

NAME: _____

BEM 103 QUIZ 10

1. *Stockholders who want management to work hard might increase leverage because*
 - A. If profits do not improve, bankruptcy will force management out**
 - B. Returns will go up because debt is cheaper than equity
 - C. They can use the borrowed money for a stock-buy back
 - D. They can hedge the leverage with put options

2. *When management receives options as incentive to increase profits*
 - A. Management then implements the shareholders' preferred plan
 - B. The incentives only work if the options are in the money
 - C. Management also has the incentive to increase risk taking**
 - D. The incentives are strongest if the strike price is low

3. *When choosing a set of projects to undertake a firm should*
 - A. Make sure the least profitable project has a return above the cost of debt
 - B. Make sure the least profitable project has a return above the marginal cost of capital**
 - C. Make sure the projects are all in the same research area
 - D. Make sure the projects all mature at the same time

4. *Why might large (old/well established) firms prefer to fund new ventures with debt rather than equity?_____Full credit for **Either β is large because the firms are large and procyclical.***

OR

Well established firms have assets they can pledge so they have access to cheap capital