

Multinational Business Finance, 13e (Eiteman/Stonehill/Moffett)

Chapter 2 Corporate Ownership, Goals, and Governance

2.1 Who Owns the Business?

Multiple Choice

1) Foreign stock markets are frequently characterized by controlling shareholders for the individual publicly traded firms. Which of the following is NOT identified by the authors as typical controlling shareholders?

- A) the government (for example, privatized utilities)
- B) institutions (such as banks in Germany)
- C) family (such as in France)
- D) All of the above were identified by the authors as controlling shareholders.

Answer: D

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

2) Which of the following is NOT typically associated with the *public ownership* of business organizations?

- A) the state
- B) the government
- C) families
- D) civil society

Answer: C

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

3) Which of the following is NOT typically associated with the *private ownership* of business organizations?

- A) the government
- B) families
- C) individuals
- D) publicly traded, widely-held organizations

Answer: A

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

4) *State Owned Enterprises* (SOEs):

- A) are a form of public ownership.
- B) are created for commercial activities rather than civil or social activities.
- C) are the dominant form of business organization in some countries.
- D) are all of the above.

Answer: D

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

5) The problems that may arise due to the separation of ownership and management in large business organizations is know as:

- A) separation anxiety.
- B) the agency problem.
- C) corporate disconnect theory.
- D) none of the above

Answer: B

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Conceptual

6) Privatization is a term used to describe:

- A) firms that are purchased by the government.
- B) government operations that are purchased by corporations and other investors.
- C) firms that do not use publicly available debt.
- D) non-public meetings held by members of interlocking directorates.

Answer: B

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

True/False

1) In the U.S. and U.K. stock markets are characterized by ownership of firms concentrated in the hands of a few controlling shareholders. In contrast, the rest of the world tends to have more widespread ownership of shares.

Answer: FALSE

Comment: Just the opposite is true. In the U.S. and U.K. ownership is more widespread than in the rest of the world, and management tends to own only a small portion of the firm.

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

2) *State Owned Enterprises (SOEs)* by their very name cannot be traded on stock exchanges because they are government owned.

Answer: FALSE

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Conceptual

3) In recent years the trend has been for markets to increasing focus on the shareholder wealth form of wealth maximization.

Answer: TRUE

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

4) Non-Anglo-American markets are dominated by the "one-vote-one-share" rule.

Answer: FALSE

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

5) According to recent research, family-owned firms in some highly-developed economies typically outperform publicly-owned firms.

Answer: TRUE

Diff: 1

Topic: 2.1 Who Owns the Business?

Skill: Recognition

Essay/Short Answer

1) What are the most important distinctions that make *state owned enterprises* (SOEs) different from other forms of government organizations?

Answer: *State owned enterprises* are created distinctly for the purpose of commercial activities, rather than the multitude of other social, civil, and regulatory activities of government. SOEs are today, in many countries, the dominant form of business entity.

Diff: 2

Topic: 2.1 Who Owns the Business?

Skill: Conceptual

2.2 The Goal of Management

Multiple Choice

1) "Maximize corporate wealth":

A) is the primary objective of the non-Anglo-American model of management.

B) as a management objective treats shareholders on a par with other corporate stakeholders such as creditors, labor, and local community.

C) has a broader definition than just financial wealth.

D) all of the above

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

2) The Shareholder Wealth Maximization Model (SWM):

A) combines the interests and inputs of shareholders, creditors, management, employees, and society.

B) is being usurped by the Stakeholder Capitalism Model as those types of MNEs dominate their global industry segments.

C) clearly places shareholders as the primary stakeholder.

D) is the dominant form of corporate management in the European-Japanese governance system.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

3) The Stakeholder Capitalism Model (SCM):

A) clearly places shareholders as the primary stakeholder.

B) combines the interests and inputs of shareholders, creditors, management, employees, and society.

C) has financial profit as its goal and is often termed impatient capital.

D) is the Anglo-American model of corporate governance.

Answer: B

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

4) In the Anglo-American model of corporate governance, the primary goal of management is to:

A) maximize the wealth of all stakeholders.

