



Module 2 Exam - SOLUTIONS

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Test No.:	See question 38	This is your test version (ABCD) and unique ID number (0 to 9999)
Date:	2	This is the module number for this exam
Hour (Period):	101, 102, 103, etc.	This is your Discussion Section number – see below

Section	Day / Time	GSI Name
101	Tu 8-9A	Jonathan Heyne
102	Tu 9-10A	Dan Githinji
103	Tu 10-11A	Diego Butrich
104	Tu 11A-12P	Andy Kang
105	Tu 12-1P	Diego Butrich
106	W 8-9A	Udit Nakhat
107	W 10-11A	Udit Nakhat
108	W 11A-12P	Victor Villalobos
109	W 12-1P	Victor Villalobos
110	W 1-2P	Deepak Nainani
111	Th 8-9A	Carol Macavilca Paredes/Robert Gutierrez
112	Th 9-10A	Christine Chen
113	Th 10-11A	Carol Macavilca Paredes/Robert Gutierrez
114	Th 11A-12P	Andy Kang
115	Th 12-1P	Hans Klinger
116	Th 1-2P	Hans Klinger
117	Tu 1-2P	Deepak Nainani
118	Tu 2-3P	Christine Chen
119	Th 2-3P	Dan Githinji

UGBA 10 – Principles of Business

MODULE 2 EXAM SOLUTIONS – Fall 2017 10/13/2017

FINANCE & ACCOUNTING

Instructor: Professor Briginshaw

1) What is profit or earnings?

- A) Total money taken in by a corporation
- B) Increases in income from year to year
- C) Increases in a corporation's stock price
- D) Revenue generated by goods and services
- E) Difference between revenues and expenses

Answer: E

Explanation: E) Profits represent the difference between an organization's revenues and its expenses and profits are the goal of most businesses and allow people to open and expand businesses. REF: Chapter 1 of Custom text

2) What is the term for the physical and intellectual contributions of people while engaged in the production of goods and services?

- A) Human resources
- B) Working capital
- C) Physical resources
- D) Planned resources
- E) Market resources

Answer: A

Explanation: A) Human resources, often referred to as labor or human capital, is comprised of those who contribute physically or intellectually to the production of a good or service for economic production. REF: Chapter 1 of Custom text

3) As common practice, an executive working within a firm to manage the profitability of a small group of products would receive information from...

- A) ...from the firm's financial accounting system.
- B) ...from the firm's managerial accounting system.
- C) ...from both the firm's financial accounting system and its forensic accounting system.
- D) ...from the firm's investment accounting system.
- E) As common practice, the executive would not receive any information from the firm's accounting system.

Answer: B

Explanation: Internal users, such as brand or product managers, use the firm's managerial accounting system.

4) Which of the following refers to the financial statement detailing a firm's assets, liabilities, and owners' equity?

- A) Income statement
- B) Statement of cash flows
- C) Balance sheet
- D) Expense report

E) Annual budget

Answer: C

Explanation: C) A balance sheet uses the accounting equation to show the financial position.

5) The Federal Reserve has followed a loose monetary policy by adding large amounts of money supply to the economy. What is the major risk of this policy?

- A) Inability to purchase bonds on the open market
- B) Inability to track the resulting increase in the money supply
- C) Excessive unemployment
- D) Excessive inflation

Answer: D

Explanation: an excessive amount of money in the market depresses the value or purchasing power of the money. This is inflation.

6) All of the following are advantages of deposit insurance (such as the FDIC) except...

- A) Prevents “run on the bank”
- B) Enhances confidence of savers, even in a financial crisis
- C) Imposes insurance costs and administrative requirements on banks
- D) Decreases the need for small savers to investigate bank strength before saving there

Answer: C (this is the “downside” or cost of deposit insurance)

7) A customer has a bond fund which returns 2% per year before fees, and the fees/charges for the fund are 1% of the investment per year. In 2014, the customer invested \$10,000 in the fund. After three years, the customer’s funds would be closest to:-

- a) \$9700
- b) \$10,000
- c) \$10,300
- d) \$10,600

Answer: C

Explanation: Customer earns \$200 per year (2%) but pays \$100 in fees.

8) Luxan Cheese is a cheese shop. In January, Luxan finds some excellent cheese called Tallegio from Italy. Luxan buy \$2000 worth on credit, taking delivery in January and paying suppliers **after 30 days** (in February). In February they start to sell the cheese, and deliver 75% (three quarters) of the cheese to selected customers for a 100% markup in February. Luxan sells and delivers the remaining cheese to customers in **March**, at a 50% markup. Luxan’s customers pay cash after 30 days. What is the **Revenue for the three months** January, February and March?

	January	February	March
	Revenue	Revenue	Revenue
a)	-2000	1500	500
b)	0	2250	1000
c)	2000	1000	750
d)	0	3000	750

ANSWER: D

Explanation: January – no cheese sold, so revenue = 0

February: 75% of the \$2000 cheese is sold => cost of cheese is \$1500. The cheese is marked up by 100% => Revenue of \$3000

March: Remaining cheese is 25% of \$2000 => cost of cheese is \$500. However, this cheese is only marked up 50% => Revenue of \$750

Contribution Margin

9) Adam's Pizza pays \$2000 fixed rent per month and each pizza costs \$6 in ingredients and hourly paid labor. Pizzas sell for \$10 per pizza - what is the break even number of pizzas for Adam's pizza?

- a) 400 pizzas
- b) 267 pizzas
- c) 667 pizzas
- d) 500 pizzas

ANSWER: D

Explanation: Profit = Unit CM x Units – Fixed cost

Set Profit = 0 => Units = F/Unit CM = \$2000/(10-6) = 500

10) Commissions based on sales volume and the cost of ingredients are two possible costs a pizza restaurant could incur. Thinking about a variable vs fixed cost framework, what type of costs would these each be?

- | | Sales commissions | Cost of ingredients |
|----|-------------------|---------------------|
| a) | Variable | Variable |
| b) | Variable | Fixed |
| c) | Fixed | Variable |
| d) | Fixed | Fixed |

ANSWER: A

Explanation: Sales commissions and cost of ingredients each increase with activity

USE THE FOLLOWING INFORMATION TO ANSWER THE NEXT TWO QUESTIONS

Global Economy's Stubborn Reality: Plenty of Work, Not Enough Pay

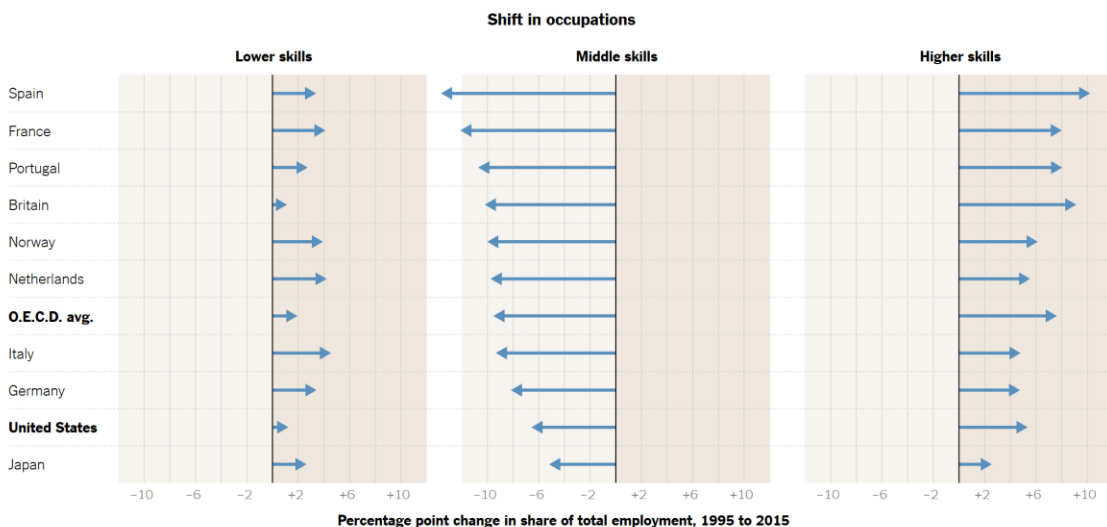
By PETER S. GOODMAN and JONATHAN SOBLE

THE NEW YORK TIMES, OCT. 7, 2017

In the three-plus decades since Ola Karlsson began painting houses and offices for a living, he has seen oil wealth transform the Norwegian economy. He has participated in a construction boom that has refashioned Oslo, the capital. He has watched the rent climb at his apartment in the center of the city.

