

# ch3

Student: \_\_\_\_\_

1. The trading of stock that was previously issued takes place
  - A. in the secondary market.
  - B. in the primary market.
  - C. usually with the assistance of an investment banker.
  - D. A and B.
  - E. B and C.
  
2. A purchase of a new issue of stock takes place
  - A. in the secondary market.
  - B. in the primary market.
  - C. usually with the assistance of an investment banker.
  - D. A and B.
  - E. B and C.
  
3. Firms raise capital by issuing stock
  - A. in the secondary market.
  - B. in the primary market.
  - C. to unwary investors.
  - D. only on days when the market is up.
  - E. C and D.
  
4. The following statements regarding the specialist are **true**:
  - A. Specialists maintain a book listing outstanding unexecuted limit orders.
  - B. Specialists earn income from commissions and spreads in stock prices.
  - C. Specialists stand ready to trade at quoted bid and ask prices.
  - D. Specialists cannot trade in their own accounts.
  - E. A, B, and C are all true.
  
5. Investment bankers
  - A. act as intermediaries between issuers of stocks and investors.
  - B. act as advisors to companies in helping them analyze their financial needs and find buyers for newly issued securities.
  - C. accept deposits from savers and lend them out to companies.
  - D. A and B.
  - E. A, B, and C.
  
6. In a "firm commitment"
  - A. the investment banker buys the stock from the company and resells the issue to the public.
  - B. the investment banker agrees to help the firm sell the stock at a favorable price.
  - C. the investment banker finds the best marketing arrangement for the investment banking firm.
  - D. B and C.
  - E. A and B.

7. The secondary market consists of
- A. transactions on the AMEX.
  - B. transactions in the OTC market.
  - C. transactions through the investment banker.
  - D. A and B.
  - E. A, B, and C.
8. The use of the Internet to trade and underwrite securities
- A. is illegal under SEC regulations.
  - B. is regulated by the New York Stock Exchange.
  - C. decreases underwriting costs for a new security issue.
  - D. increases underwriting costs for a new security issue.
  - E. is regulated by the National Association of Securities Dealers.
9. Initial margin requirements are determined by
- A. the Securities and Exchange Commission.
  - B. the Federal Reserve System.
  - C. the New York Stock Exchange.
  - D. B and C.
  - E. A and B
10. You purchased JNJ stock at \$50 per share. The stock is currently selling at \$65. Your gains may be protected by placing a \_\_\_\_\_.
- A. stop-buy order
  - B. limit-buy order
  - C. market order
  - D. limit-sell order
  - E. none of the above.
11. You sold JCP stock short at \$80 per share. Your losses could be minimized by placing a \_\_\_\_\_.
- A. limit-sell order
  - B. limit-buy order
  - C. stop-buy order
  - D. day-order
  - E. none of the above
12. Which one of the following statements regarding orders is **false**?
- A. A market order is simply an order to buy or sell a stock immediately at the prevailing market price.
  - B. A limit sell order is where investors specify prices at which they are willing to sell a security.
  - C. If stock ABC is selling at \$50, a limit-buy order may instruct the broker to buy the stock if and when the share price falls below \$45.
  - D. A day order expires at the close of the trading day.
  - E. None of the above.

13. Restrictions on trading involving insider information apply to the following **except**
- A. corporate officers and directors.
  - B. relatives of corporate directors and officers.
  - C. major stockholders.
  - D. All of the above are subject to insider trading restrictions.
  - E. None of the above is subject to insider trading restrictions.
14. The cost of buying and selling a stock consists of \_\_\_\_\_.
- A. broker's commissions
  - B. dealer's bid-asked spread
  - C. a price concession an investor may be forced to make.
  - D. A and B.
  - E. A, B, and C.
15. Assume you purchased 200 shares of GE common stock on margin at \$70 per share from your broker. If the initial margin is 55%, how much did you borrow from the broker?
- A. \$6,000
  - B. \$4,000
  - C. \$7,700
  - D. \$7,000
  - E. \$6,300
16. You sold short 200 shares of common stock at \$60 per share. The initial margin is 60%. Your initial investment was
- A. \$4,800.
  - B. \$12,000.
  - C. \$5,600.
  - D. \$7,200.
  - E. none of the above.
17. You purchased 100 shares of IBM common stock on margin at \$70 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin.
- A. \$21
  - B. \$50
  - C. \$49
  - D. \$80
  - E. none of the above
18. You purchased 100 shares of common stock on margin at \$45 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$30? Ignore interest on margin.
- A. 0.33
  - B. 0.55
  - C. 0.43
  - D. 0.23
  - E. 0.25

19. You purchased 300 shares of common stock on margin for \$60 per share. The initial margin is 60% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$45 per share? Ignore interest on margin.
- A. 25%
  - B. -33%
  - C. 44%
  - D. -42%
  - E. -54%
20. Assume you sell short 100 shares of common stock at \$45 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$40/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. 20%
  - B. 25%
  - C. 22%
  - D. 77%
  - E. none of the above
21. You sold short 300 shares of common stock at \$55 per share. The initial margin is 60%. At what stock price would you receive a margin call if the maintenance margin is 35%?
- A. \$51
  - B. \$65
  - C. \$35
  - D. \$40
  - E. none of the above
22. Assume you sold short 100 shares of common stock at \$50 per share. The initial margin is 60%. What would be the maintenance margin if a margin call is made at a stock price of \$60?
- A. 40%
  - B. 33%
  - C. 35%
  - D. 25%
  - E. none of the above
23. Specialists on stock exchanges perform the following functions
- A. Act as dealers in their own accounts.
  - B. Analyze the securities in which they specialize.
  - C. Provide liquidity to the market.
  - D. A and B.
  - E. A and C.
24. Shares for short transactions
- A. are usually borrowed from other brokers.
  - B. are typically shares held by the short seller's broker in street name.
  - C. are borrowed from commercial banks.
  - D. B and C.
  - E. none of the above.

25. Which of the following orders is most useful to short sellers who want to limit their potential losses?
- A. Limit order
  - B. Discretionary order
  - C. Limit-loss order
  - D. Stop-buy order
  - E. None of the above
26. Which of the following orders instructs the broker to buy at the current market price?
- A. Limit order
  - B. Discretionary order
  - C. Limit-loss order
  - D. Stop-buy order
  - E. Market order
27. Which of the following orders instructs the broker to buy at or below a specified price?
- A. Limit-loss order
  - B. Discretionary order
  - C. Limit-buy order
  - D. Stop-buy order
  - E. Market order
28. Which of the following orders instructs the broker to sell at or below a specified price?
- A. Limit-sell order
  - B. Stop-loss
  - C. Limit-buy order
  - D. Stop-buy order
  - E. Market order
29. Which of the following orders instructs the broker to sell at or above a specified price?
- A. Limit-buy order
  - B. Discretionary order
  - C. Limit-sell order
  - D. Stop-buy order
  - E. Market order
30. Which of the following orders instructs the broker to buy at or above a specified price?
- A. Limit-buy order
  - B. Discretionary order
  - C. Limit-sell order
  - D. Stop-buy order
  - E. Market order

