Future Business Leaders of America (FBLA) Securities and Investments Practice Test (Sample)

Study Guide

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Questions

1. **Which rate is charged by the Federal Reserve to member banks?**
   - **A. Prime rate**
   - **B. Discount rate**
   - **C. Fed funds rate**
   - **D. T-bill rate**

2. **What is the investment objective focused on current income through fixed income securities called?**
   - **A. Capital appreciation**
   - **B. Growth**
   - **C. Income**
   - **D. Speculation**

3. **Which factor is NOT considered in sustainable investing?**
   - **A. Corporate governance practices**
   - **B. Environmental impact of investments**
   - **C. Short-term market fluctuations**
   - **D. Social responsibility of companies**

4. **What is the primary purpose of the Securities and Exchange Commission (SEC)?**
   - **A. To regulate and oversee securities markets and protect investors**
   - **B. To provide investment advice to individual investors**
   - **C. To facilitate mergers and acquisitions**
   - **D. To promote international trade agreements**

5. **What does T + 3 signify in trading?**
   - **A. The settlement occurs two days after the trade date**
   - **B. The settlement occurs on the trade date**
   - **C. The settlement occurs three business days after the trade date**
   - **D. The settlement occurs one day after the trade date**

6. What does an indication of interest signify?

- **A. A commitment to purchase securities immediately**
- **B. An investor's expression of interest in a new issue**
- **C. A formal offer for purchasing shares**
- **D. A professional endorsement of the security**

7. What type of offering allows underwriters to purchase shares that are not subscribed to in a rights offering?

- **A. Standby offering**
- **B. Private placement**
- **C. Auction market**
- **D. Best efforts**

8. What distinguishes a general obligation bond from other bonds?

- **A. It is backed by the project's revenue**
- **B. It is backed by the issuer's full faith and credit**
- **C. It must be paid back in a specified timeframe**
- **D. It has a variable interest rate**

9. What is NOT a function of the Federal Reserve?

- **A. Conducting monetary policy**
- **B. Regulating commercial banking**
- **C. Setting tax rates**
- **D. Providing financial services to the government**

10. How do interest rates typically affect bond prices?

- **A. When interest rates rise, bond prices also rise**
- **B. When interest rates fall, bond prices typically fall**
- **C. When interest rates rise, bond prices typically fall**
- **D. Interest rates have no effect on bond prices**

Answers

1. B
2. C
3. C
4. A
5. C
6. B
7. A
8. B
9. C
10. C

Explanations

1. Which rate is charged by the Federal Reserve to member banks?

A. Prime rate

B. Discount rate

C. Fed funds rate

D. T-bill rate

The correct answer is the discount rate, which is the interest rate charged by the Federal Reserve to member banks for short-term loans. This rate is a key tool used by the Federal Reserve to influence monetary policy and manage the economy. By adjusting the discount rate, the Fed can either encourage or discourage borrowing by banks, which in turn affects the availability of credit in the economy. When the discount rate is lowered, it becomes cheaper for banks to borrow money, which can stimulate lending to businesses and consumers, ultimately spurring economic growth. Conversely, raising the discount rate makes borrowing more expensive, which can help to cool off an overheated economy or control inflation. The other rates mentioned, like the prime rate, reflect the interest that banks charge their best customers and are influenced by the discount rate but are not directly set by the Federal Reserve. The federal funds rate is the interest rate at which banks lend to each other overnight and is also influenced by the Fed's monetary policy but is not the rate charged directly by the Federal Reserve to member banks. T-bill rates pertain to Treasury bills and represent the return on short-term government debt securities, which are unrelated to the lending practices of the Federal Reserve.

2. What is the investment objective focused on current income through fixed income securities called?

A. Capital appreciation

B. Growth

C. Income

D. Speculation

The investment objective focused on current income through fixed income securities is known as "income." This strategy is geared towards generating a steady stream of income, often through investments like bonds or dividend-paying stocks. Investors who select this approach typically prioritize receiving regular cash flows over increasing the value of their initial investment. Income-focused investments provide a predictable return that can be especially appealing to those in or nearing retirement who require consistent cash flow to meet living expenses. This objective contrasts with capital appreciation, which aims for an increase in the value of investments over time, and growth, which emphasizes investing in assets expected to increase in value. Additionally, speculation involves taking significant risk in hopes of achieving high returns, usually through short-term investments or trading strategies, which is quite different from the income-focused approach that seeks stability and predictability.

