

Part A. Economic Principles Related to Business Management

1. When economists speak of scarcity, they are referring to the _____ .
 - a. Condition in which society is not employing all its resources in an efficient way
 - b. Condition in which people's wants outstrip the limited resources available to satisfy those wants
 - c. Economic condition that exists in only very poor countries of the world
 - d. Condition in which society produces too many frivolous goods and not enough socially desirable goods.
2. Which of the following is **NOT** one of the categories of resources?
 - a. Labor
 - b. Government
 - c. Capital
 - d. Entrepreneurship
3. "Entrepreneurship" is _____ .
 - a. the talent for organizing the use of land, labor and capital, among other things
 - b. skill in influencing government regulators and legislators
 - c. accumulated technical knowledge in using labor and capital
 - d. knowledge of the particular natural resources to be found in a given area.
4. Some years ago, chemists at 3M Corporation were trying to create a super-strong glue. Somehow they got their molecules twisted and came up with one of the weakest glues ever made. Rather than pouring it down the drain, they tried coating some paper with it. Voila! The "Post-It Note" was born. In this case, 3M was acting as _____ .
 - a. A utility
 - b. A rationer
 - c. An entrepreneur
 - d. An abstraction
5. Economic profit is the difference between total revenue and _____ .
 - a. Explicit costs
 - b. Implicit costs
 - c. Sunk costs
 - d. The sum of explicit and implicit costs
6. A cost of resources used in production for which no actual monetary payment is made is a(n) _____ cost.
 - a. Tacit
 - b. Implicit
 - c. Covert
 - d. Explicit

7. Five months ago Wilson opened up a health club. Which of the following is an implicit cost related to the health club?
 - a. Wilson paid \$120 for an outside laundry service to clean the towels used at the club.
 - b. Wilson paid \$100 for the pest control exterminator to spray the health club.
 - c. Wilson previously worked as an accountant, earning \$3,000 a month.
 - d. Wilson usually eats four hamburgers a day, priced at \$3 each.
8. If a firm earns a normal profit, then it has generated revenues _____ .
 - a. Equal to the sum of implicit and explicit costs
 - b. Greater than total opportunity costs
 - c. Sufficient to cover explicit costs, but not implicit costs
 - d. Sufficient to cover implicit costs, but not explicit costs
9. An unrecoverable cost that should be disregarded in any current or future decision is also called a(n) _____ cost.
 - a. Sunk
 - b. Explicit
 - c. Implicit
 - d. Variable
10. A fixed input is an input whose quantity _____ .
 - a. Can be changed as output changes in the short term
 - b. Cannot be changed as output changes in the short run
 - c. Cannot be changed as output changes in the long run
 - d. Both (A) and (C)
11. Average fixed cost _____ .
 - a. Is usually greater at lower levels of output than at higher levels
 - b. Does not change as output changes
 - c. Exists only in the short run
 - d. Both (A) and (C)
12. At 200 units of output, total cost is \$36,000 and total variable cost is \$20,000. What does total fixed cost equal at 200 units?
 - a. \$38,000
 - b. \$20,000
 - c. \$16,000
 - d. \$80
13. Which of these statements is false?
 - a. There are no fixed costs in the long run.
 - b. Total costs are equal to total fixed costs plus total variable costs.
 - c. In the short run, all inputs are fixed inputs.
 - d. A fixed cost is a cost that does NOT change as output changes.
14. Costs that do not change with output are called _____ costs.
 - a. Marginal
 - b. Average
 - c. Fixed
 - d. Variable

