflation than anticipated will decrease the value of debt in real terms, shifting wealth to borrowers.

7. The market capitalization of a company provides information on:

1 / 1 point

- ☐ The capital expenditures of the company.
- ☐ The pension benefits provided by the company.
- ☒ The value of a company.
- ☐ The industry the company operates in.

✓ **Correct**

8. Which of the following are true for stock splits ? (check all that apply)

1 / 1 point

- ☒ Market price per share is reduced after the split.

✓ **Correct**

- ☒ The total number of outstanding shares increases.

✓ **Correct**

- ☒ Proportional ownership is unchanged.

✓ **Correct**

☐ Retained earnings are changed.

9. A rationale for preferred stock:

1 / 1 point

- ☐ It lowers the cost of financing, as compared with debt issuance.
- ☐ The dividends associated with it are tax-deductible.
- ☒ It expands the capital base without diluting common equity.
- ☐ Its holder benefits from an increased ownership in the company.

✓ Correct

10. The Pecking Order Theory indicates that firms prefer _____ financing to _____ financing.

1 / 1 point

- ☐ stock; debt
- ☒ internal; external
- ☐ stock; retained earning
- ☐ flexible; risky

✓ Correct

11. If the company I invest in issues a stock dividend at 5%, the value of my original shares are _____ by a factor _____. I am _____ since I have an additional _____ of value in the new shares.

1 / 1 point

- ☐ lowered, $1/1.05$, worse off, $0.05/1.05$
- ☐ raised, $1.05/1$, worse off, $0.05/1.05$
- ☒ lowered, $1/1.05$, better off, $0.05/1.05$
- ☐ raised, $1.05/1$, better off, $0.05/1.05$

✓ Correct

12. Which one of the following statements is correct?

1 / 1 point

- ☐ Stock repurchases provide more income to shareholders compared to dividends.
- ☐ A cash dividend has no effect on the market value per share.
- ☐ A stock repurchase increases the market value per share.
- ☒ Stock repurchases are more tax advantageous than are cash dividends.

 **Correct**

13. A company whose stock is selling at a price-to-earnings (P/E) ratio that is greater than the P/E ratio of the market most likely has:

1 / 1 point

- ☐ An unpredictable future stream of earnings.
- ☐ A larger dividend yield compared to the dividend yield of an average traded firm within the market.
- ☐ An anticipated earnings growth rate which is less than that of the average traded firm within the market.
- ☒ A dividend yield which is smaller than that of an average traded firm within the market.

 **Correct**

14. What are the main implications of John Lintner's dividend model?

1 / 1 point

- ☐ A firm should always pay a dividend equal to its EPS (earnings per share).
- ☒ A firm has to strike a balance. It should pay a dividend to share some of its earnings with shareholders but its dividend should not be too high, because that might lead to a cut in the dividend in a following year, which leads to a negative reaction among shareholders.
- ☐ If the company's EPS is smaller than last year's dividend, the company should engage in share repurchases.
- ☐ A firm should never pay any dividends.

 **Correct**