



Module 1 Exam SOLUTION

Spring 2020

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- This is an exam. Do not talk.
- Books, notes, and electronic devices including calculators, must be put completely away, out of sight.
- Do not begin the exam until you are told to begin.
- Once you leave the exam room, you may not return. No bathroom or other breaks during the exam.
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- Hold onto the exam until scores are posted. It will come in handy if you there are issues with your answer to question 38.
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Section	Day/time	GSI Name
101	Tu 1-2P	Jessica Slocovich
102	Tu 2-3P	Maria Antolinez
103	Tu 3-4P	Maria Antolinez
104	Tu 5-6P	Jessica Slocovich
105	Wed 9-10A	Jin Kim
106	Wed 10-11A	Jin Kim
107	Wed 11A-12P	Celso Garcia
108	Wed 12-1P	Celso Garcia
109	Wed 1-2P	Sebastian Ochoteco
110	Wed 2-3P	Cristina Paulsen

Section	Day / Time	GSI Name
111	Wed 3-4P	Cristina Paulsen
112	Wed 4-5P	Adelaida Valencia
113	Wed 5-6P	Adelaida Valencia
114	Thu 1-2P	Cristobal Sarquis
115	Thu 2-3P	Daniela Kurinaga
116	Thu 3-4P	Daniela Kurinaga
117	Thu 5-6P	Cristobal Sarquis
118	Th 8-9A	Sebastian Ochoteco
119	Th 9-10A	Antonio Ciudad
120	Th 10-11A	Antonio Ciudad

MAKE SURE TO:

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- **FILL OUT ALL SCANTRON FIELDS AS EXPLAINED ABOVE**

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UGBA 10 – Principles of Business
MODULE 1 EXAM Spring 2020
FINANCE & ACCOUNTING
Instructor: Professor Briginshaw

2/14/2020
EXAM SOLUTION

- 1) What is the best description of expenses?
- A) Cash flows that go out of a company during the month
 - B) The difference between assets and liabilities
 - C) The costs incurred in producing a good or service
 - D) The money taken out each month to benefit the owners

Answer: C. See custom text page 51

- 2) Which of the following are **not** classified as “Tools of the Fed”?

- A) Reserve requirements.
- B) Interest rate controls.
- C) Government spending controls.
- D) Open market operations.

Answer: C

Explanation: Spending is a facet of fiscal policy, which is controlled by Congress.

- 3) As common practice, a fund or investment manager holding common stock in a firm 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 managerial accounting system and its financial accounting system.
- D) ...from the firm's investment accounting system.
- E) As common practice, a fund manager does not receive any information from the firm's accounting system.

Answer: A

Explanation: As an external user, the investment manager (like any external investor) will only receive access to the financial accounting data. See custom text page 41. Firms cannot invest in their own common stock.

- 4) The reading “Delivery Start-Ups Are Back Like It’s 1999” compares the failed 1990s grocery delivery startup Webvan to Instacart. What is one key difference in the economics that the article points out?

- A) Instacart charges no fee while Webvan charged \$3.99 per order
- B) Instacart uses company-owned vehicles to deliver products to maximize marketing appeal
- C) Webvan required an internet connection whereas Instacart does not
- D) Webvan invested heavily in distribution centers whereas Instacart has not

Answer: D. This is discussed in paragraph 9 of the reading. The other answers are untrue or counter-factual.

- 5) Which of the following terms refers to the amount of money that owners would receive if they sold all of a company's assets and paid all of its liabilities?

- A) Asset
- B) Owners' equity

- C) Inventory
 - D) Liability
 - E) Credit
- Answer: B

- 6) The International Monetary Fund (IMF) has all of the following aims **except**...
- A) Promotion of stable exchange rates
 - B) Provision of temporary short term loans to member countries
 - C) Funding of national improvements such as schools, roads, power plants and hospitals
 - D) Encourage development of a system for international payments

Answer: C

Explanation: A, B & D describe the IMF. C describes the World Bank. See custom text p. 96-97

- 7) A customer has a bond fund which returns 1% per year before fees, and the fees/charges for the fund are 1.5% of the investment per year. In 2017, the customer invested \$10,000 in the fund. After three years, the customer's funds would be closest to:-

- a) \$9,700
- b) \$9,850
- c) \$10,150
- d) \$10,300

Answer: B

Explanation: The investor has a net loss of 0.5% per year, or about \$50. So over three years the fund will decrease by \$150 to \$9,850.

