Stock Market Game Test

A test of basic economic concepts and institutions related to saving, investing, risk, the stock market, and productivity

1. A personal investment such as purchasing stocks or corporate bonds should be made once the return on the investment is expected to be:

   a. Greater than the interest rate on federally insured savings accounts or on government bonds.
   b. The same as the interest rate on federally insured savings accounts or on government bonds.
   c. Greater than zero but less than the interest rate on federally insured savings accounts or on government bonds.
   d. Positive—that is, greater than zero.

2. You bought 100 shares of stock at $20 each. At the end of the year, you received a total of $400 in dividends, and the market value of your stock was $2,500. Your total annual rate of return was:

   a. 90 %
   b. 50 %
   c. 45 %
   d. 20 %

3. Capital gains are earned whenever:

   a. Companies must pay federal and state taxes on the profits they have earned.
   b. Assets such as stocks are sold at prices greater than their purchase price.
   c. A stock pays dividends.
   d. A stock splits.

4. Economists assume that they typical individual investor in common stocks is:

   a. Wealthy.
   b. Risk averse.
   c. A speculator or gambler.
   d. Risk seeking or at least risk neutral.

5. Which of the following groups usually bears the greatest cost if a firm declares bankruptcy and goes out of business?

   a. The firm’s managers.
   b. The firm’s suppliers.
   c. The firm’s bondholders.
   d. The firm’s stockholders.

6. Which of the following statements about the efficient market hypothesis is true?

    a. The rate of return of stocks with a given risk profile is always changing, and never in equilibrium.
    b. Stock prices will not change as a result of unexpected events affecting a company's sales, production costs, and earnings.
    c. The equilibrium rate of return is paid on all stocks, given their different risk characteristics, so all investors will earn the same amount of money on their investments.
    d. On average, a portfolio of stocks picked by throwing darts at a listing of all stocks will do just as well as a portfolio picked by experts who work for the leading brokerage houses.

7. Information about a new issue of common stock by a corporation, including the size of the issue and how these funds will be used by the firm, is provided to potential investors in a document known as a:

    a. Prospectus.
    b. Letter of commitment.
    c. Registration statement.
    d. Tombstone advertisement.

8. Risk-return management means that:

    a. Individuals and firms should avoid all risks.
    b. Low but safe earnings are better than high but risky earnings.
    c. Individuals and firms should choose the investments that have the highest possible returns.
    d. There is an appropriate trade-off between risk and return that is different for different people and firms depending on their investment objectives.

9. To maximize its stock holders' wealth, a corporation should:

    a. Use advertisements to make its brand names more widely known by consumers.
    b. Increase the overall value of the firm as much as possible.
    c. Maximize the firm's short-run economic profits.
    d. Pay out all of its profits as dividends.

10. Insider trading occurs when:

    a. The managers or members of the Board of Directors of a company buy more stock in the firm.
    b. Lawyers and investment bankers buy or sell common stock in the companies their firms represent.
    c. A company's common stock is purchased by competing firms, in violation of federal antitrust laws.
    d. Anyone with information that is not available to the public at large uses that information to make money by buying and selling stocks.

11. A firm's retained earnings belong to the firm's:

    a. Common stockholders.
    b. Preferred stockholders.
    c. Bondholders.
    d. Suppliers.

12. A guaranteed payment of $100 to be received one year from today is worth:

    a. Less than a guaranteed payment of $100 to be received two years from today.
    b. More than a guaranteed payment of $100 to be received two years from today.
    c. Exactly the same amount as a guaranteed payment of $100 to be received two years from today.
    d. We cannot determine whether the payment will be worth more, less, or the same as an identical payment to be received two years from today—that depends on too many other things.

13. Other things being equal, increases in the interest rate will:

    a. Raise the price of corporate bonds.
    b. Raise the price of preferred stocks.
    c. Lower the price of common stocks.
    d. Lower the payments on savings account at commercial banks.

14. If people who invest in the stock market become more risk averse:

    a. A smaller financial return will be required to make investors accept risks.
    b. Companies will find it a good time to offer new issues of stocks and bonds.
    c. The price of stocks and bonds will fall in order to increase the expected rate of return.
    d. Funds deposited in savings accounts in commercial banks will shrink, while investments in common stocks increase.