31. Shelf registration
- A. is a way of placing issues in the primary market.
  - B. allows firms to register securities for sale over a two-year period.
  - C. increases transaction costs to the issuing firm.
  - D. A and B.
  - E. A and C.
32. Block transactions are transactions for more than \_\_\_\_\_ shares and they account for about \_\_\_\_\_ percent of all trading on the NYSE.
- A. 1,000; 5
  - B. 500; 10
  - C. 100,000; 50
  - D. 10,000; 30
  - E. 5,000; 23
33. A program trade is
- A. a trade of 10,000 (or more) shares of a stock.
  - B. a trade of many shares of one stock for one other stock.
  - C. a trade of analytic programs between financial analysts.
  - D. a coordinated purchase or sale of an entire portfolio of stocks.
  - E. not feasible with current technology but is expected to be popular in the near future.
34. When stocks are held in street name
- A. the investor receives a stock certificate with the owner's street address.
  - B. the investor receives a stock certificate without the owner's street address.
  - C. the investor does not receive a stock certificate.
  - D. the broker holds the stock in the brokerage firms' name on behalf of the client.
  - E. C and D.
35. NASDAQ subscriber levels
- A. permit those with the highest level, 3, to "make a market" in the security.
  - B. permit those with a level 2 subscription to receive all bid and ask quotes, but not to enter their own quotes.
  - C. permit level 1 subscribers to receive general information about prices.
  - D. include all OTC stocks.
  - E. A, B, and C.
36. You want to buy 100 shares of Hotstock Inc. at the best possible price as quickly as possible. You would most likely place a
- A. stop-loss order
  - B. stop-buy order
  - C. market order
  - D. limit-sell order
  - E. limit-buy order

37. You want to purchase XON stock at \$60 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$3000 to invest, how many shares can you buy?
- A. 100 shares
  - B. 200 shares
  - C. 50 shares
  - D. 500 shares
  - E. 25 shares
38. A sale by IBM of new stock to the public would be a(n)
- A. short sale.
  - B. seasoned equity offering.
  - C. private placement.
  - D. secondary market transaction.
  - E. initial public offering.
39. The finalized registration statement for new securities approved by the SEC is called
- A. a red herring
  - B. the preliminary statement
  - C. the prospectus
  - D. a best-efforts agreement
  - E. a firm commitment
40. The minimum market value required for an initial listing on the New York Stock Exchange is
- A. \$2,000,000
  - B. \$2,500,000
  - C. \$1,100,000
  - D. \$60,000,000
  - E. 100,000,000
41. In 2005, the price of a seat on the NYSE reached a high of
- A. \$1,000,000
  - B. \$4,000,000
  - C. \$1,750,000
  - D. \$2,225,000
  - E. \$3,000,000
42. The floor broker is best described as
- A. an independent member of the exchange who owns a seat and handles overload work for commission brokers.
  - B. someone who makes a market in one or more securities.
  - C. a representative of a brokerage firm who is on the floor of the exchange to execute trade.
  - D. a frequent trader who performs no public function but executes trades for himself.
  - E. any counter party to a trade executed on the floor of the exchange.

43. You sell short 100 shares of Loser Co. at a market price of \$45 per share. Your maximum possible loss is
- A. \$4500
  - B. unlimited
  - C. zero
  - D. \$9000
  - E. cannot tell from the information given
44. You buy 300 shares of Qualitycorp for \$30 per share and deposit initial margin of 50%. The next day Qualitycorp's price drops to \$25 per share. What is your actual margin?
- A. 50%
  - B. 40%
  - C. 33%
  - D. 60%
  - E. 25%
45. When a firm markets new securities, a preliminary registration statement must be filed with
- A. the exchange on which the security will be listed.
  - B. the Securities and Exchange Commission.
  - C. the Federal Reserve.
  - D. all other companies in the same line of business.
  - E. the Federal Deposit Insurance Corporation.
46. In a typical underwriting arrangement the investment banking firm
- I) sells shares to the public via an underwriting syndicate.
  - II) purchases the securities from the issuing company.
  - III) assumes the full risk that the shares may not be sold at the offering price.
  - IV) agrees to help the firm sell the issue to the public but does not actually purchase the securities.
- A. I, II, and III
  - B. I, III, and IV
  - C. I and IV
  - D. II and III
  - E. I and II
47. Which of the following is **true** regarding private placements of primary security offerings?
- A. Extensive and costly registration statements are required by the SEC.
  - B. For very large issues, they are better suited than public offerings.
  - C. They trade in secondary markets.
  - D. The shares are sold directly to a small group of institutional or wealthy investors.
  - E. They have greater liquidity than public offerings.
48. A specialist on the AMEX Stock Exchange is offering to buy a security for \$37.50. A broker in Oklahoma City wants to sell the security for his client. The Intermarket Trading System shows a bid price of \$37.375 on the NYSE. What should the broker do?
- A. Route the order to the AMEX Stock Exchange.
  - B. Route the order to the NYSE.
  - C. Call the client to see if she has a preference.
  - D. Route half of the order to AMEX and the other half to the NYSE.
  - E. It doesn't matter - he should flip a coin and go with it.

49. You sold short 100 shares of common stock at \$45 per share. The initial margin is 50%. Your initial investment was
- A. \$4,800.
  - B. \$12,000.
  - C. \$2,250.
  - D. \$7,200.
  - E. none of the above.
50. You sold short 150 shares of common stock at \$27 per share. The initial margin is 45%. Your initial investment was
- A. \$4,800.60.
  - B. \$12,000.25.
  - C. \$2,250.75.
  - D. \$1,822.50.
  - E. none of the above.
51. You purchased 100 shares of XON common stock on margin at \$60 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin.
- A. \$42.86
  - B. \$50.75
  - C. \$49.67
  - D. \$80.34
  - E. none of the above
52. You purchased 1000 shares of CSCO common stock on margin at \$19 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin
- A. \$12.86
  - B. \$15.75
  - C. \$19.67
  - D. \$13.57
  - E. none of the above
53. You purchased 100 shares of common stock on margin at \$40 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$25? Ignore interest on margin.
- A. 0.33
  - B. 0.55
  - C. 0.20
  - D. 0.23
  - E. 0.25

54. You purchased 1000 shares of common stock on margin at \$30 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$24? Ignore interest on margin.
- A. 0.33
  - B. 0.375
  - C. 0.20
  - D. 0.23
  - E. 0.25
55. You purchased 100 shares of common stock on margin for \$50 per share. The initial margin is 50% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$56 per share? Ignore interest on margin.
- A. 28%
  - B. 33%
  - C. 14%
  - D. 42%
  - E. 24%
56. You purchased 100 shares of common stock on margin for \$35 per share. The initial margin is 50% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$42 per share? Ignore interest on margin.
- A. 28%
  - B. 33%
  - C. 14%
  - D. 40%
  - E. 24%
57. Assume you sell short 1000 shares of common stock at \$35 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$25/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. 20.47%
  - B. 25.63%
  - C. 57.14%
  - D. 77.23%
  - E. none of the above
58. Assume you sell short 100 shares of common stock at \$30 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$35/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. -33.33%
  - B. -25.63%
  - C. -57.14%
  - D. -77.23%
  - E. none of the above