15. Suppose that one fixed and one variable input are used to produce good X. As the marginal physical product of the variable input increases, then marginal cost _____ .
- Increases
 - Decreases
 - Remains constant
 - There is not enough information to answer the question
16. One major reason for the law of demand is that _____ .
- One price changing requires at least one other price to change in the opposite direction
 - People substitute relatively lower-priced goods for relatively higher-priced goods
 - A higher price never reduced quantity demanded by enough to lower total revenue
 - People are willing to produce more units at a higher price
17. If an increase in income results in an increase in the demand for chicken, then chicken is _____ .
- A neutral good
 - A luxury good
 - A normal good
 - An inferior good
18. Which of the following is true about the relationship between price and quantity supplied?
- There is always a direct relationship.
 - There is always an inverse relationship.
 - There is usually a direct relationship.
 - There is usually an inverse relationship.
19. If Max's demand for hot dogs falls as his income rises, then hot dogs are _____ .
- A bad good
 - An inferior good
 - A preferential good
 - A normal good
20. An increase in the number of buyers in an area will result in a _____ .
- Movement up the demand curve
 - Movement down the demand curve
 - Leftward shift in the demand curve
 - Rightward shift in the demand curve
21. "Doubling the number of acres farmed in 10 years" is an example of a _____ .
- long-run goal
 - short-run goal
 - mission statement
 - decision

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22. Which of the following is an example of a strategic decision?
- Determining fertilizer levels for crops
 - Deciding when to sell grain
 - Determining what type of business/legal organization to use
 - Setting milking times for a dairy
23. Which of the following is an example of a tactical decision?
- Balancing a livestock ration
 - Forming a partnership with a relative
 - Joining a feeder pig cooperative
 - Installing an irrigation system
24. "What managers do" is best described by which of the following?
- Gather information
 - Make decisions
 - Analyze data
 - Organize the farm
25. The statement "To achieve an average feed conversion rate of 2.75 pounds of feed per pound of gain for my market hogs by 2020" is _____ .
- A mission statement
 - A goal
 - A strategy
 - An example of external scanning
26. A prepaid expense is one where payment is made _____ .
- By check
 - In an accounting period prior to the one in which the item will be used to produce income
 - In a series of payments over time
 - Before the bill is even received
27. Which of the following would **NOT** be recorded when using a single-entry, cash accounting system?
- Charging \$2,000 worth of chemicals at the farm supply store
 - Billing a neighbor \$850 for baling hay
 - Recognizing that \$3,476.34 of interest has accrued since the last interest payment
 - ALL of the above
28. At the end of the year, a farmer has an unpaid bill at the local machinery repair shop. It would be shown in an accrual accounting system as a(n) _____ .
- Prepaid expense
 - Account receivable
 - Account payable
 - Accrued expense

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29. A major advantage of accrual accounting over cash accounting is _____ .
- a. A more accurate estimate of annual profit
 - b. Simplicity
 - c. Always show a higher profit
 - d. Can use single entry instead of double entry
30. When something is purchased and paid for in a year before it will be used to produce income it is called a(n) _____ .
- a. Accrued expense
 - b. Account payable
 - c. Prepaid expense
 - d. Account receivable
31. An organized list of all accounts used by an accounting system is called _____ .
- a. A chart of accounts
 - b. A balance sheet
 - c. An income statement
 - d. A debit
32. According to the cash accounting method, expenses are recorded _____ .
- a. When they are paid
 - b. When they are accrued
 - c. At the end of the month
 - d. ALL of the above
33. Which of the following is an example of a noncurrent liability?
- a. Farm machinery
 - b. Loan on feeder livestock
 - c. Loan on farm machinery
 - d. Prepaid expense
34. Which of the following is an example of a current asset?
- a. Dairy cows
 - b. Farm buildings
 - c. Farm machinery
 - d. NONE of the above
35. Another term which has the same meaning as owner's equity is _____ .
- a. Net worth
 - b. Net farm income
 - c. Total asset value
 - d. Total liabilities
36. Of the following, which is the most liquid asset?
- a. Farm machinery
 - b. Balance in checking account
 - c. Breeding livestock
 - d. Feeder livestock

