1) The results of the dividend growth model: 1) _______
A) are most reliable when the growth rate exceeds 10 percent.
B) are highly dependent upon the beta used in the model.
C) are sensitive to the rate of dividend growth.
D) vary directly with the market rate of return.
E) can only be applied to projects that have a growth rate equal to that of the current firm.

2) All else constant, an increase in a firm's cost of debt: 2) _______
A) will lower the firm's cost of equity.
B) will increase the firm's capital structure weight of debt.
C) will result in an increase in the firm's cost of capital.
D) could be caused by an increase in the firm's tax rate.
E) will lower the firm's weighted average cost of capital.

3) A firm has a cost of equity of 13 percent, a cost of preferred of 11 percent, an aftertax cost of debt of 5.2 percent, and a tax rate of 35 percent. Given this, which one of the following will increase the firm's weighted average cost of capital? 3) _______
A) Increasing the firm's beta B) Increasing the firm's tax rate
C) Issuing new bonds at par D) Increasing the debt-equity ratio

4) Which one of the following will increase the cost of equity, all else held constant? 4) _______
A) Increase in stock price B) Increase in the dividend growth rate
C) Decrease in beta D) Decrease in market risk premium

5) Judy's Boutique just paid an annual dividend of $1.48 on its common stock and increases its dividend by 2.2 percent annually. What is the rate of return on this stock if the current stock price is $29.60 a share? 5) _______
A) 8.37 percent B) 8.33 percent C) 7.31 percent D) 8.19 percent

6) Musical Charts just paid an annual dividend of $1.84 per share. This dividend is expected to increase by 2.1 percent annually. Currently, the firm has a beta of 1.12 and a stock price of $31 a share. The risk-free rate is 4.3 percent and the market rate of return is 13.2 percent. What is the cost of equity capital for this firm? 6) _______
A) 11.95 percent B) 11.21 percent
C) 12.29 percent D) 13.42 percent

7) Titans has 7 percent bonds outstanding that mature in 16 years. The bonds pay interest semiannually and have a face value of $1,000. Currently, the bonds are selling for $1,015 each. What is the firm's pretax cost of debt? 7) _______
A) 7.14 percent B) 6.40 percent C) 6.97 percent D) 6.84 percent

8) Electronic Products has 22,500 bonds outstanding that are currently quoted at 101.6. The bonds mature in 8 years and pay an annual coupon payment of $90. What is the firm's aftertax cost of debt if the applicable tax rate is 34 percent? 8) _______
A) 4.79 percent B) 5.75 percent C) 5.47 percent D) 6.98 percent

9) The Five and Dime Store has a cost of equity of 14.8 percent, a pretax cost of debt of 6.7 percent, and a tax rate of 34 percent. What is the firm's weighted average cost of capital if the debt-equity ratio is .46? 9) _______
A) 10.18 percent B) 14.93 percent C) 11.53 percent D) 13.49 percent

10) Holiday Decor is an all-equity firm with a total market value of $347,000 and 12,000 shares of stock outstanding. Management is considering issuing $48,000 of debt at an interest rate of 7 percent and using the proceeds on a stock repurchase. As an all-equity firm, management believes its earnings before interest and taxes (EBIT) will be $33,000 if the economy is normal, $8,000 if it is in a recession, and $41,000 if the economy booms. Ignore taxes. What will the EPS be if the economy falls into a recession and the firm maintains its all-equity status? 10) ______

A) $.67 B) $1.33 C) $.75 D) $1.50 E) $1.21

11) A firm has fixed operating costs of $175,000, total sales revenue of $3,000,000 and total variable costs of $2,250,000. The firm's degree of operating leverage is ________. 11) ______

A) 0.81 B) 4.29 C) 0.77 D) 1.30

12) ________ is the potential use of fixed operating costs to magnify the effects of changes in sales on earnings before interest and taxes. 12) ______

A) Ratio analysis
B) Financial leverage
C) Operating budget
D) Operating leverage

13) A firm has fixed operating costs of $650,000, a sales price per unit of $20, and a variable cost per unit of $13. At a base sales level of 500,000 units, the firm's degree of operating leverage is _______. 13) ______

A) 1.11 B) 1.18 C) 1.23 D) 1.07

14) The market rate of return is 11.8 percent and the risk-free rate is 3.45 percent. Galaxy Co. has 36 percent more systematic risk than the overall market and has a dividend growth rate of 3.5 percent. The firm's stock is currently selling for $42 a share and has a dividend yield of 2.8 percent. What is the firm's cost of equity? 14) ______

A) 10.55 percent B) 19.82 percent C) 21.11 percent D) 15.31 percent

15) Bird Houses is an all-equity firm with a total market value of $388,980 and 18,000 shares of stock outstanding. Management is considering issuing $68,000 of debt at an interest rate of 6.5 percent and using the proceeds on a stock repurchase. Ignore taxes. How many shares will the firm repurchase if it issues the debt securities? (Round the number of shares repurchased down to the nearest whole share.) 15) ______

A) 3,146 shares B) 3,167 shares C) 3,207 shares D) 3,116 shares

Answer Key
Testname: 12-13PRACTICEPROBLEMSCHAPTERS12,13

1) C
2) C
3) A
4) B
5) C
6) B
7) D
8) B
9) C
10) A
11) D
12) D
13) C
14) A
15) A