

INVESTMENT BANKING BASICS PRACTICE TEST (SAMPLE)

STUDY GUIDE



SAMPLE STUDY GUIDE WITH LIMITED QUESTIONS

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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 – 45 minutes). Review a handful of questions, reflect on the explanations.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning. Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly, adapt the tips above to fit your pace and learning style. You've got this!

Questions

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- 1. In simplifying the enterprise value calculation, replacing debt with net debt and removing the subtraction of cash implies what?**
 - A. Cash is already accounted for within net debt
 - B. Cash is ignored completely
 - C. Debt increases by cash
 - D. EV becomes meaningless
- 2. What does Funds From Operations (FFO) for REITs do with depreciation and gains on sale?**
 - A. FFO adds back depreciation and subtracts gains on sale of properties
 - B. FFO subtracts depreciation and adds gains
 - C. FFO ignores depreciation and gains
 - D. FFO is net income
- 3. Which item is excluded from EBITDA?**
 - A. Depreciation
 - B. Revenue
 - C. Operating expenses
 - D. Sales discounts
- 4. Which order of valuation methods is described as highest to lowest in the material?**
 - A. Precedent transactions, DCF, Market comps, Market valuation
 - B. Market comps, DCF, Precedent transactions, Market valuation
 - C. DCF, Precedent transactions, Market valuation, Market comps
 - D. Market valuation, Market comps, DCF, Precedent transactions
- 5. Which valuation method is used to determine how much a private equity firm could pay and set a floor on valuation?**
 - A. LBO Analysis
 - B. Liquidation Valuation
 - C. Replacement Value
 - D. Future Share Price Analysis

- 6. How would you determine how much debt can be raised and how many tranches there would be in an LBO?**
- A. Use only internal projections to determine debt.
 - B. Review comparable LBOs and examine their debt terms and tranching for similar size and industry.
 - C. Debt amount is irrelevant to LBO.
 - D. Assume the maximum debt lenders will allow.
- 7. Rank the 3 valuation methodologies from highest to lowest expected value.**
- A. There is no fixed ranking; Precedent Transactions often exceed Comparable Companies due to the control premium; DCF is most variable.
 - B. Precedent Transactions are always the highest; DCF always the lowest.
 - C. DCF is always the highest value.
 - D. Comparable Companies are always the highest value.
- 8. What does the PV of cash flows equal when discounted by the WACC in a DCF?**
- A. Equity Value
 - B. Enterprise Value
 - C. Net Present Value
 - D. Market Capitalization
- 9. How are convertible bonds treated in computing diluted shares when determining Equity Value?**
- A. Convertibles are counted using the Treasury Stock Method.
 - B. Convertible bonds are ignored.
 - C. If in-the-money, count as equity; if out-of-the-money, treat as debt.
 - D. Convertibles are always counted as cash.
- 10. In building a merger model, which items are typically assumed at Step 1?**
- A. The combined company's post-merger tax rate
 - B. The purchase price and whether the deal is funded by cash, stock, or debt
 - C. The target's long-term growth rate
 - D. The regulatory environment

Answers

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

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Explanations

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1. In simplifying the enterprise value calculation, replacing debt with net debt and removing the subtraction of cash implies what?

A. Cash is already accounted for within net debt

- B. Cash is ignored completely
- C. Debt increases by cash
- D. EV becomes meaningless

The idea is that cash and debt are combined in one number called net debt. Net debt equals total debt minus cash. So when you use net debt in the enterprise value calculation, you've already baked cash into that figure. If you also drop the separate cash subtraction, you're not ignoring cash; you're relying on net debt to reflect cash's impact. For example, with debt of 100 and cash of 20, net debt is 80. Using equity value plus net debt gives equity value plus 80, which matches the result you'd get from equity value plus debt (100) minus cash (20). So cash is already accounted for within net debt.