59. You want to purchase GM stock at \$40 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$4000 to invest, how many shares can you buy?
- A. 100 shares
  - B. 200 shares
  - C. 50 shares
  - D. 500 shares
  - E. 25 shares
60. You want to purchase IBM stock at \$80 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$2000 to invest, how many shares can you buy?
- A. 100 shares
  - B. 200 shares
  - C. 50 shares
  - D. 500 shares
  - E. 25 shares
61. Assume you sold short 100 shares of common stock at \$40 per share. The initial margin is 50%. What would be the maintenance margin if a margin call is made at a stock price of \$50?
- A. 40%
  - B. 20%
  - C. 35%
  - D. 25%
  - E. none of the above
62. Assume you sold short 100 shares of common stock at \$70 per share. The initial margin is 50%. What would be the maintenance margin if a margin call is made at a stock price of \$85?
- A. 40.5%
  - B. 20.5%
  - C. 35.5%
  - D. 23.5%
  - E. none of the above
63. You sold short 100 shares of common stock at \$45 per share. The initial margin is 50%. At what stock price would you receive a margin call if the maintenance margin is 35%?
- A. \$50
  - B. \$65
  - C. \$35
  - D. \$40
  - E. none of the above
64. You sold short 100 shares of common stock at \$75 per share. The initial margin is 50%. At what stock price would you receive a margin call if the maintenance margin is 30%?
- A. \$90.23
  - B. \$88.52
  - C. \$86.54
  - D. \$87.12
  - E. none of the above

65. IPO average first-day returns are largest in \_\_\_\_\_.
- A. The United States
  - B. Denmark
  - C. Japan
  - D. China
  - E. France
66. Despite large first-day IPO returns, average first-year returns in the US are approximately \_\_\_\_\_ percent.
- A. 6.7
  - B. 18.2
  - C. 26.4
  - D. 4.8
  - E. 9.1
67. Average second-year IPO returns in the US are approximately \_\_\_\_\_ percent.
- A. 6.7
  - B. 18.2
  - C. 26.4
  - D. 5.3
  - E. 9.1
68. Average third-year IPO returns in the US are approximately \_\_\_\_\_ percent.
- A. 6.7
  - B. 18.2
  - C. 26.4
  - D. 5.3
  - E. 10.3
69. The preliminary prospectus is referred to as a \_\_\_\_\_.
- A. red herring
  - B. indenture
  - C. green mail
  - D. tombstone
  - E. headstone
70. The minimum revenue required for an initial listing on the New York Stock Exchange is
- A. \$2,000,000
  - B. \$25,000,000
  - C. \$50,000,000
  - D. \$75,000,000
  - E. 100,000,000

71. The minimum annual pretax income in the previous two years required for an initial listing on the New York Stock Exchange is
- A. \$2,000,000
  - B. \$25,000,000
  - C. \$50,000,000
  - D. \$75,000,000
  - E. 100,000,000
72. The daily dollar volume of trading on the NYSE in 2006 was approximately \_\_\_\_\_ dollars.
- A. \$75 billion
  - B. \$4 trillion
  - C. \$12 billion
  - D. \$4 billion
  - E. none of the above
73. The average daily number of shares traded on the NYSE in 2006 was approximately \_\_\_\_\_ dollars.
- A. 1.8 billion
  - B. 1.8 trillion
  - C. 12 billion
  - D. 4 trillion
  - E. none of the above
74. The \_\_\_\_\_ had the largest trading volume of securities in 2006.
- A. NASDAQ
  - B. NYSE
  - C. London
  - D. Tokyo
  - E. Hong Kong
75. The securities act of 1933 \_\_\_\_\_.
- I) requires full disclosure of relevant information relating to the issue of new securities
  - II) requires registration of new securities
  - III) requires issuance of a prospectus detailing financial prospects of the firm
  - IV) established the SEC
  - V) requires periodic disclosure of relevant financial information
  - VI) empowers SEC to regulate exchanges, OTC trading, brokers, and dealers
- A. I, II and III
  - B. I, II, III, IV, V, and VI
  - C. I, II and V
  - D. I, II and IV
  - E. IV only

76. The securities act of 1934 \_\_\_\_\_.
- I) requires full disclosure of relevant information relating to the issue of new securities
  - II) requires registration of new securities
  - III) requires issuance of a prospectus detailing financial prospects of the firm
  - IV) established the SEC
  - V) requires periodic disclosure of relevant financial information
  - VI) empowers SEC to regulate exchanges, OTC trading, brokers, and dealers
- A. I, II and III
  - B. I, II, III, IV, V, and VI
  - C. I, II and V
  - D. I, II and IV
  - E. IV, V, and VI
77. Which of the following is **not** required under the CFA Institute standards of professional conduct?
- A. knowledge of all applicable laws, rules and regulations
  - B. disclosure of all personal investments whether or not they may conflict with a client's investments
  - C. disclosure of all conflicts to clients and prospects
  - D. reasonable inquiry into a client's financial situation
  - E. All of the above are required under the CFA Institute standards.
78. According to the CFA Institute Standards of Professional Conduct, CFA Institute members have responsibilities to all of the following **except**:
- A. the government
  - B. the profession
  - C. the public
  - D. the employer
  - E. clients and prospective clients
79. Of the secondary stock markets, which have been expanding and which have been contracting? Give some of the reasons for the changes.
80. Discuss margin buying of common stocks. Include in your discussion the advantages and disadvantages, the types of margin requirements, how these requirements are met, and who determines these requirements.

81. List three factors that are listing requirements for the New York Stock Exchange. Why does the exchange have such requirements?

## ch3 Key

1. The trading of stock that was previously issued takes place

- A. in the secondary market.
- B. in the primary market.
- C. usually with the assistance of an investment banker.
- D. A and B.
- E. B and C.

Secondary market transactions consist of trades between investors.

*Bodie - Chapter 03 #1  
Difficulty: Easy*

2. A purchase of a new issue of stock takes place

- A. in the secondary market.
- B. in the primary market.
- C. usually with the assistance of an investment banker.
- D. A and B.
- E. B and C.

Funds from the sale of new issues flow to the issuing corporation, making this a primary market transaction. Investment bankers usually assist by pricing the issue and finding buyers.

*Bodie - Chapter 03 #2  
Difficulty: Easy*

3. Firms raise capital by issuing stock

- A. in the secondary market.
- B. in the primary market.
- C. to unwary investors.
- D. only on days when the market is up.
- E. C and D.

Funds from the sale of new issues flow to the issuing corporation, making this a primary market transaction.

*Bodie - Chapter 03 #3  
Difficulty: Easy*

4. The following statements regarding the specialist are **true**:
- A. Specialists maintain a book listing outstanding unexecuted limit orders.
  - B. Specialists earn income from commissions and spreads in stock prices.
  - C. Specialists stand ready to trade at quoted bid and ask prices.
  - D. Specialists cannot trade in their own accounts.
  - E.** A, B, and C are all true.

The specialists' functions are all of the items listed in A, B, and C. In addition, specialists trade in their own accounts.

*Bodie - Chapter 03 #4  
Difficulty: Moderate*

5. Investment bankers
- A. act as intermediaries between issuers of stocks and investors.
  - B. act as advisors to companies in helping them analyze their financial needs and find buyers for newly issued securities.
  - C. accept deposits from savers and lend them out to companies.
  - D.** A and B.
  - E. A, B, and C.

The role of the investment banker is to assist the firm in issuing new securities, both in advisory and marketing capacities. The investment banker does not have a role comparable to a commercial bank, as indicated in C.

