***Financial Markets and Institutions, 7e* (Saunders)**

**Chapter 5 Money Markets**

1) Everything else equal, an effective annual rate will be greater than the bond equivalent yield on the same security.

2) Money markets exist to help reduce the opportunity cost of holding cash balances.

3) The majority of money market securities are low-denomination, low-risk investments designed to appeal to individual investors with excess cash.

4) Commercial paper is a short-term obligation of the U.S. government issued to cover government budget deficits and to refinance maturing government debt.

5) Commercial paper, Treasury bills, and banker's acceptance rates are all quoted as discount yields.

6) Euro commercial paper is a short-term obligation of the European Central Bank.

7) The U.S. Treasury switched from a discriminating price auction to a single price auction because the latter lowered the average price paid by investors.

8) In the T-bill secondary market the ask yield will normally be less than the bid yield.

9) The largest secondary money market in the United States is the secondary market for T-bills.

10) Fed funds are short-term unsecured loans while repos are short-term secured loans.

11) 360/*n* times the difference between the face value and the current value divided by the face value gives you the discount yield on an instrument.

12) The bond equivalent yield times 365/360 is equal to the single payment yield.

13) LIBOR is the rate that would be charged when banks borrow from other banks in Eurodollar market.

14) Maturities on Eurodollar CDs are usually more than one year.

15) In general, the federal funds rate is slightly lower than the LIBOR.

16) For the purposes for which they are used, money market securities should have which of the following characteristics?

I.  Low trading costs

II.  Little price risk

III.  High rate of return

IV.  Life greater than one year

A) I and III

B) II and IV

C) III and IV

D) I and II

E) I, II, and III

17) Money market securities exhibit which of the following?

I.  Large denomination

II.  Maturity greater than one year

III.  Low default risk

IV. Contractually determined cash flows

A) I, II, and III

B) I, III, and IV

C) II, III, and IV

D) II and IV

E) I, II, III, and IV

18) A repo is in essence a collateralized

A) banker's acceptance.

B) certificate of deposit.

C) Fed funds loan.

D) commercial paper loan.

E) Eurodollar deposit.

19) A short-term unsecured promissory note issued by a company is

A) commercial paper.

B) a T-bill.

C) a repurchase agreement.

D) a negotiable CD.

E) a banker's acceptance.

20) A time draft payable to a seller of goods with payment guaranteed by a bank is a

A) commercial paper security.

B) T-bill.

C) repurchase agreement.

D) negotiable CD.

E) banker's acceptance.

21) In the T-bill auction process, the competitive bidder is guaranteed a \_\_\_\_\_\_\_\_ and a noncompetitive bidder is guaranteed a \_\_\_\_\_\_\_\_.

A) minimum price; maximum price.

B) maximum price; minimum price.

C) maximum price; given quantity.

D) minimum price; maximum quantity.

E) None of these choices are correct.

22) A dealer is quoting a $10,000 face 180-day T-bill quoted at 2.75 bid, 2.65 ask. You could buy this bill at \_\_\_\_\_\_\_\_ or sell it at \_\_\_\_\_\_\_\_.

A) $9,869.23; $9,864.36.

B) $9,864.36; $9,869.23.

C) $9,867.50; $9,862.50.

D) $9,862.50; $9,867.50.

E) None of these choices are correct.

23) Rates on federal funds and repurchase agreements are stated

A) on a bond equivalent basis with a 360-day year.

B) on a bond equivalent basis with a 365-day year.

C) as a discount yield with a 360-day year.

D) as an EAR.

E) as a discount yield with a 365-day year.

24) The discount yield on a T-bill differs from the T-bill's bond equivalent yield (BEY) because

I. the discount yield is the return per dollar of face value and the BEY is a return per dollar originally invested.

II. a 360-day year is used on the discount yield and the BEY uses 365 days.

III. the discount yield is calculated without compounding, and the BEY is calculated with compounding.

A) I only

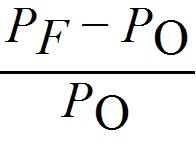
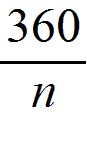
B) II only

C) I and II only

D) II and III only

E) I, II, and III

25) The following formula is used to calculate the \_\_\_\_\_\_\_\_ of a money market investment.

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A) EAR

B) APR

C) single-payment yield

D) discount yield

E) BEY

26) The rate of return on a repo is

A) determined by the rate of return on the underlying collateral.

B) strongly affected by the current Fed funds rate at the time of the repo.

C) determined at the time of the repo.

D) determined by the rate of return on the underlying collateral and determined at the time of the repo.

E) strongly affected by the current Fed funds rate at the time of the repo and determined at the time of the repo.

27) Which one of the following statements about commercial paper is *not* true? Commercial paper issued in the United States

A) is an unsecured short-term promissory note.

B) has a maximum maturity of 270 days.

C) is virtually always rated by at least one ratings agency.

D) has no secondary market.

E) carries an interest rate above the prime rate.

28) A negotiable CD

A) is a bank-issued transactions deposit.

B) is a registered instrument.

C) is a bank-issued time deposit.

D) has denominations ranging from $50,000 to $10 million.

E) pays discount interest.

29) A 180-day $3 million CD has a 4.25 percent annual rate quote. If you buy the CD, how much will you collect in 180 days?

A) $3,047,439

B) $3,045.678

C) $3,062,877

D) $3,063,750

E) $3,127,500

30) A banker's acceptance is

A) a time draft drawn on the exporter's bank.

B) a method to help importers evaluate the creditworthiness of exporters.

C) a liability of the importer and the importer's bank.

D) an add-on instrument.

E) for greater than one year maturity.

31) The most liquid of the money market securities are

A) commercial paper.

B) banker's acceptances.

C) T-bills.

D) Fed funds.

E) repurchase agreements.

32) In dollars outstanding in 2016, the largest money market security was

A) commercial paper.

B) banker's acceptances.

C) T-bills.

D) Fed funds and repos.

33) You buy a $10,000 par Treasury bill at $9,575 and sell it 60 days later for $9,675. What was your EAR?

A) 4.44 percent

B) 6.29 percent

C) 6.35 percent

D) 6.52 percent

E) 6.67 percent

34) LIBOR is generally \_\_\_\_\_\_\_\_ the Fed funds rate because foreign bank deposits are generally \_\_\_\_\_\_\_\_ than domestic bank deposits.

A) greater than; less risky

B) less than; more risky

C) the same as; equally risk

D) greater than; more risky

E) less than; less risky

35) A U.S. exporter sells $150,000 of furniture to a Latin American importer. The exporter requires the importer to obtain a letter of credit. When the bank accepts the draft, the exporter discounts the 120-day note at a 5.25 percent discount. What is the exporter's true effective annual financing cost?

A) 5.52 percent

B) 5.42 percent

C) 5.34 percent

D) 5.29 percent

E) 5.25 percent

36) A Chinese exporter sells $200,000 of toys to a French importer. The Chinese exporter requires the French importer to obtain a letter of credit. When the bank accepts the draft, the exporter discounts the 90-day note at a 4 percent discount. What is the exporter's true effective annual financing cost?

A) 4.00 percent

B) 4.04 percent

C) 4.10 percent

D) 4.16 percent

E) 4.22 percent

37) If a $10,000 par T-bill has a 3.75 percent discount quote and a 90-day maturity, what is the price of the T-bill to the nearest dollar?

A) $9,625.

B) $9,906.

C) $9,908.

D) $9,627.

E) None of these choices are correct.

38) A 90-day T-bill is selling for $9,900. The par is $10,000. The effective annual return on the T-bill is (watch your rounding)

A) 4.00 percent.

B) 4.16 percent.

C) 4.10 percent.

D) 4.04 percent.

E) 4.21 percent.

39) Suppose that $10 million face value commercial paper with a 270-day maturity is selling for $9.55 million. What is the BEY on the paper?

A) 4.71 percent

B) 6.42 percent

C) 6.37 percent

D) 6.28 percent

E) 4.50 percent

40) A $2 million jumbo CD is paying a quoted 3.55 percent interest rate on 180-day maturity CDs. How much money will you have at maturity if you invest in the CD?

A) $2,000,000

B) $2,035,014

C) $2,035,500

D) $2,071,000

E) $2,088,400

41) From 1990 to 2016, which one of the following money market securities actually declined in terms of dollar amount outstanding?