37. If a business has working capital greater than \$0, its current ratio will be _____ .
- Greater than one
 - Equal to one
 - Less than one
 - There is no relationship between the amount of working capital and the current ratio
38. If the debt/asset ratio is increasing, then the debt/equity ratio will be _____ .
- Increasing
 - Decreasing
 - Constant
 - Indeterminate, need more information
39. Which of the following best describes a balance sheet?
- It shows changes in assets and liabilities over the last accounting period.
 - It shows changes in asset and liabilities over a period of time.
 - It shows assets and liabilities at a point in time.
 - It shows profit for the last accounting period.
40. The best description of a business which has increased its debt/asset ratio is one which has _____ .
- Purchased more assets
 - Sold some assets
 - Increased its debt
 - Increased its debt relative to total assets
41. Which of the following assets would have the same value using either a cost or a market based valuation?
- Land
 - Machinery
 - Prepaid expenses
 - Purchased breeding livestock
42. The degree to which a farm's assets adequately cover or exceed its liabilities is referred to as _____ .
- Solvency
 - Profitability
 - Liquidity
 - Working capital
43. A statement of owner equity shows _____ .
- A list of all assets and liabilities
 - The valuation adjustment for owner equity
 - Owner equity for the past 20 years
 - The sources and amounts of changes in owner equity

44. Which financial statement covers only a single point in time rather than a period of time?
- Income statement
 - Statement of owner equity
 - Statement of cash flows
 - Balance sheet
45. The proper term for the value found by subtracting accumulated depreciation from the asset's original cost is _____ .
- Salvage value
 - Market value
 - Book value
 - Use value
46. The total depreciation over an asset's useful life is equal to _____ .
- Cost minus salvage value
 - Cost plus salvage value
 - Book value
 - Salvage value
47. To be depreciable, an asset must have a useful life of _____ .
- More than ten years
 - Five years or more
 - More than one year
 - Six months or longer
48. Depreciation is a cost associated with which of the following assets?
- Livestock feed
 - Nitrogen fertilizer
 - A machinery storage shed
 - Corn silage stored in a silo
49. Which of the following items on a balance sheet would **NOT** be considered when making accrual adjustments to net income?
- Accrued interest
 - Change in market value of land
 - Inventories of market livestock
 - Pre-paid expenses
50. Which of the following is **NOT** included as an expense on the net farm income statement?
- Depreciation
 - Interest payments made on loans
 - Principal payments made on loans
 - The cost of supplies used but not yet paid for

51. Which type of financial statements would be most useful for keeping record of expenses?
- Net worth statement
 - Net income statement
 - Statement of owner equity
 - Statement of cash flows
52. The current ratio is a measure of a farm firm's _____ .
- Return on equity
 - Ability to pay short-term credit obligations
 - Return on investment in current assets
 - Level of total debt to total assets at the present time
53. The degree to which a farm's assets adequately secure its debts is referred to as _____ .
- Liquidity
 - Solvency
 - Efficiency
 - Profitability
54. Which of the following would **NOT** appear on a cash flow budget?
- Feed purchases
 - Inventory change
 - Family living expenses
 - Cost of new tractor
55. Which of the following would appear on an income statement but **NOT** on a cash flow budget?
- Gain or loss on sale of capital asset
 - Inventory changes
 - Depreciation
 - ALL of the above
56. When preparing a cash flow budget it is important to _____ .
- Take into account the expected timing of cash inflows and outflows
 - Include all noncash expenses
 - Include only noncash revenues
 - Estimate expected cash inflows and outflows for a whole year only
57. A cash flow budget can be used to _____ .
- Estimate when and how much money will need to be borrowed during the year
 - Estimate when and how much debt can be repaid during the year
 - Estimate when excess cash may be available so plans can be made to invest it
 - ALL of the above
58. A projected negative annual cash flow indicates _____ .
- Net farm income will be negative
 - Depreciation expense is too high
 - Projected cash inflows are less than projected cash outflows
 - Projected asset values are less than projected liability values