- 8) Unemployment rate and labor force participation are key economic indicators associated with the labor market. Which combination of values of these indicators would be most likely to cause or be associated with **wage inflation**?

- | | Unemployment rate | Labor Force Participation |
|----|-------------------|---------------------------|
| A) | Lower | Lower |
| B) | Lower | Higher |
| C) | Higher | Lower |
| D) | Higher | Higher |

Answer: B

Explanation: Wage inflation is inflation (increase) in wages. This is a result of fewer people being available for work, together with constant or increasing demand for labor. Effectively, wage inflation is caused by an **absence** of labor market slack, because when there is no slack, the only way to recruit an employee is to bid up wage rates to get them to give up an existing job. Just as labor market slack is observed when unemployment is high and/or participation is low, its absence occurs when unemployment is low and/or participation is high. Discussed in lecture 5.

Contribution Margin

Use the following information about "Instadash" to answer the next two questions:-

Instadash is a delivery startup that helps grocery shoppers get their groceries by shopping at Safeway and delivering the groceries to the customer's house. Instadash charges a markup of 50% on the groceries, but does not charge a per shipment or per delivery fee. Instadash receives no discount from Safeway. So, for a loaf of bread priced at \$2 in the Safeway store, Instadash charges its customer \$3, and pays Safeway \$2.

Instadash workers are paid \$20 per hour to collect and deliver groceries and the average time to complete a delivery (including shopping) is 29 minutes. The cost of the workers and the payments for groceries (to Safeway) are the only variable costs. Total fixed costs for Instadash are \$100 million per year.

9) Looking at the options below, what is the lowest order size in dollars at Safeway prices (i.e. excluding the markup) that will provide Instadash with a positive contribution margin on the order?

- a) \$10
- b) \$20
- c) \$30
- d) \$40

Answer: b

Solution: 29 minutes is slightly less than half an hour, so the shopper is paid slightly less than \$10 for that time. Therefore, a \$20 order, which provides \$10 of revenue, provides a small amount of positive contribution to Instadash. A \$10 order provides \$5 revenue (less than the costs of the shopper). Options C and D provide too much revenue and contribution, since the question asks for the lowest dollar amount above break-even.

10) Assume an average order size at Safeway prices (i.e. excluding the markup) of \$120. The break-even number of orders per year for Instadash is **closest** to...?

- a) 0.5 million orders
- b) 1 million orders
- c) 1.5 million orders
- d) 2 million orders

Answer: d

Notes: A \$120 order provides \$60 of markup to Instadash. The payment to the shopper (Variable cost) is just less than \$10, meaning that the contribution from each order is approximately \$50. Therefore, 2 million orders are required to secure a small profit for Instadash. Alternatives a, b and c would result in losses

11) Jim's Specialty Cheese is a cheese shop. In January, Jim's finds some excellent cheese called Manchego from Spain. They (Jim's) buy \$800 worth on credit, taking delivery in January, to pay Manchego in 30 days (i.e. they will pay the supplier in February). In February they start to sell the cheese, and deliver half of the cheese to their favorite customers for a 100% markup in February. The customers will pay in March. What is the Revenue, Income and Cash flow for Jim's Specialty Cheese in **February**?

	Revenue	Income	Cash flow
a)	800	400	800
b)	0	800	0
c)	400	400	400
d)	800	400	-800

Answer: d

Cost of Goods Sold = 50% x \$800 = \$400

Revenue = \$400 + (\$400 x 100%) = \$800

Income = \$800 - \$400 = \$400

Cash flow = -\$800 (cash from customers is not received until March, but supplier must be paid in February)

12. According to the study.net reading “A Funny Thing Happened on the Way to the Stock Market Record” what is the “core problem” identified by forecaster David Levy?

- A. Household and corporate balance sheets have gotten too big
- B. Inflation has risen too high in the US
- C. Interest rates are too high in Europe
- D. Investors refuse to buy risky “Covenant lite” loans

Answer: A. “The core problem, Levy says, is that household and business balance sheets have gotten too big” (about 60% through the reading). This was noted in the lecture 7A slide 28 and mentioned in lecture 8. All the other options are the reverse of the truth, for example the reading refers to a “deflationary profile”, “rates (falling) below zero in Europe” and to US “investors snapping up risky “Covenant lite” loans.

13) A company is about to start trading. The company's owners invested \$10,000 total into company equity, but also secured bank funding for the company so that its total assets stand at \$17,000. What is the amount of the **liabilities** of this company?