*Bodie - Chapter 03 #5  
Difficulty: Moderate*

6. In a "firm commitment"
- A.** the investment banker buys the stock from the company and resells the issue to the public.
  - B. the investment banker agrees to help the firm sell the stock at a favorable price.
  - C. the investment banker finds the best marketing arrangement for the investment banking firm.
  - D. B and C.
  - E. A and B.

In a "firm commitment" the investment banker buys the stock from the company and resells the issue to the public.

*Bodie - Chapter 03 #6  
Difficulty: Moderate*

7. The secondary market consists of
- A. transactions on the AMEX.
  - B. transactions in the OTC market.
  - C. transactions through the investment banker.
  - D.** A and B.
  - E. A, B, and C.

The secondary market consists of transactions on the organized exchanges and in the OTC market. The investment banker is involved in the placement of new issues in the primary market.

*Bodie - Chapter 03 #7  
Difficulty: Moderate*

8. The use of the Internet to trade and underwrite securities
- A. is illegal under SEC regulations.
  - B. is regulated by the New York Stock Exchange.
  - C.** decreases underwriting costs for a new security issue.
  - D. increases underwriting costs for a new security issue.
  - E. is regulated by the National Association of Securities Dealers.

The SEC permits trading and underwriting of securities over the Internet, but has required firms participating in this activity to take steps to safeguard investment funds. This form of underwriting is expected to grow quickly due to its lower cost.

*Bodie - Chapter 03 #8  
Difficulty: Moderate*

9. Initial margin requirements are determined by
- A. the Securities and Exchange Commission.
  - B.** the Federal Reserve System.
  - C. the New York Stock Exchange.
  - D. B and C.
  - E. A and B

The Board of Governors of the Federal Reserve System determines initial margin requirements. The New York Stock Exchange determines maintenance margin requirements on NYSE-listed stocks; however, brokers usually set maintenance margin requirements above those established by the NYSE.

*Bodie - Chapter 03 #9  
Difficulty: Moderate*

10. You purchased JNJ stock at \$50 per share. The stock is currently selling at \$65. Your gains may be protected by placing a \_\_\_\_\_.
- A. stop-buy order
  - B. limit-buy order
  - C. market order
  - D. limit-sell order**
  - E. none of the above.

With a limit-sell order, your stock will be sold only at a specified price, or better. Thus, such an order would protect your gains. None of the other orders are applicable to this situation.

*Bodie - Chapter 03 #10  
Difficulty: Moderate*

11. You sold JCP stock short at \$80 per share. Your losses could be minimized by placing a \_\_\_\_\_.
- A. limit-sell order
  - B. limit-buy order
  - C. stop-buy order**
  - D. day-order
  - E. none of the above

With a stop-buy order, the stock would be purchased if the price increased to a specified level, thus limiting your loss. None of the other orders are applicable to this situation.

*Bodie - Chapter 03 #11  
Difficulty: Moderate*

12. Which one of the following statements regarding orders is **false**?
- A. A market order is simply an order to buy or sell a stock immediately at the prevailing market price.
  - B. A limit sell order is where investors specify prices at which they are willing to sell a security.
  - C. If stock ABC is selling at \$50, a limit-buy order may instruct the broker to buy the stock if and when the share price falls below \$45.
  - D. A day order expires at the close of the trading day.
  - E. None of the above.**

All of the order descriptions above are correct.

*Bodie - Chapter 03 #12  
Difficulty: Moderate*

13. Restrictions on trading involving insider information apply to the following **except**

- A. corporate officers and directors.
- B. relatives of corporate directors and officers.
- C. major stockholders.
- D.** All of the above are subject to insider trading restrictions.
- E. None of the above is subject to insider trading restrictions.

A, B, and C are corporate insiders and are subject to restrictions on trading on inside information. Further, the Supreme Court held that traders may not trade on nonpublic information even if they are not insiders.

*Bodie - Chapter 03 #13  
Difficulty: Moderate*

14. The cost of buying and selling a stock consists of \_\_\_\_\_.

- A. broker's commissions
- B. dealer's bid-asked spread
- C. a price concession an investor may be forced to make.
- D. A and B.
- E.** A, B, and C.

All of the above are possible costs of buying and selling a stock.

*Bodie - Chapter 03 #14  
Difficulty: Moderate*

15. Assume you purchased 200 shares of GE common stock on margin at \$70 per share from your broker. If the initial margin is 55%, how much did you borrow from the broker?

- A. \$6,000
- B. \$4,000
- C. \$7,700
- D. \$7,000
- E.** \$6,300

$200 \text{ shares} * \$70/\text{share} * (1-0.55) = \$14,000 * (0.45) = \$6,300.$

*Bodie - Chapter 03 #15  
Difficulty: Moderate*

16. You sold short 200 shares of common stock at \$60 per share. The initial margin is 60%. Your initial investment was
- A. \$4,800.
  - B. \$12,000.
  - C. \$5,600.
  - D. \$7,200.**
  - E. none of the above.

$$200 \text{ shares} * \$60/\text{share} * 0.60 = \$12,000 * 0.60 = \$7,200$$

*Bodie - Chapter 03 #16  
Difficulty: Moderate*

17. You purchased 100 shares of IBM common stock on margin at \$70 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin.
- A. \$21
  - B. \$50**
  - C. \$49
  - D. \$80
  - E. none of the above

$$100 \text{ shares} * \$70 * .5 = \$7,000 * 0.5 = \$3,500 \text{ (loan amount); } 0.30 = (100P - \$3,500)/100P; 30P = 100P - \$3,500; -70P = -\$3,500; P = \$50.$$

*Bodie - Chapter 03 #17  
Difficulty: Difficult*

18. You purchased 100 shares of common stock on margin at \$45 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$30? Ignore interest on margin.
- A. 0.33
  - B. 0.55
  - C. 0.43
  - D. 0.23
  - E. 0.25**

$$100 \text{ shares} * \$45/\text{share} * 0.5 = \$4,500 * 0.5 = \$2,250 \text{ (loan amount); } X = [100(\$30) - \$2,250]/100(\$30); X = 0.25.$$

*Bodie - Chapter 03 #18  
Difficulty: Difficult*

19. You purchased 300 shares of common stock on margin for \$60 per share. The initial margin is 60% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$45 per share? Ignore interest on margin.
- A. 25%
  - B. -33%
  - C. 44%
  - D. -42%**
  - E. -54%

$300(\$60)(0.60) = \$10,800$  investment;  $300(\$60) = \$18,000$  X  $(0.40) = \$7,200$  loan; Proceeds after selling stock and repaying loan:  $\$13,500 - \$7,200 = \$6,300$ ; Return =  $(\$6,300 - \$10,800)/\$10,800 = -41.67\%$ .

*Bodie - Chapter 03 #19  
Difficulty: Difficult*

20. Assume you sell short 100 shares of common stock at \$45 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$40/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. 20%
  - B. 25%
  - C. 22%**
  - D. 77%
  - E. none of the above

Profit on stock =  $(\$45 - \$40) * 100 = \$500$ ,  $\$500/\$2,250$  (initial investment) = 22.22%.