B) maximize shareholder wealth.

C) minimize costs.

D) minimize risk.

Answer: B

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

- 5) In finance, an efficient market is one in which:
- A) prices are assumed to be correct.
 - B) prices adjust quickly and accurately to new information.
 - C) prices are the best allocators of capital in the macro economy.
 - D) all of the above

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

- 6) Systematic risk can be defined as:
- A) the total risk to the firm.
 - B) the risk of the individual security.
 - C) the risk of the market in general.
 - D) the risk that can be systematically diversified away.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

- 7) Unsystematic risk can be defined as:
- A) the total risk to the firm.
 - B) the risk of the individual security.
 - C) the added risk that a firm's shares bring to a diversified portfolio.
 - D) the risk of the market in general.

Answer: B

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

- 8) The study of how shareholders can motivate management to accept the prescriptions of the shareholder wealth maximization model is called:

- A) market efficiency.
- B) the SWM model.
- C) agency theory.
- D) the SCM model.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

9) Under the Shareholder Wealth Maximization Model (SWM) of corporate governance, poor firm performance is likely to be faced with all but which of the following?

- A) sale of shares by disgruntled current shareholders
- B) shareholder activism to attempt a change in current management
- C) as a maximum threat, initiation of a corporate takeover
- D) prison time for executive management

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

10) Which of the following is a reason why managers act to maximize shareholder wealth in Anglo-American markets?

- A) the use of stock options to align the goals of shareholders and managers
- B) the market for corporate control that allows for outside takeover of the firm
- C) performance based compensation for executive management
- D) all of the above

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

11) Which of the following is NOT true regarding the stakeholder capitalism model?

- A) Banks and other financial institutions are less important creditors than securities markets.
- B) Labor unions are more powerful than in the Anglo-American markets.
- C) Governments interfere more in the marketplace to protect important stakeholder groups.
- D) All of the above are TRUE.

Answer: A

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

12) The stakeholder capitalism model:

- A) typically avoids the flaw of impatient capital.
- B) tries to meet the desires of multiple stakeholders.
- C) may leave management without a clear signal about tradeoffs among the several stakeholders.
- D) all of the above

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

13) Which of the following is generally NOT considered to be a viable operational goal for a firm?

- A) maintaining a strong local currency
- B) maximization of after-tax income
- C) minimization of the firm's effective global tax burden
- D) correct positioning of the firm's income, cash flows and available funds as to country and currency

Answer: A

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

14) Which of the following operational goals for the international firm may be incompatible with the others?

- A) maintaining a strong local currency
- B) maximization of after-tax income
- C) minimization of the firm's effective global tax burden
- D) Each of these goals may be incompatible with one or more of the others.

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

15) The primary operational goal for the firm is to:

- A) maximize after-tax profits in each country where the firm is operating.
- B) minimize the total financial risk to the firm.
- C) maximize the consolidated after-tax profits of the firm.
- D) maximize the total risk to the firm.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

16) Which of the following broad topics is NOT identified as an area to be established as good corporate governance practice by the Organization for Economic Cooperation and Development (OECD)?

- A) protect the rights of shareholders
- B) disclosure and transparency
- C) the proper role of stakeholders in the governance of the firm
- D) All of the above should be a concern of good corporate governance.

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

17) The relationship among stakeholders used to determine and control the strategic direction and performance of an organization is termed:

- A) corporate governance.
- B) Anglo-American activism.
- C) capital structure.
- D) working capital management.

Answer: A

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

18) When discussing the structure of corporate governance, the authors distinguish between internal and external factors. _____ is an example of an internal factor, and _____ is an example of an external factor.

- A) Equity markets; executive management
- B) Debt markets; board of directors
- C) Executive management; auditors
- D) Auditors; regulators

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

19) Which of the following is NOT commonly associated with a government affiliated form of corporate governance regime?

- A) no minority influence
- B) lack of transparency
- C) state ownership of enterprise
- D) All are associated with this type of corporate governance regime.

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

20) Generally speaking, which of the following is NOT considered an important factor in the composition and control of corporate boards of directors?

