

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 150 points (to be scaled up to 210 points) and is scheduled to take 75 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I can give extra time but not much.

For all calculator questions, tell me what you typed into the calculator.

1) (4 points each) Define THREE of the following terms.

- A) short position on a futures contract
- B) tick size
- C) a price quote on a Treasury future of 113 010 for a bond with a face value of \$100,000.
- D) dual banking system
- E) negotiable CDs
- F) non-current loans

2) (4 points each) Define THREE of the following terms.

- A) FHA loan
- B) reverse annuity mortgage
- C) balloon payment
- D) flash trading
- E) underwriters' spread
- F) proxy vote

3) (10 points) Answer EITHER Part A OR Part B.

- A) Suppose the spot exchange rate is ¥100/\$ and over time changes to \$.02/¥. For both currencies, tell me if they appreciated, depreciated, revalued, or devalued. Explain your logic and show all work.
- B) Suppose the following exchange rates exist. \$.01/¥ and £.6/\$. Then, what is $S_{GB/J}$? (¥ is the symbol for the Japanese yen and £ is the symbol for the British pound.) Show all work and explain what you did.

4) (10 points) Answer EITHER Part A OR Part B.

- A) We have discussed several different stock indices like, NYSE Composite, NASDAQ Composite, Dow Jones, Wilshire 5000, and S & P 500. Why do we need so many different indices? Make sure you explain in general how they are different.
- B) Which is less risky for a underwriter, an IPO or a seasoned offering? Explain your logic defining both terms.

5) (12 points) Answer EITHER Part A OR Part B.

- A) Is the equation for interest rate parity between the US and Japan $1 + i_{us,t} = (1/S_{US/J,t})(1 + i_{J,t})(F_{US/J,t})$ or is it $1 + i_{US,t} = (S_{US/J,t})(1 + i_{J,t})(1/F_{US/J,t})$? Explain your logic.
- B) Explain absolute purchasing power parity (absolute PPP). State what it says and explain why it may hold.

6) (14 points) Answer EITHER Part A OR Part B.

A) Suppose you were going to take a 30-year conventional mortgage at 9% which will fully amortize the debt. How much would your annual payment be? If they offered to reduce the interest rate to 8% if you paid 3 discount points, would it be worthwhile to take the offer? Explain your logic.

B) Suppose the largest monthly mortgage payment you could afford was \$1000. If the current interest rate was 6%, what is the largest 30-year conventional mortgage you can afford? What is the largest 15-year mortgage you could afford?

7) (14 points) Answer EITHER Part A OR Part B.

A) What are TWO of the differences between *preferred stocks* and *common stocks*? Which would you prefer to have if you thought the company was going to do extremely well? Explain your logic.

B) Explain what is meant by a *shelf registration* of a stock. Explain why a firm might want to do that.

8) (16 points) Answer EITHER Part A OR Part B.

A) What is meant by a fully amortizing ARM? What is the advantage (for you) of that over a conventional mortgage? What is the disadvantage of taking out the ARM?

B) How did Fannie Mae contribute to the financial meltdown in 2008? Should it be eliminated? Explain your logic.

9) (16 points) Answer EITHER Part A OR Part B.

A) Draw the diagram for the intrinsic value and the price of a put option with an exercise price of \$8/share. Explain how you determined where the two lines are.

B) Draw the potential payoff for the issuer of a put option with an exercise price of \$20/share and an option price of \$1.20. Explain how you determined what the line looks like. What is the issuer hoping will happen to the stock price? Explain your logic.

10) (16 points) For EITHER *interest rate swap* OR *currency swap*, define what it is. Also explain why each party would want to participate in the swap. Be specific about what is being swapped and why.

11) (18 points) Answer EITHER Part A OR Part B.

A) Which do you think would be more relevant to how profitable a firm is now, the *interest rate spread* or the *net interest margin*? Explain your logic making sure you define both terms.

B) What was the TARP program? What was the big problem with it?