15. Rank the following four projects from the least to the most risky, for most U.S. firms:

1. Introducing an entirely new product in U.S Markets.
2. Introducing an entirely new product in the countries of the former Soviet bloc.
3. Expanding a current product line in existing markets.
4. Repairing machinery at a current production site or factory.

    a. 4, 3, 1, 2
    b. 4, 3, 2, 1
    c. 1, 2, 3, 4
    d. 1, 2, 4, 3

16. New issues of common stock released by large corporations are usually underwritten and sold to the public by:

    a. The New York and American Stock Exchanges.
    b. The corporations that issue the stock.
    c. Investment bankers.
    d. Commercial bankers.

17. The value of the best alternative forgone whenever an economic choice is made, including the choice to buy a stock or bond, is known as the:

    a. Price.
    b. Resource cost.
    c. Opportunity cost.
    d. Cost of production.

18. Which of the following is considered an economic factor of production (i.e. productive resource)?

    a. Labor.
    b. Money.
    c. Government bonds.
    d. A firm's common stock.

19. Which of the following would definitely increase the price of the common stock for a company that has its stock traded on the New York Stock Exchange?

    a. A decrease in both the supply or and demand for the stock.
    b. An increase in both the supply of and demand for the stock.
    c. And increase in the supply of and a decrease in the demand for the stock.
    d. An increase in the demand for and a decrease in the supply of the stock.

20. Other things being equal, as the price of a share of common stock in the XYZ Company decreases:

    a. The supply of the stock will decrease.
    b. The demand for the stock will increase.
    c. Sellers will offer more shares of the stock for sale.
    d. Buyers will want to buy more shares of stock in XYZ Company.

21. Other things being equal, an increase in savings by households will:

    a. Increase the interest rate and increase investment spending.
    b. Increase the interest rate and decrease investment spending.
    c. Decrease the interest rate and decrease investment spending.
    d. Decrease the interest rate and increase investment spending.

22. A secondary financial market is one where:

    a. New government bonds are sold.
    b. New issues of common stocks are bought and sold.
    c. Existing securities such as stocks and bonds are bought and sold.
    d. Securities such as stocks and bonds are purchased and retired by the firms or governments that issued them.

23. Other things being equal, household savings increase as interest rates rise because:

    a. Companies reduce investment spending as interest rates rise.
    b. The government tries to borrow more money at higher interest rates.
    c. People reduce current consumption when higher interest rates reward them for doing so.
    d. The Federal Reserve is trying to increase income and consumption spending by raising interest rates.

24. The main difference between common stocks and bonds is that:

    a. Stocks sometimes pay out at a fixed rate of interest, but bonds don't.
    b. Stocks are not a contractual promise to pay a specific amount of money in the future; bonds are.
    c. Bonds are only issued by government agencies, while stocks are issued by private companies.
    d. Changes in a corporation's expected earnings (profits) will lead to changes in its bond prices, but not its stock prices.

25. The main economic role of profits is to:

    a. Compensate owners of land and other natural resources for using up those nonrenewable resources.
    b. Signal owners of firms where to direct resources to satisfy consumers' demands.
    c. Provide income to pay salaries to a firm's managers.
    d. Provide income to pay wages to a firm's employees.

26. The difference between accounting profits and economic profits is:

    a. There is no difference—they are the same thing.
    b. Economic profits cannot be earned in the long run, but accounting profits can.
    c. Accounting profits are the difference between revenues and explicit costs; economic profits are the difference between revenues and opportunity costs.
    d. Both use the same measure of total costs, but accounting profits only count revenues that have been received, while economic profits also add accounts receivable.

27. The major sources of long-run productivity growth in the U.S economy over the last century have included all of the following *EXCEPT*:

    a. Technological change.
    b. Rising rates of public and private savings.
    c. Better education and training or workers.
    d. Investments in capital goods, such as factories and machines.

28. What person or organization sets monetary policy and tries to control the overall availability of credit in the U.S.?

    a. The Federal Reserve.
    b. The U.S. Treasury.
    c. The Congress.
    d. The President.

29. An increase in which of the following would be most likely to increase wages for U.S. workers?

    a. Productivity.
    b. Stock prices.
    c. Interest rates.
    d. Business inventories.

30. As a return on investment, or stockholder's equity, the average rate of profits for U.S corporations is usually:

    a. 1 – 9 %
    b. 10 – 20 %
    c. 21 – 40 %
    d. 41 – 60 %

Note: This test was prepared by Michael Watts, Professor of Economics and Director of the Center for Economic Education at Purdue University.