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59. A cash flow budget can be used to monitor the farm business by _____ .
- Comparing actual cash inflows and outflows to the budgeted monthly cash flows
 - Comparing actual cash inflows and outflows to 10-year averages
 - Comparing the projected ending cash balances to the actual balances for each month
 - Comparing actual selling prices to those assumed in the cash flow budget
60. A cash flow analysis of an investment in a new capital asset should include projections for _____ .
- Several months
 - One year on a monthly basis
 - One year for a whole year only
 - Several years
61. The last step in constructing a cash flow budget should be _____ .
- Estimating the amount of crop and livestock production for the year
 - Estimating how much new current debt will be needed and can be repaid each month
 - Estimating family living expenses
 - Estimating when payments on existing debt are due
62. A cash flow budget should contain all of the following items except _____ .
- Depreciation
 - Principal payments on machinery loans
 - Cost of new farm machinery to be purchased
 - Diesel fuel
63. A projected negative cash balance at the end of the year can be made positive by _____ .
- Delaying proposed purchases of capital assets
 - Carrying over less inventory of stored grain to the following year
 - Lengthening repayment periods on term loans
 - ALL of the above
64. Which of the following may be included on a partial budget?
- Fixed costs
 - Variable costs
 - Opportunity costs
 - ALL of the above
65. The values shown on a partial budget are _____ .
- Total revenues and total expenses for the farm
 - Only total expenses for the farm
 - Only total revenue for the farm
 - Only changes in revenues and expenses
66. Which of the following are the profit increasing changes on a partial budget?
- Additional costs and additional revenue
 - Reduced costs and reduced revenue
 - Reduced costs and additional revenue
 - Additional costs and reduced revenue

67. Which of the following are the profit decreasing changes on a partial budget?
- Additional costs and additional revenue
 - Additional costs and reduced revenue
 - Reduced costs and additional revenue
 - Reduced costs and reduced revenue
68. If a partial budget shows some fixed or ownership costs under Reduced Costs, it means _____ .
- The proposed alternative required purchasing a new capital asset
 - A new capital asset must be purchased next year with either alternative
 - The proposed alternative would allow sale of a capital asset that will no longer be needed
 - There is an error on the budget as fixed costs are never included under Reduced Costs
69. A partial budget is designed to analyze the effect of a proposed management change on _____ .
- Profit
 - Revenue only
 - Expenses only
 - Crop yields only
70. A partial budget would be the most useful type of budget for estimating _____ .
- The amount of borrowing required for the next year
 - The break even price needed to cover all costs of cotton production
 - Labor needed on the farm during the next year
 - The change in profit from installing an irrigation system in one field
71. A partial budget is an appropriate tool for analyzing _____ .
- The expansion of an existing enterprise
 - The profit or loss from a single enterprise
 - The cash flows in the business
 - The start up costs in a new business
72. On a partial budget which analyzes switching 120 acres from growing wheat to growing barley, which of the following costs would **NOT** be included on the budget?
- Seed expense for either crop
 - Fertilizer for the barley
 - Fertilizer for the wheat
 - Property tax on the land
73. Estate planning is most concerned with passing on the _____ of the farm to the next generation.
- Income
 - Ownership
 - Management
 - Debt

74. A “limited” partnership is one in which _____ .
- Some partners do NOT participate in management, and have limited liability
 - The maximum number of acres farmed is fixed by law
 - The number of partners must not exceed 75
 - Only one type of enterprise is carried out
75. A limited liability company combines the legal aspects of _____ .
- A sole proprietorship and a partnership
 - A partnership and a corporation
 - A corporation and a cooperative
 - A sole proprietorship and a corporation
76. In a cooperative, shareholders have voting rights _____ .
- In proportion to the number of shares owned
 - In proportion to the amount of business done with the cooperative
 - In proportion to the capital contributed
 - That are equal for all members
77. The most common form of farm business organization is the _____ .
- Sole proprietorship
 - Partnership
 - