

Personal Finance IQ Multiple Choice Test

Using economic reasoning and holding all else constant, identify the correct answer to each multiple choice question.

1. The widespread financial insecurity of Americans is primarily because
 - a. the incomes of Americans are low.
 - b. most Americans save a very high proportion of their income.
 - c. government programs are unavailable to help people when they are disabled or experience unemployment.
 - d. the saving rate of Americans is low and many borrow in order to spend more than they earn.

2. Tax-deferred investment plans
 - a. decrease your taxable income, and thereby reduce your current tax liability.
 - b. make it more difficult for people to save and accumulate wealth.
 - c. increase your current tax liability so you can pay lower taxes in the future.
 - d. help individuals with the lowest incomes, but they are of little value to those with the highest incomes who want to save for retirement.

3. A monthly budget can help you achieve financial security by
 - a. helping you choose stocks that are most likely to increase in price.
 - b. reducing the likelihood that you will face unexpected expenditures for maintenance and repairs.
 - c. expanding the borrowing limits on your existing credit cards and increasing the number of credit cards you hold.
 - d. increasing your financial awareness and helping you allocate your funds more effectively.

4. Which of the following is the best place to set funds aside for “surprise” expenditures?
 - a. The stock market.
 - b. Your regular checking account.
 - c. A savings account.
 - d. Ownership of real estate.

5. Funds invested for a newborn child’s college education would be best placed in:
 - a. an indexed equity mutual fund.
 - b. a savings account.
 - c. a checking account.
 - d. a U.S. Treasury bond.

6. A prudent person is most likely to find the use of financing attractive when purchasing which one of the following items?
 - a. Entertainment
 - b. Clothes
 - c. Rental housing
 - d. A college education

7. Who is most likely to face the highest finance charges?
 - a. An employed individual who makes timely payments.
 - b. A person who pays off a credit card balance each month.
 - c. A person with a bad credit history and a lot of debt.
 - d. A customer who pays bills online.

8. Which of the following makes it easy for anyone to benefit from the diversified ownership of American corporations?
 - a. Money market mutual funds.
 - b. Equity mutual funds.
 - c. Corporate bond mutual funds.
 - d. Interest earning checking accounts.

9. Which of the following outstanding debts would be most prudent to pay off first?
 - a. \$5000 borrowed from your parents at a 0 interest rate.
 - b. A \$2000 debt on a credit card charging an 18 percent annual interest rate.
 - c. A home equity loan of \$10000 which has an effective interest rate of 6 percent.
 - d. A student loan of \$40,000 with a fixed interest rate of 4 percent.

10. People with coffee habits spend about \$4 a day. If a 7% return can be earned, the cost of this coffee habit over a 50 year period would be:
 - a. Nothing.
 - b. \$1,460.
 - c. \$73,000.
 - d. \$ 443,918.

11. Should you accept your employer's offer to match eligible earnings used to purchase company stock?
 - a. Yes, you should purchase the company stock and hold onto it for as long as possible.
 - b. Probably, the matching of your contributions makes it attractive, but if you buy the company stock you should sell it when permitted to do so in order to keep your portfolio diversified.
 - c. No, you should not participate. The company is merely trying to take advantage of you.
 - d. No. It never makes sense to buy the stock of the company for which you work.

12. Personal financial success is primarily the result of
 - a. generous welfare and unemployment programs.
 - b. spending more than you earn.
 - c. doing what you are passionate about regardless of whether others value it.
 - d. providing services others value while working hard to achieve financial goals.

13. If you are using a credit card prudently, you should
 - a. make only the minimum payment each month.
 - b. pay the balance in full each month.
 - c. pay only the interest on any outstanding balance.
 - d. gradually expand the amount borrowed to the card's credit limit.

14. Which of the following will help you generate income and accumulate wealth?
 - a. Getting another credit card so you will have more borrowing power in the future.
 - b. Borrowing funds in order to increase your current consumption .
 - c. Allocating funds regularly into savings and investments.
 - d. Making only the minimum monthly payment on your outstanding credit card balances.

15. A couple that is currently renting but is contemplating a move to another city in the near future should
 - a. buy if they can arrange a monthly mortgage payment less than their current rent.
 - b. buy because real estate will always increase in value.
 - c. continue renting because real estate is illiquid and costly to buy and sell.
 - d. continue renting because rental payments are tax-deductible but mortgage interest payments are not.

16. Historically, which of the following has yielded the highest rate of return when held over a long period of time?
- A diverse holding of corporate bonds.
 - A diverse holding of common stocks.
 - Money market mutual funds.
 - U.S. Treasury bonds.
17. Diversification of one's stock portfolio is important because
- it reduces the likelihood of a dramatic change in value over a relatively short period of time.
 - it will always yield a higher rate of return than a narrow group of related stock investments.
 - the dividends of a diversified stock portfolio are guaranteed.
 - the initial funds used to purchase the stocks will always be returned to the investor.
18. A monthly budget is an effective tool that will help you
- spend a larger share of your earnings now.
 - manage your spending and save for the future in order to accumulate wealth.
 - keep your transportation costs low by purchasing a new car every two or three years.
 - select stocks that are more likely to increase in value over the long run.
19. It is costly to purchase a new car every two or three years because
- the maintenance cost of a new car is generally higher than for a used one.
 - the financing cost is significantly higher for a new car than for a used one.
 - a new car will depreciate rapidly in value during the first few years of use.
 - the taxes for the fuel of a new car are generally higher than for a used one.
20. Compared to managed equity funds, indexed equity mutual funds generally yield a
- lower return because the indexed funds spend more on research and stock trading, and therefore have higher administrative costs than managed funds.
 - higher return because the indexed funds spend less on research and stock trading, and therefore have lower administrative costs than managed funds.
 - lower return because the managed funds have more profitable companies in their portfolio.
 - higher return because the indexed funds are tied to the consumer price index, which assures that their value will always keep up with the inflation rate.