*Bodie - Chapter 03 #20  
Difficulty: Moderate*

21. You sold short 300 shares of common stock at \$55 per share. The initial margin is 60%. At what stock price would you receive a margin call if the maintenance margin is 35%?
- A. \$51
  - B. \$65**
  - C. \$35
  - D. \$40
  - E. none of the above

Equity =  $300(\$55) * 1.6 = \$26,400$ ;  $0.35 = (\$26,400 - 300P)/300P$ ;  $105P = 26,400 - 300P$ ;  $405P = 26,400$ ;  $P = \$65.18$

*Bodie - Chapter 03 #21  
Difficulty: Difficult*

22. Assume you sold short 100 shares of common stock at \$50 per share. The initial margin is 60%. What would be the maintenance margin if a margin call is made at a stock price of \$60?
- A. 40%
  - B. 33%**
  - C. 35%
  - D. 25%
  - E. none of the above

$$\$5,000 \times 1.6 = \$8,000; [\$8,000 - 100(\$60)]/100(\$60) = 33\%.$$

*Bodie - Chapter 03 #22  
Difficulty: Difficult*

23. Specialists on stock exchanges perform the following functions
- A. Act as dealers in their own accounts.
  - B. Analyze the securities in which they specialize.
  - C. Provide liquidity to the market.
  - D. A and B.
  - E. A and C.**

Specialists are both brokers and dealers and provide liquidity to the market; they are not analysts.

*Bodie - Chapter 03 #23  
Difficulty: Moderate*

24. Shares for short transactions
- A. are usually borrowed from other brokers.
  - B. are typically shares held by the short seller's broker in street name.**
  - C. are borrowed from commercial banks.
  - D. B and C.
  - E. none of the above.

Typically, the only source of shares for short transactions is those held by the short seller's broker in street name; often these are margined shares.

*Bodie - Chapter 03 #24  
Difficulty: Moderate*

25. Which of the following orders is most useful to short sellers who want to limit their potential losses?

- A. Limit order
- B. Discretionary order
- C. Limit-loss order
- D.** Stop-buy order
- E. None of the above

By issuing a stop-buy order, the short seller can limit potential losses by assuring that the stock will be purchased (and the short position closed) if the price increases to a certain level.

*Bodie - Chapter 03 #25  
Difficulty: Moderate*

26. Which of the following orders instructs the broker to buy at the current market price?

- A. Limit order
- B. Discretionary order
- C. Limit-loss order
- D. Stop-buy order
- E.** Market order

Market orders are to be executed immediately at the best prevailing price.

*Bodie - Chapter 03 #26  
Difficulty: Moderate*

27. Which of the following orders instructs the broker to buy at or below a specified price?

- A. Limit-loss order
- B. Discretionary order
- C.** Limit-buy order
- D. Stop-buy order
- E. Market order

Limit-buy orders are to be executed if the market price decreases to the specified limit price.

*Bodie - Chapter 03 #27  
Difficulty: Moderate*

28. Which of the following orders instructs the broker to sell at or below a specified price?

- A. Limit-sell order
- B.** Stop-loss
- C. Limit-buy order
- D. Stop-buy order
- E. Market order

Stop-loss orders are to be executed if the market price decreases to the specified limit price.

*Bodie - Chapter 03 #28  
Difficulty: Moderate*

29. Which of the following orders instructs the broker to sell at or above a specified price?

- A. Limit-buy order
- B. Discretionary order
- C.** Limit-sell order
- D. Stop-buy order
- E. Market order

Limit-sell orders are to be executed if the market price increases to the specified limit price.

*Bodie - Chapter 03 #29  
Difficulty: Moderate*

30. Which of the following orders instructs the broker to buy at or above a specified price?

- A. Limit-buy order
- B. Discretionary order
- C. Limit-sell order
- D.** Stop-buy order
- E. Market order

Stop-buy orders are to be executed if the market price increases to the specified limit price.

*Bodie - Chapter 03 #30  
Difficulty: Moderate*

31. Shelf registration

- A. is a way of placing issues in the primary market.
- B. allows firms to register securities for sale over a two-year period.
- C. increases transaction costs to the issuing firm.
- D.** A and B.
- E. A and C.

Shelf registration lowers transactions costs to the firm as the firm may register issues for a longer period than in the past, and thus requires the services of the investment banker less frequently.

*Bodie - Chapter 03 #31  
Difficulty: Easy*

32. Block transactions are transactions for more than \_\_\_\_\_ shares and they account for about \_\_\_\_\_ percent of all trading on the NYSE.
- A. 1,000; 5
  - B. 500; 10
  - C. 100,000; 50
  - D.** 10,000; 30
  - E. 5,000; 23

Block transactions are defined as trades of 10,000 or more shares and they account for 30 percent of NYSE trading.

*Bodie - Chapter 03 #32  
Difficulty: Moderate*

33. A program trade is
- A. a trade of 10,000 (or more) shares of a stock.
  - B. a trade of many shares of one stock for one other stock.
  - C. a trade of analytic programs between financial analysts.
  - D.** a coordinated purchase or sale of an entire portfolio of stocks.
  - E. not feasible with current technology but is expected to be popular in the near future.

Program trading is a coordinated purchase or sale of an entire portfolio of stocks.

*Bodie - Chapter 03 #33  
Difficulty: Moderate*

34. When stocks are held in street name
- A. the investor receives a stock certificate with the owner's street address.
  - B. the investor receives a stock certificate without the owner's street address.
  - C. the investor does not receive a stock certificate.
  - D.** the broker holds the stock in the brokerage firms' name on behalf of the client.
  - E. C and D.

When stocks are held in street name, the investor does not receive a stock certificate; the broker holds the stock in the brokerage firms' name on behalf of the client. This arrangement speeds transfer of securities.

*Bodie - Chapter 03 #34  
Difficulty: Moderate*

35. NASDAQ subscriber levels

- A. permit those with the highest level, 3, to "make a market" in the security.
- B. permit those with a level 2 subscription to receive all bid and ask quotes, but not to enter their own quotes.
- C. permit level 1 subscribers to receive general information about prices.
- D. include all OTC stocks.
- E.** A, B, and C.

NASDAQ links dealers in a loosely organized network with different levels of access to meet different needs.

*Bodie - Chapter 03 #35  
Difficulty: Easy*

36. You want to buy 100 shares of Hotstock Inc. at the best possible price as quickly as possible. You would most likely place a

- A. stop-loss order
- B. stop-buy order
- C.** market order
- D. limit-sell order
- E. limit-buy order

A market order is for immediate execution at the best possible price.

*Bodie - Chapter 03 #36  
Difficulty: Easy*

37. You want to purchase XON stock at \$60 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$3000 to invest, how many shares can you buy?

- A.** 100 shares
- B. 200 shares
- C. 50 shares
- D. 500 shares
- E. 25 shares

$$.5 = [(Q * \$60) - \$3,000] / (Q * \$60); \$30Q = \$60Q - \$3,000; \$30Q = \$3,000; Q = 100.$$

*Bodie - Chapter 03 #37  
Difficulty: Moderate*

38. A sale by IBM of new stock to the public would be a(n)
- A. short sale.
  - B.** seasoned equity offering.
  - C. private placement.
  - D. secondary market transaction.
  - E. initial public offering.

When a firm whose stock already trades in the secondary market issues new shares to the public this is referred to as a seasoned equity offering.

*Bodie - Chapter 03 #38  
Difficulty: Easy*

39. The finalized registration statement for new securities approved by the SEC is called
- A. a red herring
  - B. the preliminary statement
  - C.** the prospectus
  - D. a best-efforts agreement
  - E. a firm commitment

The prospectus is the finalized registration statement approved by the SEC.

*Bodie - Chapter 03 #39  
Difficulty: Moderate*

40. The minimum market value required for an initial listing on the New York Stock Exchange is
- A. \$2,000,000
  - B. \$2,500,000
  - C. \$1,100,000
  - D. \$60,000,000
  - E.** 100,000,000

See Table 3.2.

*Bodie - Chapter 03 #40  
Difficulty: Moderate*

41. In 2005, the price of a seat on the NYSE reached a high of
- A. \$1,000,000
  - B.** \$4,000,000
  - C. \$1,750,000
  - D. \$2,225,000
  - E. \$3,000,000

Seat prices have changed radically from \$4,000 in 1878 to \$4 million in 2005.

*Bodie - Chapter 03 #41  
Difficulty: Moderate*

42. The floor broker is best described as

- A.** an independent member of the exchange who owns a seat and handles overload work for commission brokers.
- B. someone who makes a market in one or more securities.
- C. a representative of a brokerage firm who is on the floor of the exchange to execute trade.
- D. a frequent trader who performs no public function but executes trades for himself.
- E. any counter party to a trade executed on the floor of the exchange.

The floor broker is an independent member of the exchange who handles work for commission brokers when they have too many orders to handle.

*Bodie - Chapter 03 #42  
Difficulty: Easy*

43. You sell short 100 shares of Loser Co. at a market price of \$45 per share. Your maximum possible loss is

- A. \$4500
- B.** unlimited
- C. zero
- D. \$9000
- E. cannot tell from the information given

A short seller loses money when the stock price rises. Since there is no upper limit on the stock price, the maximum theoretical loss is unlimited.

*Bodie - Chapter 03 #43  
Difficulty: Moderate*

44. You buy 300 shares of Qualitycorp for \$30 per share and deposit initial margin of 50%. The next day Qualitycorp's price drops to \$25 per share. What is your actual margin?

- A. 50%
- B.** 40%
- C. 33%
- D. 60%
- E. 25%

$$AM = [300 (\$25) - .5 (300) (\$30)] / [300 (\$25)] = .40$$

*Bodie - Chapter 03 #44  
Difficulty: Moderate*

45. When a firm markets new securities, a preliminary registration statement must be filed with
- A. the exchange on which the security will be listed.
  - B.** the Securities and Exchange Commission.
  - C. the Federal Reserve.
  - D. all other companies in the same line of business.
  - E. the Federal Deposit Insurance Corporation.

The SEC requires the registration statement and must approve it before the issue can take place.

*Bodie - Chapter 03 #45  
Difficulty: Easy*

46. In a typical underwriting arrangement the investment banking firm
- I) sells shares to the public via an underwriting syndicate.
  - II) purchases the securities from the issuing company.
  - III) assumes the full risk that the shares may not be sold at the offering price.
  - IV) agrees to help the firm sell the issue to the public but does not actually purchase the securities.
- A.** I, II, and III
  - B. I, III, and IV
  - C. I and IV
  - D. II and III
  - E. I and II

A typical underwriting arrangement is made on a firm commitment basis.

*Bodie - Chapter 03 #46  
Difficulty: Moderate*

47. Which of the following is **true** regarding private placements of primary security offerings?
- A. Extensive and costly registration statements are required by the SEC.
  - B. For very large issues, they are better suited than public offerings.
  - C. They trade in secondary markets.
  - D.** The shares are sold directly to a small group of institutional or wealthy investors.
  - E. They have greater liquidity than public offerings.

Firms can save on registration costs, but the result is that the securities cannot trade in the secondary markets and therefore are less liquid. Public offerings are better suited for very large issues.

*Bodie - Chapter 03 #47  
Difficulty: Moderate*

48. A specialist on the AMEX Stock Exchange is offering to buy a security for \$37.50. A broker in Oklahoma City wants to sell the security for his client. The Intermarket Trading System shows a bid price of \$37.375 on the NYSE. What should the broker do?
- A. Route the order to the AMEX Stock Exchange.
  - B. Route the order to the NYSE.
  - C. Call the client to see if she has a preference.
  - D. Route half of the order to AMEX and the other half to the NYSE.
  - E. It doesn't matter - he should flip a coin and go with it.

The broker should try to obtain the best price for his client. Since the client wants to sell shares and the bid price is higher on the AMEX, he should route the order there.

*Bodie - Chapter 03 #48  
Difficulty: Moderate*

49. You sold short 100 shares of common stock at \$45 per share. The initial margin is 50%. Your initial investment was
- A. \$4,800.
  - B. \$12,000.
  - C. \$2,250.
  - D. \$7,200.
  - E. none of the above.

$$100 \text{ shares} * \$45/\text{share} * 0.50 = \$4,500 * 0.50 = \$2,250$$

*Bodie - Chapter 03 #49  
Difficulty: Moderate*

50. You sold short 150 shares of common stock at \$27 per share. The initial margin is 45%. Your initial investment was
- A. \$4,800.60.
  - B. \$12,000.25.
  - C. \$2,250.75.
  - D. \$1,822.50.
  - E. none of the above.

$$150 \text{ shares} * \$27/\text{share} * 0.45 = \$4,050 * 0.45 = \$1,822.50$$

*Bodie - Chapter 03 #50  
Difficulty: Moderate*

51. You purchased 100 shares of XON common stock on margin at \$60 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin.

A. \$42.86  
B. \$50.75  
C. \$49.67  
D. \$80.34  
E. none of the above

$$100 \text{ shares} * \$60 * .5 = \$6,000 * 0.5 = \$3,000 \text{ (loan amount); } 0.30 = (100P - \$3,000)/100P; 30P = 100P - \$3,000; -70P = -\$3,000; P = \$42.86$$

*Bodie - Chapter 03 #51  
Difficulty: Difficult*

52. You purchased 1000 shares of CSCO common stock on margin at \$19 per share. Assume the initial margin is 50% and the maintenance margin is 30%. Below what stock price level would you get a margin call? Assume the stock pays no dividend; ignore interest on margin

A. \$12.86  
B. \$15.75  
C. \$19.67  
D. \$13.57  
E. none of the above

$$1000 \text{ shares} * \$19 * .5 = \$19,000 * 0.5 = \$9,500 \text{ (loan amount); } 0.30 = (1000P - \$9,500)/1000P; 300P = 1000P - \$9,500; -700P = -\$9,500; P = \$13.57$$

*Bodie - Chapter 03 #52  
Difficulty: Difficult*

53. You purchased 100 shares of common stock on margin at \$40 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$25? Ignore interest on margin.

A. 0.33  
B. 0.55  
C. 0.20  
D. 0.23  
E. 0.25

$$100 \text{ shares} * \$40/\text{share} * 0.5 = \$4,000 * 0.5 = \$2,000 \text{ (loan amount); } X = [100(\$25) - \$2,000]/100(\$25); X = 0.20.$$

*Bodie - Chapter 03 #53  
Difficulty: Difficult*

54. You purchased 1000 shares of common stock on margin at \$30 per share. Assume the initial margin is 50% and the stock pays no dividend. What would the maintenance margin be if a margin call is made at a stock price of \$24? Ignore interest on margin.
- A. 0.33
  - B. 0.375**
  - C. 0.20
  - D. 0.23
  - E. 0.25

$1000 \text{ shares} * \$30/\text{share} * 0.5 = \$30,000 * 0.5 = \$15,000$  (loan amount);  $X = [1000(\$24) - \$15,000]/1000(\$24)$ ;  $X = 0.375$ .

*Bodie - Chapter 03 #54  
Difficulty: Difficult*

55. You purchased 100 shares of common stock on margin for \$50 per share. The initial margin is 50% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$56 per share? Ignore interest on margin.
- A. 28%
  - B. 33%
  - C. 14%
  - D. 42%
  - E. 24%**

$100(\$50)(0.50) = \$2,500$  investment; gain on stock sale =  $(56 - 50)(100) = \$600$ ; Return =  $(\$600/\$2,500) = 24\%$ .

*Bodie - Chapter 03 #55  
Difficulty: Difficult*

56. You purchased 100 shares of common stock on margin for \$35 per share. The initial margin is 50% and the stock pays no dividend. What would your rate of return be if you sell the stock at \$42 per share? Ignore interest on margin.
- A. 28%
  - B. 33%
  - C. 14%
  - D. 40%**
  - E. 24%

$100(\$35)(0.50) = \$1,750$  investment; gain on stock sale =  $(42 - 35)(100) = \$700$ ; Return =  $(\$700/\$1,750) = 40\%$ .

*Bodie - Chapter 03 #56  
Difficulty: Difficult*

57. Assume you sell short 1000 shares of common stock at \$35 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$25/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. 20.47%
  - B. 25.63%
  - C. 57.14%**
  - D. 77.23%
  - E. none of the above

Profit on stock =  $(\$35 - \$25)(1,000) = \$10,000$ ; initial investment =  $(\$35)(1,000)(.5) = \$17,500$ ; return =  $\$10,000/\$17,500 = 57.14\%$ .

*Bodie - Chapter 03 #57  
Difficulty: Moderate*

58. Assume you sell short 100 shares of common stock at \$30 per share, with initial margin at 50%. What would be your rate of return if you repurchase the stock at \$35/share? The stock paid no dividends during the period, and you did not remove any money from the account before making the offsetting transaction.
- A. -33.33%**
  - B. -25.63%
  - C. -57.14%
  - D. -77.23%
  - E. none of the above

Profit on stock =  $(\$30 - \$35)(100) = -500$ ; initial investment =  $(\$30)(100)(.5) = \$1,500$ ; return =  $-\$500/\$1,500 = -33.33\%$ .

*Bodie - Chapter 03 #58  
Difficulty: Moderate*

59. You want to purchase GM stock at \$40 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$4000 to invest, how many shares can you buy?
- A. 100 shares
  - B. 200 shares**
  - C. 50 shares
  - D. 500 shares
  - E. 25 shares

you can buy  $(\$4000/\$40) = 100$  shares outright and you can borrow \$4,000 to buy another 100 shares.

*Bodie - Chapter 03 #59  
Difficulty: Moderate*

60. You want to purchase IBM stock at \$80 from your broker using as little of your own money as possible. If initial margin is 50% and you have \$2000 to invest, how many shares can you buy?
- A. 100 shares
  - B. 200 shares
  - C. 50 shares**
  - D. 500 shares
  - E. 25 shares

You can buy  $(\$2000/\$80) = 25$  shares outright and you can borrow \$2,000 to buy another 25 shares.

*Bodie - Chapter 03 #60  
Difficulty: Moderate*

61. Assume you sold short 100 shares of common stock at \$40 per share. The initial margin is 50%. What would be the maintenance margin if a margin call is made at a stock price of \$50?
- A. 40%
  - B. 20%**
  - C. 35%
  - D. 25%
  - E. none of the above

$\$4,000 \times 1.5 = \$6,000$ ;  $[\$6,000 - 100(\$50)]/100(\$50) = 20\%$ .

*Bodie - Chapter 03 #61  
Difficulty: Difficult*

62. Assume you sold short 100 shares of common stock at \$70 per share. The initial margin is 50%. What would be the maintenance margin if a margin call is made at a stock price of \$85?
- A. 40.5%
  - B. 20.5%
  - C. 35.5%
  - D. 23.5%**
  - E. none of the above

$\$7,000 \times 1.5 = \$10,500$ ;  $[\$10,500 - 100(\$85)]/100(\$85) = 23.5\%$ .

*Bodie - Chapter 03 #62  
Difficulty: Difficult*

63. You sold short 100 shares of common stock at \$45 per share. The initial margin is 50%. At what stock price would you receive a margin call if the maintenance margin is 35%?
- A. \$50
  - B. \$65
  - C. \$35
  - D. \$40
  - E. none of the above

$$\text{Equity} = 100(\$45) * 1.5 = \$6,750; 0.35 = (\$6,750 - 100P)/100P; 35P = 6,750 - 100P; 135P = 6,750; P = \$50.00$$

*Bodie - Chapter 03 #63  
Difficulty: Difficult*

64. You sold short 100 shares of common stock at \$75 per share. The initial margin is 50%. At what stock price would you receive a margin call if the maintenance margin is 30%?
- A. \$90.23
  - B. \$88.52
  - C. \$86.54
  - D. \$87.12
  - E. none of the above

$$\text{Equity} = 100(\$75) * 1.5 = \$11,250; 0.30 = (\$11,250 - 100P)/100P; 30P = 11,250 - 100P; 130P = 11,250; P = \$86.54$$

*Bodie - Chapter 03 #64  
Difficulty: Difficult*

65. IPO average first-day returns are largest in \_\_\_\_\_.
- A. The United States
  - B. Denmark
  - C. Japan
  - D. China
  - E. France

See Figure 3.2.

*Bodie - Chapter 03 #65  
Difficulty: Easy*

66. Despite large first-day IPO returns, average first-year returns in the US are approximately \_\_\_\_\_ percent.

- A.** 6.7
- B. 18.2
- C. 26.4
- D. 4.8
- E. 9.1

See Figure 3.3.

*Bodie - Chapter 03 #66  
Difficulty: Easy*

67. Average second-year IPO returns in the US are approximately \_\_\_\_\_ percent.

- A. 6.7
- B. 18.2
- C. 26.4
- D.** 5.3
- E. 9.1

See Figure 3.3.

*Bodie - Chapter 03 #67  
Difficulty: Easy*

68. Average third-year IPO returns in the US are approximately \_\_\_\_\_ percent.

- A. 6.7
- B. 18.2
- C. 26.4
- D. 5.3
- E.** 10.3

See Figure 3.3.

*Bodie - Chapter 03 #68  
Difficulty: Easy*

69. The preliminary prospectus is referred to as a \_\_\_\_\_.

- A.** red herring
- B. indenture
- C. green mail
- D. tombstone
- E. headstone

The preliminary prospectus is referred to as a red herring.

*Bodie - Chapter 03 #69  
Difficulty: Easy*

70. The minimum revenue required for an initial listing on the New York Stock Exchange is
- A. \$2,000,000
  - B. \$25,000,000
  - C. \$50,000,000
  - D.** \$75,000,000
  - E. 100,000,000

See Table 3.2.