2. What does Funds From Operations (FFO) for REITs do with depreciation and gains on sale?

A. FFO adds back depreciation and subtracts gains on sale of properties

- B. FFO subtracts depreciation and adds gains
- C. FFO ignores depreciation and gains
- D. FFO is net income

Funds From Operations (FFO) for REITs focuses on recurring operating performance by adjusting GAAP net income for items that distort true cash generation. Depreciation is a non-cash charge that lowers net income but does not affect cash, so FFO adds it back. Gains on the sale of properties come from transactions rather than ongoing operations, so FFO subtracts those gains to avoid inflating earnings from one-time events. This combination shows a clearer picture of how the REIT's core real estate operations are actually performing, though FFO is not the same as cash flow from operations or net income.

3. Which item is excluded from EBITDA?

A. Depreciation

- B. Revenue
- C. Operating expenses
- D. Sales discounts

EBITDA shows earnings before interest, taxes, depreciation, and amortization, so it removes non-cash charges to focus on cash earnings from operations. Depreciation is excluded because it's a non-cash expense used for allocating asset costs over time; EBITDA adds back depreciation to EBIT to reflect cash profitability. Revenue, operating expenses, and even sales discounts all figure into the earnings measure that EBITDA starts from, with depreciation and amortization the only adjustments made back.

4. Which order of valuation methods is described as highest to lowest in the material?

- A. Precedent transactions, DCF, Market comps, Market valuation**
- B. Market comps, DCF, Precedent transactions, Market valuation
- C. DCF, Precedent transactions, Market valuation, Market comps
- D. Market valuation, Market comps, DCF, Precedent transactions

In valuation, some methods tend to produce higher estimates because they embed premiums and strategic value seen in actual deals, while others reflect market pricing or intrinsic cash-flow assumptions. Precedent transactions pull prices paid in real deals for similar companies, which include control premiums and potential synergies. That makes these values typically the highest. The DCF approach builds value from a company's own projected cash flows discounted to present value; it is powerful and disciplined, but it hinges on the assumptions used (growth, margins, discount rate), so it sits below the premium-rich transaction valuations. Market comps rely on multiples from publicly traded peers; they reflect current investor sentiment and liquidity but exclude any control premium, so these valuations are usually lower than precedent deals and often higher than plain market pricing depending on conditions. Market valuation, the current market price for the company, captures what the market is willing to pay right now and generally represents the lowest end of this spectrum because it doesn't include the uplift from a completed acquisition or the company-specific strategic value assumed in other methods.

5. Which valuation method is used to determine how much a private equity firm could pay and set a floor on valuation?

- A. LBO Analysis**
- B. Liquidation Valuation
- C. Replacement Value
- D. Future Share Price Analysis

Leveraged Buyout analysis is what PE firms use to figure out how much they could justify paying for a target and to anchor a floor on valuation by tying price to financing constraints and required returns. In an LBO model, you forecast the target's cash flows, build a highly leveraged capital structure (debt and equity), and model an exit scenario. By setting a target equity return (and often an exit multiple), you determine the highest enterprise value that still allows debt to be serviced and the sponsor to achieve the minimum return. That implied price ceiling effectively sets the practical floor for what the firm would consider paying today—the deal must be financed cleanly and meet return hurdles, or it isn't attractive. Other methods aren't designed to capture how much leverage and return targets constrain purchase price: liquidation valuation focuses on asset-at-sale recoveries, replacement value on asset replacement costs, and futures based on public stock prices apply to public companies rather than private, highly levered deals.

6. How would you determine how much debt can be raised and how many tranches there would be in an LBO?

- A. Use only internal projections to determine debt.
- B. Review comparable LBOs and examine their debt terms and tranching for similar size and industry.**
- C. Debt amount is irrelevant to LBO.
- D. Assume the maximum debt lenders will allow.

In an LBO, how much debt you can raise and how many debt tranches you include depends on current market terms and lender appetite. The most reliable way to gauge this is to look at comparable LBOs that are similar in size and industry and study their debt terms, including the total leverage and the mix of debt tranches (senior secured loans, revolvers, mezzanine, etc.). This market-based benchmarking shows what lenders are actually willing to finance under present conditions and helps you set a realistic, lender-friendly capital structure with appropriate covenants and amortization. Relying only on internal projections misses how lenders price risk and structure terms, and assuming you can push to the maximum debt lenders will allow tends to be overly aggressive and risky in downside scenarios. By reviewing comps, you can identify typical leverage ranges and tranche structures for deals like yours, then tailor your model to those realities.