3. Which factor is NOT considered in sustainable investing?

- A. Corporate governance practices
- B. Environmental impact of investments
- C. Short-term market fluctuations
- D. Social responsibility of companies

Sustainable investing focuses on incorporating environmental, social, and governance (ESG) factors into investment decisions to promote long-term sustainability while seeking financial returns. The correct answer highlights that short-term market fluctuations do not align with the principles of sustainable investing. In sustainable investing, factors such as corporate governance practices, environmental impact, and social responsibility are all crucial considerations. These elements play significant roles in evaluating how a company's operations affect society and the environment, which influences investor decisions aimed at promoting ethical and responsible business practices. Sustainable investors typically prioritize long-term performance and stability over reactionary moves to short-term market changes, which do not reflect the fundamental values of sustainability. Thus, while short-term market fluctuations may impact individual investments temporarily, they are not a key focus in the broader context of sustainable investing, which seeks to foster enduring positive impacts on society and the environment.

4. What is the primary purpose of the Securities and Exchange Commission (SEC)?

- A. To regulate and oversee securities markets and protect investors
- B. To provide investment advice to individual investors
- C. To facilitate mergers and acquisitions
- D. To promote international trade agreements

The primary purpose of the Securities and Exchange Commission (SEC) is to regulate and oversee securities markets and protect investors. Established in response to the stock market crash of 1929, the SEC's mission is fundamentally about maintaining fair, orderly, and efficient markets. It aims to promote trust in the financial systems by requiring full disclosure of important financial information, thereby allowing investors to make informed decisions. The SEC enforces securities laws to prevent fraud and manipulation in the stock and securities markets, ensuring that all investors have access to the same critical information. This regulatory oversight also includes the registration of securities offerings, monitoring of trading practices, and enforcement of compliance with applicable laws. Focusing on the other options, while providing investment advice (the second option) might be beneficial for investors, it falls outside the SEC's role, which is more about regulation than advisory services. Facilitating mergers and acquisitions (the third option) is typically the domain of corporate finance professionals and regulatory bodies focused on antitrust laws rather than the SEC's core responsibilities. Promoting international trade agreements (the fourth option) is more aligned with governmental trade agencies and departments focused on international relations rather than the SEC’s mission. Therefore, the correct answer accurately captures the essence of the SEC’s primary role

5. What does T + 3 signify in trading?

A. The settlement occurs two days after the trade date

B. The settlement occurs on the trade date

C. The settlement occurs three business days after the trade date

D. The settlement occurs one day after the trade date

T + 3 refers to the settlement of a securities transaction, indicating that the settlement occurs three business days after the trade date. In the context of trading, the "T" stands for the trade date, which is the day when the transaction is executed. The "+3" denotes the additional three business days required to finalize the transaction, which includes the transfer of securities from the seller to the buyer and the corresponding exchange of funds. This three-day settlement period was traditionally used for most securities transactions and provided a time buffer for various administrative processes. Understanding this concept is crucial for investors and traders, as it affects liquidity, cash flow management, and transaction timing in the securities market. The shift to a T + 2 settlement cycle for most securities in recent years reflects the industry's effort to streamline processes and reduce credit risk. However, T + 3 remains relevant in certain contexts and historical discussions. Other answers misconstrue the definition of the T + number framework by suggesting shorter settlement periods or same-day settlements, which do not reflect the standard practices for securities settlements.

6. What does an indication of interest signify?

A. A commitment to purchase securities immediately

B. An investor's expression of interest in a new issue

C. A formal offer for purchasing shares

D. A professional endorsement of the security

An indication of interest signifies an investor’s expression of interest in a new issue. This term is commonly used in the context of initial public offerings (IPOs) or other new securities offerings. When investors indicate interest, they are essentially communicating their intent to consider purchasing the securities once they become available, but it does not constitute a binding agreement or commitment to purchase. This expression of interest allows underwriters and issuers to gauge demand for the security before the formal offering takes place, which can be crucial for pricing and structuring the offering. Investors can show this interest typically during a roadshow or preliminary offering period, where they provide feedback to the company on potential pricing and volume without making a definitive purchase commitment.