A) Commercial paper

B) Treasury bills

C) Federal funds and repos

D) Negotiable CDs

E) Banker's acceptances

42) A 50-day maturity money market security has a bond equivalent yield of 3.60 percent. The security's EAR is

A) 3.69 percent.

B) 3.61 percent.

C) 3.55 percent.

D) 3.87 percent.

E) 3.66 percent.

43) In a Treasury auction, preferential bidding status is granted to

A) competitive bidders.

B) noncompetitive bidders.

C) short sale committed bidders.

D) commercial bank bidders.

E) no group of bidders.

44) If your firm enters into an overnight reverse repurchase agreement, your firm is

A) borrowing Fed funds temporarily.

B) selling a security now while agreeing to buy it back tomorrow.

C) giving an unsecured loan to the counterparty.

D) procuring a banker's acceptance.

E) None of these choices are correct.

45) Eurodollar CDs would include

A) CDs denominated in Euros.

B) dollar investments by European entities in the United States.

C) dollars deposited in Caribbean banks.

D) dollars deposited in Europe.

E) dollars deposited in Caribbean banks and dollars deposited in Europe.

46) Which of the following descriptions does not apply to money market securities?

A) Short-term

B) Low-risk

C) Highly liquid

D) Long maturity

E) High denominations

47) The most active and important participant in the U.S. money market

A) is the U.S. Treasury.

B) are the large banks.

C) are the investment banks.

D) are the insurance companies.

E) is the Federal Reserve.

48) The most significant borrower in the U.S. money markets?

A) Are commercial banks

B) Are large corporations

C) Is the U.S. Treasury

D) Are the investment banks

E) Are the insurance companies

49) A noncompetitive bid for Treasury bill auction provides

A) all noncompetitive bidders the same price.

B) all competitive bidders the same price.

C) all noncompetitive bidders the same quantity.

D) all noncompetitive bidders lesser price than the competitive bidders.

E) all competitive bidders the same quantity.

50) What is the price of 182-day money market security with face value of $7,000 if the BEY is 3.574%?

A) $6,877.44

B) $6,925.48

C) $6,634.47

D) $6,725.36

E) $6,452.39

51) Why do most money market securities have large denominations?

52) Given the functions of the money markets, why is it necessary for money market securities to have a maturity of one year or less and low default risk?

53) What is the difference between a discriminating auction and a single price auction? How is the final price determined in a single price auction? Why did the Treasury switch to a single price auction?

54) A government securities dealer needs to make a 7 percent pretax annual return on $10 million of capital employed to make it worthwhile to make a market in T-bills. If the bid discount on $10,000 face value 90-day T-bills is 3.50 percent, and the dealer can expect to do 5,200 round trip deals today, what must the ask discount be? Hint: A round trip is a buy and a sell transaction.

55) How does a repo differ from a Fed funds transaction? How do their rates compare?

56) As a corporate treasurer who is unsure how soon funds will be needed, which type of money market investment might you prefer? Explain the trade-offs. Would your answer differ if you had a definite time period during which you would not need the money? Explain.

57) A corporate treasurer is looking to invest about $4 million for 60 days. Commercial paper rates are a 3.65 percent discount and CD rates are 3.66 percent. Comparing the bond equivalent yields over a 365-day year, which is the best alternative? What is the opportunity cost of leaving the funds idle? (Watch your rounding.)

58) How does a banker's acceptance (BA) help create more international trade?

59) Who are the major participants in money markets?

60) One-hundred-eighty-day commercial paper can be bought at a 3.75 percent discount. What are the bond equivalent yield and the effective annual rate on the commercial paper? Why do these rates differ?

61) You are a corporate treasurer for Esso Oil. The quoted rate on dollar-denominated euro commercial paper has just blipped down recently. Your firm can issue $10 million of 180-day euro commercial paper in the London markets at 3.45 percent. You can also invest the proceeds in the United States in comparable maturity negotiable dollar-denominated CDs, which are quoting 3.95 percent. Ignoring any transactions costs, how much money, if any, can Esso make by borrowing in the euro markets and investing in the United States? Is this a good deal or not? Should you expect it to last? Explain.