*Bodie - Chapter 03 #70  
Difficulty: Moderate*

71. The minimum annual pretax income in the previous two years required for an initial listing on the New York Stock Exchange is
- A.** \$2,000,000
  - B. \$25,000,000
  - C. \$50,000,000
  - D. \$75,000,000
  - E. 100,000,000

See Table 3.2.

*Bodie - Chapter 03 #71  
Difficulty: Moderate*

72. The daily dollar volume of trading on the NYSE in 2006 was approximately \_\_\_\_\_ dollars.
- A.** \$75 billion
  - B. \$4 trillion
  - C. \$12 billion
  - D. \$4 billion
  - E. none of the above

The trading volume of the NYSE averaged 1.8 billion shares with an approximate value of \$75 billion.

*Bodie - Chapter 03 #72  
Difficulty: Easy*

73. The average daily number of shares traded on the NYSE in 2006 was approximately \_\_\_\_\_ dollars.
- A.** 1.8 billion
  - B. 1.8 trillion
  - C. 12 billion
  - D. 4 trillion
  - E. none of the above

The trading volume of the NYSE averaged 1.8 billion shares with an approximate value of \$75 billion.

*Bodie - Chapter 03 #73  
Difficulty: Easy*

74. The \_\_\_\_\_ had the largest trading volume of securities in 2006.
- A. NASDAQ
  - B.** NYSE
  - C. London
  - D. Tokyo
  - E. Hong Kong

See Figure 3.6.

*Bodie - Chapter 03 #74  
Difficulty: Easy*

75. The securities act of 1933 \_\_\_\_\_.
- I) requires full disclosure of relevant information relating to the issue of new securities
  - II) requires registration of new securities
  - III) requires issuance of a prospectus detailing financial prospects of the firm
  - IV) established the SEC
  - V) requires periodic disclosure of relevant financial information
  - VI) empowers SEC to regulate exchanges, OTC trading, brokers, and dealers
- A.** I, II and III
  - B. I, II, III, IV, V, and VI
  - C. I, II and V
  - D. I, II and IV
  - E. IV only

The securities act of 1933 requires full disclosure of relevant information relating to the issue of new securities, requires registration of new securities, and requires issuance of a prospectus detailing financial prospects of the firm.

*Bodie - Chapter 03 #75*

76. The securities act of 1934 \_\_\_\_\_.
- I) requires full disclosure of relevant information relating to the issue of new securities
  - II) requires registration of new securities
  - III) requires issuance of a prospectus detailing financial prospects of the firm
  - IV) established the SEC
  - V) requires periodic disclosure of relevant financial information
  - VI) empowers SEC to regulate exchanges, OTC trading, brokers, and dealers
- A. I, II and III
  - B. I, II, III, IV, V, and VI
  - C. I, II and V
  - D. I, II and IV
  - E. IV, V, and VI**

The securities act of 1934 established the SEC, requires periodic disclosure of relevant financial information, and empowers SEC to regulate exchanges, OTC trading, brokers, and dealers.

*Bodie - Chapter 03 #76  
Difficulty: Easy*

77. Which of the following is **not** required under the CFA Institute standards of professional conduct?
- A. knowledge of all applicable laws, rules and regulations
  - B. disclosure of all personal investments whether or not they may conflict with a client's investments**
  - C. disclosure of all conflicts to clients and prospects
  - D. reasonable inquiry into a client's financial situation
  - E. All of the above are required under the CFA Institute standards.

*Bodie - Chapter 03 #77  
Difficulty: Moderate*

78. According to the CFA Institute Standards of Professional Conduct, CFA Institute members have responsibilities to all of the following **except**:
- A. the government**
  - B. the profession
  - C. the public
  - D. the employer
  - E. clients and prospective clients

See "Excerpts from CFA Institute Standards of Professional Conduct".

*Bodie - Chapter 03 #78  
Difficulty: Moderate*

79. Of the secondary stock markets, which have been expanding and which have been contracting? Give some of the reasons for the changes.

The over the counter market (OTC) has grown dramatically in recent years. The market has become much more automated and information-efficient. The National Association of Security Dealers Automated Quotations (NASDAQ) system is part of the reason for this growth. NASDAQ consists of the more broadly traded OTC stocks. Up to date price quotations are available on these stocks, and thus investors are much more willing to invest in these stocks than prior to the creation of this system. In recent years, many firms which have grown large enough to qualify for NYSE listing have chosen to remain NASDAQ traded.

The OTC market has taken some growth from the NYSE, largely due to the increased technology of the OTC market. The American Stock Exchange (AMEX) has decreased in size dramatically in recent years. This exchange is being pressured both from the top and from the bottom. That is, as mergers and acquisitions occurred (primarily in the 1980s), often two AMEX firms merged into one firm large enough for NYSE listing. In addition, the AMEX also has experienced the pressure from the OTC market as larger firms chose to remain in that market.

Feedback: This questions tests the student's understanding of changes that have been occurring in secondary markets.

*Bodie - Chapter 03 #79  
Difficulty: Moderate*

80. Discuss margin buying of common stocks. Include in your discussion the advantages and disadvantages, the types of margin requirements, how these requirements are met, and who determines these requirements.

Buying stock on margin means buying stock with partially borrowed funds. These funds are borrowed from your broker, who has borrowed the funds from a commercial bank. The initial margin requirement is the percent of the funds that must be your own. The current initial margin requirement is 50% and is set by the Federal Reserve System. Margin is simply equity as a percent of the value of your account. Subsequent to opening the account, stock prices change and thus the margin of your account changes. The maintenance margin is the relevant margin after you open your account. A 25% maintenance margin is required for NYSE listed stocks; however, most brokers will require a maintenance margin above that amount. If the margin of your account falls below the maintenance margin requirement, you will receive a margin call. You can either send your broker more cash to reduce the amount of the original loan to get your account back to the required maintenance margin, or your broker can sell some of the shares for you, using the proceeds to reduce the amount of your original loan, thus getting your account back to the margin requirement.

If the price of the stock increases, your account will become overmargined and you can either pyramid (buy more shares without using any of your own cash) or you can withdraw cash from the account (increasing the amount of the loan). If you execute either of these actions, you must not let your account fall below the initial margin requirement (increasing the number of shares or the amount of the loan requires the account to be treated as a new account).

The advantage of margin is that of leverage. If the price of stock increases you own more shares than had you used only your own funds and your returns will be greater. The disadvantage of margin is that if the price of the stock declines you will own more shares and your losses will be greater than had you used only your own funds.

Feedback: This question tests the student's understanding of margin requirements and how they work.

*Bodie - Chapter 03 #80  
Difficulty: Moderate*

81. List three factors that are listing requirements for the New York Stock Exchange. Why does the exchange have such requirements?

Factors include, but are not limited to, minimum pretax income in the last year, minimum average annual pretax income in the previous two years, minimum market value of publicly held stock, minimum number of shares publicly held, and a minimum number of holders of one hundred shares or more. The NYSE has these requirements to ensure that the firm has enough trading interest for the NYSE to allocate facilities and floor space.

Feedback: This question tests the student's understanding of listing requirements for the NYSE and why those requirements exist.

*Bodie - Chapter 03 #81  
Difficulty: Moderate*

## ch3 Summary

<u>Category</u>	<u># of Questions</u>
Bodie - Chapter 03	81
Difficulty: Difficult	15
Difficulty: Easy	18
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