- A) the number of insider vs outside directors
- B) the total number of directors on the board
- C) the composition of the compensation committee
- D) All of the above are important factors of board composition.

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

21) Signed into law on July 30, 2002, the _____ Act requires CEOs of publicly traded companies to vouch for the veracity of the firm's published financial statements.

- A) Smoot-Hawley
- B) Humphrey-Hawkins
- C) McCain-Merrill
- D) Sarbanes-Oxley

Answer: D

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

22) The Sarbanes-Oxley Act, passed by the U.S. Congress in July 2002, was designed to:

- A) reinstitute heavy tariffs on international trade.
- B) reform corporate governance.
- C) limit the Federal Reserve Board's ability to engage in the buying and selling of gold.
- D) limit trade with countries deemed lenient on terrorism.

Answer: B

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

23) Anglo-American markets is a term used to describe business markets in:

- A) North, Central, and South America.
- B) the United States, Canada, and Western Europe.
- C) the United States, United Kingdom, Canada, Australia and New Zealand.
- D) the United States, France, Britain, and Germany.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

24) The deliberation of the of the process demonstrated in the European-Japanese system of corporate governance has sometimes been termed:

- A) socialism.
- B) impatient capital.
- C) patient capital.
- D) communism.

Answer: C

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

25) With shareholder wealth maximization as the manager's goal, capital may be termed:

- A) impatient.
- B) patient.
- C) borrowed.
- D) bought.

Answer: A

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

26) Which of the following is NOT an important concept when distinguishing between international and domestic financial management?

- A) corporate governance
- B) culture, history, and institutions
- C) political risk
- D) All of the above are important distinguishing concepts.

Answer: D

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Conceptual

27) The Board of Directors:

- A) consists exclusively of the officers of the corporation.
- B) is the legal body which is accountable for the governance of the corporation.
- C) are not subject to the external forces of the marketplace.
- D) is appointed by the Securities and Exchange Commission (SEC).

Answer: B

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

28) If share price rises from \$12 to \$15 per share, and pays a dividend of \$1 per share, what was the rate of return to shareholders?

- A) 26.67%
- B) -13.33%
- C) 33.33%
- D) 16.67%

Answer: C

Diff: 3

Topic: 2.2 The Goal of Management

Skill: Analytical

29) PolyProduction Inc. has two classes of common stock. Class A has 5 million shares with 10 votes per share. Class B has 5 million shares with 1 vote per share. If the dividends per share are equal for both class A and B stock, then Class A shareholders have _____ of the votes and _____ of the dividends.

- A) 90.91%; 90.91%
- B) 90.91%; 50.00%
- C) 50.00%; 50.00%
- D) 83.33%; 33.33%

Answer: B

Diff: 3

Topic: 2.2 The Goal of Management

Skill: Analytical

30) The number of publicly traded firms:

- A) peaked in the U.S. in 1996.
- B) peaked worldwide in 1996.
- C) increased significantly in 2009 as a result of the international financial crisis.
- D) all of the above

Answer: A

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

31) Which of the following is NOT a possible and appropriate response by shareholders dissatisfied with existing firm management of a publicly traded firm?

- A) Shareholders could sell their shares of stock.
- B) Shareholders could remain quietly disgruntled.
- C) Shareholders, perhaps with the help of others, could attempt to initiate a takeover.
- D) All of these responses may be possible and appropriate.

Answer: D

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Conceptual

True/False

1) The stakeholder capitalism model (SCM) holds that total risk (operational and financial) is more important than just systematic risk.

Answer: FALSE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

2) In recent years the trend has been for markets to increasing focus on the shareholder wealth form of wealth maximization.

Answer: TRUE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

3) Patient Capitalism is characterized by short-term focus by both management and investors.

Answer: FALSE

Comment: Impatient Capitalism is characterized by short-term focus by both management and investors.

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

4) Agency theory states that unsystematic risk can be eliminated through diversification.

Answer: FALSE

Comment: CAPM demonstrates that unsystematic risk can be eliminated through diversification.

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

5) The stakeholder capitalism model does not assume that equity markets are either efficient or inefficient.

Answer: TRUE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

6) The stakeholder capitalism model assumes that only systematic risk "counts" or is a prime concern for management.

Answer: FALSE

Comment: The shareholder wealth model assumes that only systematic risk "counts" or is a prime concern for management.

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

7) Dividend yield is the change in the share price of stock as traded in the public equity markets.

Answer: FALSE

Comment: Capital gain or loss is the change in the share price of stock as traded in the public equity markets.

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

8) Regarding comparative corporate governance regimes: Bank-based regimes characterized by government influence in bank lending and a lack of transparency is often found in countries such as Korea and Germany.

Answer: TRUE

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Recognition

9) Investor protection is typically better in countries with codified civil law (the Code Napoleon) than in countries with a legal system based in English common law.

Answer: FALSE

Comment: Investor protection is typically better in countries with with a legal system based in English common law.

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Conceptual

10) The relatively low cost of compliance with the Sarbanes-Oxley Act (SOX) has been a surprising benefit of the act.

Answer: FALSE

Comment: The relatively high cost of compliance with the Sarbanes-Oxley Act (SOX) has been a result of the act.

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

11) According to recent research, family-owned firms in some highly-developed economies typically outperform publicly-owned firms.

Answer: TRUE

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Recognition

12) The goal of all international corporations is to maximize shareholder wealth.

Answer: FALSE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

13) Systematic risk can be eliminated through portfolio diversification.

Answer: FALSE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

14) According to the authors, dual classes of voting stock are the norm in non-Anglo-American markets.

Answer: TRUE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

15) A recent study shows that privately held firms use less financial leverage and enjoy lower costs of debt than publicly traded firms.

Answer: TRUE

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Recognition

16) U.S. listings of publicly traded firms as a percentage of worldwide listings of such firms INCREASED from 11% in 1996 to approximately 33% in 2010.

Answer: FALSE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Recognition

17) Having Anglo-Americans as members of the board of directors of a non-Anglo-American firm signals poor corporate governance in the firm.

Answer: FALSE

Diff: 1

Topic: 2.2 The Goal of Management

Skill: Conceptual

18) In the *stakeholder capitalism model (SCM)* the assumption of market efficiency is absolutely critical.

Answer: FALSE

Diff: 2

Topic: 2.2 The Goal of Management

Skill: Conceptual

Short Answer/ Essay

1) Describe the management objectives of a firm governed by the shareholder wealth maximization model and one governed by the stakeholder wealth maximization model. Give an example of how these two models may lead to different decision-making by executive management.

Answer: Shareholder wealth maximization attempts to do just that, typically through the maximization of share price. Stakeholder wealth maximization is much more difficult because of the necessity to satisfy many stakeholders all having approximately equal claim on the objectives of management. These stakeholders may include shareholders, creditors, customers, employees, and community. Differing decisions may occur in a situation that involves significant social costs. For example, in the U.S. the decision to shift production from a local factory to a foreign one may be in large based on the change in NPV as the result of the move with only minor consideration of the impact that a change in location would have on the community at large or the local employees. A manager of a stakeholder driven firm may place equal or greater emphasis on the local employees and community and choose to maintain the current facility rather than move even if the foreign operation provided a much greater NPV. Ultimately, the latter may cause an inefficient allocation of scarce resources and lead to an overall lower standard of living.

Diff: 3

Topic: 2.2 The Goal of Management

Skill: Conceptual

2) Define patient and impatient capitalism and discuss how each may lead to different decision-making in the shareholder wealth maximization model.

Answer: Patient capitalism may be defined as a focus on long-term shareholder wealth maximization and is often associated with management focusing on long term investments with less emphasis placed on short-term or trendy objectives. On the other hand, impatient capitalism could be described as a destructive focus on the short term by both management and investors. These differences in the time horizon could lead to different and perhaps inferior decisions by existing management and ultimately be costly to the shareholders.

Diff: 3

Topic: 2.2 The Goal of Management

Skill: Conceptual