What he has not seen in many years is a pay raise, not even as Norway’s unemployment rate has remained below 5 percent, signaling that working hands are in short supply... In many major countries, including the United States, Britain and Japan, labor markets are exceedingly tight, with jobless rates a fraction of what they were during the crisis of recent years. Yet workers are still waiting for a benefit that traditionally accompanies lower unemployment: fatter paychecks.

Why wages are not rising faster amounts to a central economic puzzle... A hollowed-out labor market is partly to blame. A fundamental refashioning of the labor market has been underway for two decades. Jobs that require middle-range skills have been declining, while those involving skills at both the lower and higher end of the spectrum have been growing. This effectively suppresses wages for many: People in lower-paid, lower-skill jobs — retail workers, janitors and home health aides — have little bargaining power to demand higher wages. Middle-skilled workers — including clerks, call center operators and factory workers — are being replaced by computers, robots and lesser-paid hands in low-wage countries. Higher-skilled workers are capturing an outsized share of pay.



Source: Organization for Economic Cooperation and Development

11) Based on the above chart, all of the below must be true **except**

- A) All the countries are experiencing a relative decrease in the need for middle skilled employees
- B) All the countries are experiencing a relative increase in the need for lower skilled employees
- C) All the countries are experiencing a relative increase in the need for higher skilled employees
- D) All the countries are experiencing a fall in total employment

ANSWER: D – although this may be true, the chart only shows the relative proportion of the skill levels within total employment, not changes in total employment itself

12) What is one **likely consequence** if the authors' contentions about the labor market are correct?

- A) Due to an increase in the need for lower skilled workers, they will be able to get large raises
- B) Scarcity of middle skilled jobs will create a shortage of workers and a rise in wages
- C) If average pay rates to higher skilled workers do not fall, that group's share of total pay will rise
- D) The share of pay of higher skilled workers will decline

ANSWER: C

Explanation: A is not true, as the authors contend that low skilled workers "have little bargaining power to demand higher wages". Scarcity of jobs will cause a fall in wages for middle skilled workers, meaning B cannot be true. C is true (and D untrue) as a matter of arithmetic, as the proportion of higher skilled workers is increasing.

13) Which of the following is a consequence of the *divisibility* characteristic of money?

- A) Units of money do not expire after a certain time limit.
- B) Units of money can be accurately matched with the value of goods.
- C) Units of money are easily carried.
- D) Units of money have relatively stable value.
- E) Units of money of different nations are easily converted to other units of money.

Answer: B

Explanation: B) Modern currency is easily divisible into smaller parts, each with a fixed value. For example, one dollar can be exchanged for 10 dimes. Thus, the actual value of goods can be approximated very well by units of money.

14) Which of the following is considered by many to be the BEST single indicator of the U.S. equities market?

- A) NASDAQ Composite
- B) Russell 2000
- C) Dow Jones Industrial Average
- D) Standard & Poor's 500
- E) New York Stock Exchange

Answer: D

Explanation: D) The S&P 500 considers more companies than the Dow Jones, and so the S&P 500 is regarded as a better indicator.

15) In which option A-D are the investments listed in order of **increasing riskiness**?

- A) Treasury bills, Mutual fund, Common stock
- B) Mutual fund, Common stock, Treasury bills
- C) Mutual fund, Treasury bills, Common stock
- A) Common stock, Mutual fund, Treasury bills

ANSWER: A

Explanation: Treasury bills are the safest of all investments. Mutual funds have a range of risks, but the riskiest of funds, which pool common stock investments, are less risky than an individual common stock.

16) All of the following are **current assets** *except*?

- A) Cash
- B) Accounts receivable
- C) Buildings
- D) Inventory

ANSWER: C

EXPLANATION: Buildings are long term assets.

17) When the value of a country's currency is **weak** in the international market, what is the **most likely** effect?

- A) Exports decrease because the cost of items is more expensive in the international market.
- B) Vacationers from the country benefit when they take an international vacation.
- C) Exports increase because the cost of items is more affordable in the international market.
- D) Both A and B are true.

ANSWER: C

Explanation: A weaker currency can buy less goods from other countries, thus making imports more expensive. However, other countries can buy more of the weak currency country's products, which makes its exports more affordable.

18) Piecrust Company has a net income of \$10 million. Piecrust's number of outstanding shares of stock is 5,000,000 shares. What is the company's earnings per share?

- A) \$0.50
- B) \$1.00
- C) \$1.50
- D) \$2.00
- E) \$2.50

Answer: D

Explanation: D) Earnings per share = Net Income/Number of Common Shares Outstanding; therefore, in this scenario, \$10m/5m = \$2.

19) Which of the following statements is true about treasury bonds as investments?

- A) Bonds are among the riskiest of all investments.
- B) Bonds are suitable for investors who seek security.
- C) Bonds will never become worth less than their purchase price.
- D) Treasury bonds are sensitive to individual company performance.

Answer: B

Explanation: B) Bonds are quite secure but can fall in value (negating C) if interest rates rise

20) A person will receive \$144 in 2 years from a business investment, having initially invested \$100. The annual rate of return on the investment is closest to...

- a) 10%
- b) 12%
- c) 20%
- d) 44%

ANSWER: C

EXPLANATION: $1.2^2 = 1.44$

21) The study.net / HBS article “Financial Statement and Ratio Analysis” identifies three fundamental factors driving company performance. What does the paper identify as the starting point for evaluating companies?

- a) profit margin
- b) asset turnover
- c) financial leverage
- d) return on equity
- e) revenue growth

ANSWER: D, see page 1 of reading

22) Which of the following **uses of cash** within the Capsim finance screen are related to **stockholders equity**?

- a) Pay interest
- b) Pay back long-term debt
- c) Issue long-term debt
- d) Pay dividends

ANSWER: D relates to stock, all others relate to debt

23) When discussing the Dupont analysis as it pertains to TESLA – how would you characterize the 2016 performance of the company as discussed in lecture?

- | | Profit margin | Financial leverage |
|----|----------------------|---------------------------|
| a) | Low or negative | High |
| b) | High | Low or negative |
| c) | Low or negative | Low |
| d) | High | High |

ANSWER: A

24) Which of the following is figured by dividing the yearly dollar amount of dividend income by the investment's current market value?

- A) Bond value
- B) Current dividend yield
- C) Debenture
- D) Trading volume
- E) Earnings per share

Answer: B

Explanation: B) The current dividend yield is the rate of return from dividends paid to shareholders.

25) Which of the following is NOT part of the M-2 money supply?

- A) Currency at hand
- B) Currency amount of written checks
- C) Balance in a checking account
- D) Currency value of time deposits
- E) Common stock

ANSWER: E

Explanation: A, B and C are included in M-1, and therefore are included in M-2 also, as M-1 is a subset of M-2. Time deposits are included in M-2 (but not M-1). Common stock is not included in either M-1 or M-2.

26) Which of the following is considered by many to be the BEST indicator of the market for common stocks of blue-chip large-cap companies?

- A) NASDAQ Composite
- B) Russell 2000
- C) Dow Jones Industrial Average
- D) Standard & Poor's 500
- E) New York Stock Exchange

ANSWER: C

Explanation: The Dow Jones Industrial Average indicates the performance of only 30 large blue chip companies, see custom text page 125.

27) Unemployment in the United States at October 2017 as measured by the BLS (Bureau of Labor Statistics) is closest to....

- A) 0%
- B) 4%
- C) 8%
- D) 12%

ANSWER: B, as discussed in lectures 1, 2 and 5 (chart).

