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QUESTION 1

An indifference curve represents combinations of portfolios having equal utility to the investor. Given that risk and returns are plotted on the horizontal and vertical axes, respectively, and that the investor is risk averse, the curve has

A. An increasingly steeper slope if the investor is less risk averse.

B. A decreasingly negative slope if the investor\\'s utility increases.

C. An increasingly positive slope

D. A decreasingly positive slope.

Correct Answer: C

An indifference curve represents combinations of portfolios having equal utility to the investor. Given that risk and returns are plotted on the horizontal and vertical axes, respectively, and that the investor is risk averse, the curve has an increasingly positive slope. As risk increase, the additional required return per unit of additional risk also increases. The steeper the slop of an indifference curve, the more risk averse an investor is. The higher the curve, the greater is the investor\\'s level of utility.

QUESTION 2

Which of the following is not a category of relevant cash flows\\'?

A. Annual net cash flows

B. Project termination cash flows.

C. Incremental cash flows.

D. Net initial investment.

Correct Answer: C

Relevant cash flows are a much more reliable guide when judging capital projects, since only they provide a true measure of a project\\'s potential to affect shareholder value. The relevant cash flows can be divided into three categories. (1) net initial investment, (2) annual net cash flows, and (3) project termination cash flows. An incremental cash flow is the difference in cash received or disbursed resulting from selecting one option instead of another. It is not a category of relevant cash Bows.

QUESTION 3

Conversion cost pricing

A. Places minimal emphasis on the cost of materials used in manufacturing a product.

B. Could be used when the customer furnishes the material used in manufacturing a product.

C. Places heavy emphasis on indirect costs and disregards consideration of direct costs.

D. Places heavy emphasis on direct costs and disregards consideration of indirect costs.

Correct Answer: B

Conversion costs consist of direct labor and factory overhead, the costs of converting raw materials into finished goods. Normally, a company does not consider only conversion costs in making pricing decisions, but if the customer were to furnish the raw materials, conversion cost pricing would be appropriate.

QUESTION 4

Which one of the following factors might cause a firm to increase the debt in TTS financial structure?

A. An increase in the corporate income tax rate.

B. Increased economic uncertainty

C. An increase in the federal funds rate.

D. An increase in the price-earnings ratio.

Correct Answer: A

An increase in the corporate income tax rate might encourage a compare to borrow because interest on debt is tax deducible, `4iereas dividends are not Accordingly, an increase in the tax rate means that the after-tax cost of debt capital will decrease, Given equal interest rates, a firm with a high tax rate 4ll have a lower after- tax cost of debt capital than a firm with a low tax rate.

QUESTION 5

The modeling technique to be used for situations involving a sequence of events with several possible outcomes associated with each event is

A. Queuing theory.

B. Simulation.

C. Linear programming.

D. Decision tree analysis.

Correct Answer: D

Decision tree analysis is useful when the most beneficial series of decisions is to be chosen. The possible decisions for each decision point, the events that might follow from each decision, the probabilities of these events, and the quantified outcomes should be known.

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