- A) \$3,000
- B) \$7,000
- C) \$13,500
- D) \$27,000

Answer: B

Calculation: The accounting equation states that $A=L+SE \Rightarrow L = A-SE = \$17,000-\$10,000$

Personal Financial Planning

14) For a typical person in the economy, what is the most important source of income that has to be managed most of all?

- A) Common stock investments
- B) Investments in Treasury Bonds
- C) Investments in Foreign Securities and Commodities
- D) The person’s Human Capital

ANSWER: D see lecture 7 slide 5

15) What have been the changes in retirement schemes in the last 20-30 years?

- a) Increasing proportion of defined benefit schemes
- b) Increasing proportion of defined contribution schemes
- c) Increasing number of employers offering defined benefit schemes
- d) Increased importance of making sure to cash out your retirement scheme when leaving an employer

Answer: B (see lecture 7, slide 8)

16) Which of the following types of retirement schemes provides the employee with a specified pension payment which is **not** dependent on the employee’s investment selections, provided the sponsor of the retirement scheme remains in business?

- A) Defined benefit
- B) Defined contribution
- C) 401K
- D) IRA

Answer: A

Explanation: see lec 7 slides 11-12. This is a description of a defined benefit scheme, whereas in defined contribution, the eventual benefit depends on the employees’ investment amounts and fund selections. C and D are types of defined contribution schemes.

17) Which of the following investment tactics is most likely to enhance the investor's net returns, irrespective of market movements?

- A) Investing a higher proportion in stocks
- B) Investing a higher proportion in bonds
- C) Investing a higher proportion with professionally managed mutual funds that have expensive marketing campaigns
- D) Selecting low cost funds with low fees

Answer: D

Explanation: The key words in this question are "irrespective of market movements". The selection of stocks vs bonds is important, but the effect of this decision on investor net returns **does** depend on market movements so alternatives A and B are incorrect. As noted in lecture 7 slide 24, 80% of professionally managed funds underperform the market and, again, their performance depends on the market, eliminating choice C. D is correct as lower fees save the investor money whether the market is up or down. Although stocks have returned more than bonds over the very long term, bonds can triumph over periods as long as 10 years, for example between early 2000 and end 2009. Even within this period, however, low fee funds would have enhanced the investors' net returns compared to high fee funds, irrespective of the investors choice of investments.

18) The FDIC insures bank deposits up to \$250,000 per depositor, per insured bank. Lady Margaret Hatt is a wealthy individual who has \$250,000 in a checking account at Wells Fargo and \$500,000 in a checking account at Chase Bank. She also has a savings account at Chase Bank with \$200,000 in it. What total dollar amount is insured by the FDIC?

- a) \$250,000
- b) \$500,000
- c) \$700,000
- d) \$750,000

Answer: B

Explanation: The FDIC adds together all of the accounts that Lady Hatt has at each bank, and insures the first \$0.25m at each bank. Thus, the full \$250K at Wells is insured, but only the first \$250K at Chase.

19) In investor psychology, which is the system whose visceral reactions can interfere with effective investing?

- A) System 1
- B) System 2
- C) System 3
- D) System 4

Answer: A, see lecture 7 slide 21

20) In 2002 the rate of exchange for one euro was \$0.87 and in February 2020 it is \$1.09. Which group of people would have **most benefited** from this change in exchange rates?

- a) French vacationers visiting the US
- b) French hotel owners
- c) US vacationers visiting France
- d) French exporters selling goods into the US

Answer: A

Explanation: The Euro became much more valuable so French holidaymakers could convert their holiday money into more dollars to pay for hotels, attractions and meals in dollars. US vacationers in France suffered the reverse effect. French exporters' product becomes more expensive for people spending dollars. The effect on French innkeepers is less marked, but they

have more difficulty attracting US and other non-Eurozone tourists, so they are somewhat disadvantaged. See page 95.

Financial Statement and ratio analysis:

Use the following information on RyanStone Incorporated to answer the next **three** questions

Average stockholders' equity	\$16,000	Net income	\$ 4,000
Average total assets	\$20,000	Sales	\$40,000
Current assets	\$8,000	Total liabilities	\$ 4,000
Current liabilities	\$2,000		

21) What is the Profit margin for Ryanstone Inc?

- a) 10% b) 15% c) 20% d) 25%

Answer: A

Explanation: $PM = \text{net income}/\text{sales} = 4000/40000 = 10\%$, see HBS reading and lecture

22) What is the Return on Equity for Ryanstone Inc?