Financial Statement and ratio analysis: Use the following information on Draftmans Inc to answer the next **two** questions. Assume that these numbers are both average and year-end, as needed.

Average stockholders' equity	\$45,000	Net income (current year)	\$ 4,500
Average total assets	\$90,000	Net sales (current year)	\$60,000
Current assets	\$10,000	Net sales (previous year)	\$40,000
Current liabilities	\$15,000		

28) What is the **return on equity** for Draftmans?

- a) 5%
- b) 10%
- c) 15%
- d) 20%

ANSWER: B

Explanation: $\text{RoE} = \text{net income}/\text{equity} = \$4,500/\$45,000 = 10\%$

29) What are the **total liabilities** of Draftmans?

- a) \$5,000
- b) \$15,000
- c) \$45,000
- d) \$80,000

ANSWER: C

Explanation: Using accounting equation $A=L+SE \Rightarrow L = A-SE = \$90K - \$45K = \$45K$

30) Which of the following reasons is the primary motivator for a commercial bank to acquire new depositors?

- A) A new deposit account will make more funds available to pay the interest on other deposit accounts.
- B) A new deposit account will make more funds available to pay the bank's employees.
- C) A new deposit account will make more funds available to give out in loans.
- D) A new deposit account will make more funds available to give out in dividends to its investors.
- E) A new deposit account will make more funds available to facilitate brokerage transactions.

Answer: C

Explanation: C) A commercial bank makes its profits from investments and loans derived from its depositors' cash.

31) Assume that 10% reserve requirement has been imposed on banks. A client of Wells Fargo discovers a \$50 bill that has been lost for 80 years and therefore was not included in the money supply statistics. He deposits the \$50 in a checking account, which the bank relends to a new client (minus the reserve requirement) in cash. What is the effect on the M-1 money supply?

- a) There is no change in the M-1 Money supply
- b) The M-1 Money supply increases by \$50
- c) The M-1 Money supply increases by \$95
- d) The M-1 Money supply increases by \$100

Answer: C

Explanation: M-1 increases by \$50 (bank balance) + (\$50*.9) (cash in hands of borrower) = \$95

32) The Federal Reserve has a **Dual Mandate** as discussed in lecture, meaning it has two main goals in conducting monetary policy. Which one of the following is **an element** of the “Fed’s” dual mandate?

- a) to maximize bond prices
- b) to increase stock prices
- c) to minimize employment
- d) achieve price stability

Answer: D

Explanation: The Federal Reserve’s dual mandate was determined by Congress in 1977. It is to promote maximum sustainable employment and price stability. Price stability is usually interpreted as low and stable inflation. Lecture 6

33) All of the following are **advantages specific to money** except?

- A) Portability
- B) Durability
- C) Store of value
- D) Divisibility

Answer: C

Store of value is a function of money, but can also be performed by other things such as cows or buildings.

34) Which person is **least likely** to secure a good retirement income by their investments?

- A) Persons who rely only on social security
- B) A person who invests 5% of their salary beginning at age 25
- C) A person who invests 10% of their salary beginning at age 25
- D) A person who invests 15% of their salary beginning at age 55

Answer: A is least likely to have a comfortable retirement, as they will have no additional savings.

35) Michael Richman has \$1,500,000 total savings. As a minimum, how many individual bank companies should he spread the savings between, to make sure that it is all insured by the FDIC?

- A. 1
- B. 3
- C. 6
- D. 15

Answer: C, \$250K per bank is insured

36. A company has positive contribution margin, but negative net margin. What can we say about the company's prospects?

- A) The company can never be profitable, irrespective of scale
- B) With sufficient growth, the company can become profitable as it grows past its break-even point
- C) As the company increases its sales, its losses will widen further
- D) The company would be profitable now, if its financial leverage were higher

Answer: B

Explanation: A company with a positive contribution margin can achieve profitability by growth in units sold, so B is correct. Answers A and C are appropriate for a company with negative contribution margin. Financial leverage can boost positive returns, but it also makes negative returns **more** negative, so D is not true.

37. A

38. [Depends on version]