7. What type of offering allows underwriters to purchase shares that are not subscribed to in a rights offering?

A. Standby offering

B. Private placement

C. Auction market

D. Best efforts

A standby offering is a type of rights offering where underwriters agree to purchase any shares that remain unsubscribed after the existing shareholders have had the opportunity to buy additional shares at a discounted price. This arrangement is beneficial because it ensures that the issuing company will be able to raise the necessary funds, as the underwriters take on the risk of buying any leftover shares not taken up by current shareholders. In contrast, a private placement involves selling securities directly to a select group of investors, which does not offer any subscription rights to existing shareholders. An auction market features a system where buyers and sellers compete for securities, rather than a structured rights offering. Lastly, a best efforts arrangement involves underwriters agreeing to sell as much of the offering as possible but do not guarantee the full amount will be sold and do not purchase leftover shares, making it distinct from a standby offering.

8. What distinguishes a general obligation bond from other bonds?

A. It is backed by the project's revenue

B. It is backed by the issuer's full faith and credit

C. It must be paid back in a specified timeframe

D. It has a variable interest rate

A general obligation bond is characterized by being backed by the issuer's full faith and credit, which means that the issuing authority pledges its taxing power to repay bondholders. This type of bond is generally issued by municipalities or government entities to fund public projects, such as schools or infrastructure. The issuer commits to using tax revenues to ensure that bondholders are repaid, making these bonds particularly secure for investors. The backing of full faith and credit implies a strong assurance of repayment, differentiating it from revenue bonds, which rely solely on the income generated from specific projects or revenue sources. In contrast, the other choices are not accurate representations of general obligation bonds. For instance, bonds backed by a project's revenue refer to revenue bonds, which depend on the income generated from the financed project rather than the general taxing power of the issuer. Specified repayment timeframes may apply to numerous types of bonds, not uniquely to general obligation bonds, and variable interest rates can apply to various bond types, including some general obligation bonds, but they are not a defining characteristic. Thus, the unique feature of general obligation bonds lies in their backing by the issuer's full faith and credit, making them a secure investment option.

9. What is NOT a function of the Federal Reserve?

A. Conducting monetary policy

B. Regulating commercial banking

C. Setting tax rates

D. Providing financial services to the government

The option that identifies a role that is not a function of the Federal Reserve is setting tax rates. The Federal Reserve primarily focuses on monetary policy, which includes managing interest rates and controlling the money supply to achieve economic stability and growth. Additionally, the Federal Reserve plays a crucial role in regulating commercial banking to ensure the stability of the financial system and protect depositors' interests. It also provides financial services to the government, such as managing the Treasury's accounts and facilitating payments. However, the setting of tax rates falls under the jurisdiction of the U.S. Congress and the Department of the Treasury, which is responsible for tax policy and revenue generation for the federal government. This clear delineation of responsibilities underscores why setting tax rates is not within the Federal Reserve's functions.

10. How do interest rates typically affect bond prices?

A. When interest rates rise, bond prices also rise

B. When interest rates fall, bond prices typically fall

C. When interest rates rise, bond prices typically fall

D. Interest rates have no effect on bond prices

When interest rates rise, bond prices typically fall because of the inverse relationship that exists between interest rates and bond prices. This phenomenon occurs due to the fixed nature of bond coupon payments. When new bonds are issued at higher interest rates, existing bonds with lower rates become less attractive to investors. As a result, the prices of these older bonds decrease so that their yields align more closely with the market rates. Essentially, investors require a discount on existing bonds to compensate for the lower interest payments compared to newly issued bonds offering higher returns. This dynamic is a fundamental concept in the bond market, demonstrating how external economic factors influence investment values. Understanding this relationship is crucial for making informed investment decisions regarding bonds.