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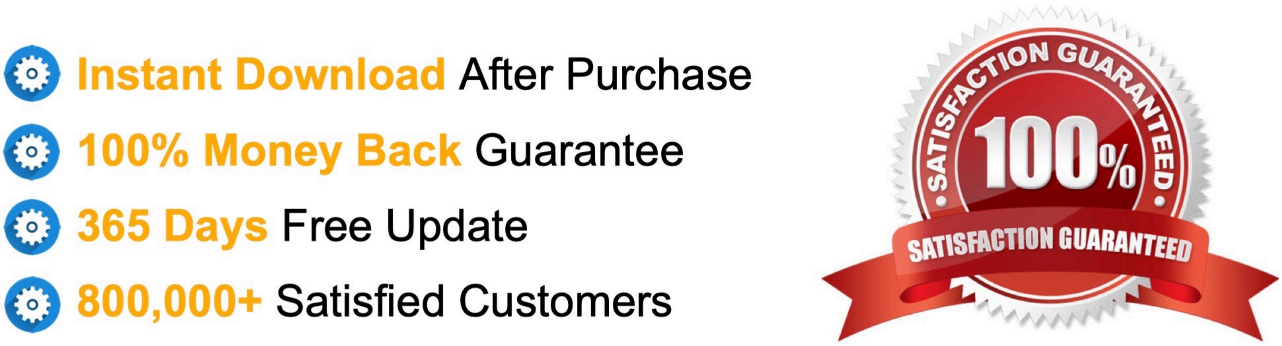

QUESTION 1

Gleason Co. has two products, a frozen dessert and ready-to-bake breakfast rolls, ready for introduction. However, plant capacity is limited, and only one product can be introduced at present. Therefore, Gleason has conducted a market study, at a cost of $26,000, to determine which product will be more profitable. The results of the study follow.

Sales of Desserts at $1.80/unit		Sales of Rolls at $1.20/unit	
Volume	Probability	Volume	Probability
250,000	.30	200,000	.20
300,000	.40	250,000	.50
350,000	.20	300,000	.20
400,000	.10	350,000	.10

*Gleason treats production tooling as a current operating expense rather than capitalizing it as a fixed asset. The expected value of Gleason\\'s operating profit directly traceable to the sale of frozen desserts is

A. $198,250

B. $150,250

C. $120,250

D. Some amount other than those given.

Correct Answer: C

The expected volume for sales of frozen desserts is 305,000 [(250000 x .30) + (300000 x 40) + (350,000 x .20) + (400 .000 x .10)]. At $1 .80 each1 the total revenue from 305,000 units would be $549,000. Variable costs would total $1.15 each ($40 + $35 + $40), or $350750 for 305.000 units. Fixed costs total $78,000 ($48,000 + $30000). Thus, operating profit would be $120,250 ($549,000 --$350,750-$78,000).

QUESTION 2

What return on equity do investors seem to expect for a firm with a $50 share price, an expected dividend of $5.50, of 9, and a constant growth rate of 4.5%?

A. 15.05%

B. 15.50%

C. 15.95%

D. 16.72%

Correct Answer: B

Dividing the $5.50 dividend by the $50 share price produces an 11% dividend yield. Adding the 11% yield to the 4.5% growth rate produces a total return of 15.5%.

QUESTION 3

Which one of the following is true regarding a relevant range?

A. Total variable costs will not change.

B. Total fixed costs will not change.

C. Actual fixed costs usually fall outside the relevant range.

D. The relevant range cannot be changed after being established.

Correct Answer: B

The relevant range is the range of activity over which unit variable costs and total fixed costs are constant. The incremental cost of one additional unit of production will be equal to the variable cost.

QUESTION 4

Future1 Inc. is in the enviable situation of having unlimited capital funds. The best decision rule, in an economic sense, for it to follow would be to invest in all projects in which the

A. Accounting rate of return is greater than the earnings as a percent of sales.

B. Payback reciprocal is greater than the internal rate of return.

C. Internal rate of return is greater than zero.

D. Net present value is greater than zero.

Correct Answer: D

Given unlimited funds1 all projects with a net present value greater than zero should be invested in. Thus, it would be profitable to invest in any company where the rate of return is greater than the cost of capital.

QUESTION 5

A consultant recommends that a company hold funds for the following two reasons:

Reason #1: Cash needs can fluctuate substantially throughout the year. Reason #2: Opportunities for

buying at a discount may appear during the year.

	Reason #1	Reason #2
A.	Speculative balances	Speculative balances
B.	Speculative balances	Precautionary balances
C.	Precautionary balances	Speculative balances
D.	Precautionary balances	Precautionary balances

A. Option A

B. Option B

C. Option C

D. Option D

Correct Answer: C

The three motives for holding cash are as a medium of exchange, as a precautionary measure, and for speculation. Reason #1 can be classified as a precautionary measure, and Reason #2 can be classified as holding cash for speculation.