7. Rank the 3 valuation methodologies from highest to lowest expected value.

- A. There is no fixed ranking; Precedent Transactions often exceed Comparable Companies due to the control premium; DCF is most variable.**
- B. Precedent Transactions are always the highest; DCF always the lowest.
- C. DCF is always the highest value.
- D. Comparable Companies are always the highest value.

The key idea is how these three valuation methods typically align in terms of the value they imply for a target. Precedent Transactions use actual deal prices paid for similar companies and inherently include the control premium that buyers are willing to pay to take control. That added premium often pushes the valuation above what you'd derive from Comparable Companies, which are based on current market multiples for similar firms but don't reflect a buyer's premium in a specific deal. DCF, on the other hand, hinges on the projections of future cash flows and the assumptions used for discounting (like the discount rate and terminal value). Those inputs can vary a lot, so the DCF result can swing higher or lower and is generally the most variable among the three. Because of that, there isn't a fixed ranking from highest to lowest. Precedent Transactions often come out higher than Comparable Companies due to the control premium, while the DCF can be anywhere along the spectrum depending on the assumptions. The important takeaway is to recognize why each method tends to push valuations in different directions and why bankers rely on a range rather than a single number.

8. What does the PV of cash flows equal when discounted by the WACC in a DCF?

- A. Equity Value
- B. Enterprise Value**
- C. Net Present Value
- D. Market Capitalization

In a DCF, the present value of unlevered cash flows (cash flows available to all providers of capital) discounted at the weighted average cost of capital represents the value of the firm's operations—the enterprise value. WACC is the blended required return for both debt and equity after tax, so discounting FCFF at this rate captures the cost of financing the entire business. This PV reflects the value of the company's assets regardless of how it's financed. To get equity value, you would subtract net debt from enterprise value; market capitalization is the equity value for a public company. Net present value is a separate concept used for evaluating specific projects.

9. How are convertible bonds treated in computing diluted shares when determining Equity Value?

- A. Convertibles are counted using the Treasury Stock Method.
- B. Convertible bonds are ignored.
- C. If in-the-money, count as equity; if out-of-the-money, treat as debt.**
- D. Convertibles are always counted as cash.

When computing diluted Equity Value, the key idea is whether converting the instrument would actually dilute shareholders. A convertible bond is counted as equity only if converting it would increase the number of shares outstanding in a way that people would implement it—the in-the-money situation. In that case, you add the potential shares from conversion to the equity base. If converting isn't advantageous (out-of-the-money), holders wouldn't convert, so there's no dilution and the instrument stays as debt in the calculation. This is why counting convertibles as equity only when they're in-the-money, and treating them as debt otherwise, is the correct approach. For context, the treasury stock method is a different technique used mainly for options and warrants, not convertibles, which is why it isn't applicable here.

10. In building a merger model, which items are typically assumed at Step 1?

- A. The combined company's post-merger tax rate
- B. The purchase price and whether the deal is funded by cash, stock, or debt**
- C. The target's long-term growth rate
- D. The regulatory environment

Starting point in a merger model is defining the deal terms: how much is being paid to acquire the target and how that payment is funded (cash, stock, or debt). This is the essential driver because it sets the sources and uses of funds, determines the change in the buyer's cash and debt, and can affect shares outstanding if stock is used. Once you know the purchase price and financing mix, you can map out the balance sheet impact, calculate goodwill, and lay the groundwork for how interest, dilution, and integration effects will flow through the model. Other inputs like the post-merger tax rate, long-term growth assumptions, or the regulatory environment influence projections later, after the basic deal structure is set. The Step 1 focus on price and financing captures the core economics that everything else is built around.

Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

<https://investmentbankingbasics.examzify.com>

We wish you the very best on your exam journey. You've got this!

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