

## Economics 252 – Financial Markets

Spring 2011

Lecture 8: Corporate Stocks

February 14, 2011

Multiple Choice Questions

### **Question 9.1**

According to data from the World Bank about the value of corporate stock as traded on stock markets, which country's or which region's stock market has the highest absolute value as of 2008?

- (a) Japan.
- (b) United Kingdom.
- (c) United States of America.
- (d) Euro-area, i.e. the countries whose currency is the euro.

### **Question 9.2**

What was the main point that Eugene Fama and Kenneth French made in their article in the Journal of Financial Economics from 2005 about Stuart Myers's Pecking Order Theory?

- (a) The Pecking Order Theory by Myers emphasizes a subordinate role of equity issuance, as compared to other forms of corporate financing. However, Myers only considered net equity issuance, whereas Fama and French looked at equity issuances and stock repurchases separately, disproving the subordinate role of equity issuance.
- (b) The Pecking Order Theory by Myers states that firms do not issue any dividends. Fama and French, in their more recent analysis, establish that firms started to issue dividends again.
- (c) Myers finds evidence contrary to the Capital Asset Pricing Model, whereas Fama and French confirm the Capital Asset Pricing Model.
- (d) The article by Fama and French does not address Pecking Order Theory at all.

## **Question 9.3**

What is a company's market capitalization, as explained in the lecture?

- (a) It is the company's assets minus its liabilities.
- (b) It is the number of the outstanding shares of the company multiplied by the stock price.
- (c) It is the value of the company's capitalization assets?
- (d) It is a synonym for the share repurchases that the company has undertaken in the past fiscal year.

## **Question 9.4**

When General Motors got into a crisis in 2009, the U.S. government bailed it out. Through which channel of financing did the bailout proceed?

- (a) The U.S. government guaranteed bank loans to General Motors.
- (b) The U.S. government bought preferred shares in General Motors.
- (c) The U.S. government bought common shares in General Motors.
- (d) The U.S. government bought General Motors bonds?

## **Question 9.5**

What are the main implications of John Lintner's dividend model?

- (a) A firm should never pay any dividends.
- (b) A firm should always pay a dividend equal to its EPS (earnings per share).
- (c) A firm has to strike a balance. On the one hand, it should pay a dividend to share some of its earnings with its shareholders. On the other hand, its dividend should not be too high, because that might lead to a cut in the dividend in a following year, which leads to a negative reaction among shareholders.
- (d) If EPS is bigger than last year's dividend, the firm should pay out the difference as a dividend. If EPS is smaller than last year's dividend, the firm should engage in share repurchases.

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## **Correct Answers**

9.1: (c)

9.2: (a)

9.3: (b)

9.4: (b)

9.5: (c)