- a) 10% b) 15% c) 20% d) 25%

Answer: d

Explanation: $RoE = \text{net income}/\text{stockholders equity} = 4/16 = 25\%$

23) What is the term for the first sale of a company's stock or common shares to the public?

- A) Venture capital
B) Secondary market
C) Initial Public Offering
D) Angel investment

Answer: C

Explanation: Venture capital and angel investments are not available to the general public. The secondary market describes trading of shares after the Initial public offering (IPO). See also lecture 2 and page 131.

24) Which of the following exists when an industry or market has only one producer?

- A) competition
B) oligopoly
C) monopoly
D) communism
E) socialism

Answer: C

Explanation: C) A monopoly is a market or industry in which there is only one producer that supplies a certain product. Monopolies in the United States economy are either discouraged or regulated so that prices are not too high. See custom text page 20

25) Which of the following is the best description of **current assets** in a company's balance sheet?

- a) All assets the company has right now, i.e. currently
- b) Assets the company expects to use or convert to cash within one month or less
- c) Assets the company expects to use or convert into cash within one year
- d) Assets such as property, equipment and goodwill

Answer: C

Explanation: See custom text page 49

26) A person invests \$200 for 2 years while the prevailing interest rate is 10%. The future value of the investment is closest to....

- a) \$250
- b) \$242
- c) \$200
- d) \$165

Answer: b

Calculation: $FV = PV \times (1+r)^t = 200 \times 1.1^2 = \242

27) Which of the following is NOT part of the M-1 money supply?

- A) Currency at hand
- B) Currency available through a debit card
- C) Currency in checking accounts
- D) Currency value of time deposits

Answer: D

28) What is the term for buying several different investments rather than just one?

- A) Spreading
- B) Shorting
- C) Margin buying
- D) Diversification
- E) Management

Answer: D

29) Danville Corporation Inc has a current stock price of \$90, annual earnings per share of \$6 and annual dividends per share of \$3. What is Danville's **price earnings ratio**?

- a) 5
- b) 10
- c) 15
- d) 30

Answer: C

Explanation: PE ratio is price divided by earnings = $\$90/\$6 = 15$ times

30) Which of the following terms refers to the examination of a company's accounting system to determine whether its financial reports fairly represent its operations?

- A) Company-wide analysis
- B) Forensic accounting
- C) Portfolio analysis
- D) Audit

Answer: D

See custom text page 42

31) Which of the following is **most reflective** of the history of the development of money according to lecture?

- A) Familial/tribal relationships → Precious metal money → Debt/duty based relationships
- B) Debt/duty based relationships → Familial/tribal relationships → Precious metal money
- C) Familial/tribal relationships → Debt/duty based relationships → Precious metal money
- D) Precious metal money → Familial/tribal relationships → Debt/duty based relationships

Answer: C see lecture 5 slide 8

32) Which is the correct formula for **dividend yield**?

- A) earnings per share multiplied by shares outstanding
- B) earnings per share divided by stock price
- C) annual dividends per share divided by stock price
- D) dividends per share divided by earnings per share

Answer: C, see lectures 2 and 7A.

33) The most recent estimate of the US unemployment rate is closest to....

- A) 0.5%
- B) 3.5%
- C) 6.5%
- D) 9.5%

Answer: B Lecture 1 homework and lecture 5 slide 13

34) Looking at the balance sheets of Microsoft and Apple, what is one weakness that we can identify?

- A) Large proportion of cash and marketable securities, which produce low returns
- B) Large proportion of intangible assets, which have no value
- C) Large proportion of fixed expenses
- D) Large proportion of variable expenses

Answer: A

Explanation: Discussed in lecture 7A and 8. Intangible assets (B) (such as brand or goodwill) can have value in generating future revenues. C and D refer to expenses, which is related to the income statement.

35) Which of the following federal laws made transactions between banks significantly more efficient?

- A) the Check Clearing for the 21st Century Act
- B) the Bank Secrecy Act
- C) the USA Patriot Act
- D) the Federal Reserve Act
- E) the Economic Emergency Recovery Act

Answer: A

Explanation: A) It made electronic clearing of checks legal. See page 92 and lecture 6

36) Which of the following would be an example of a non-deposit institution?

- A) Insurance company
- B) Mutual Savings Bank
- C) Commercial Bank
- D) Credit Union

Answer : A

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Explanation: Insurance companies do not take deposits, but they do participate in the financial system by insuring against risks, and by investing insurance premia to enhance profits and therefore offer lower fees. See custom text page 82.

37. I have carefully checked my Scantron. My section number and name are correctly shown
a. Yes

38. Depends on version.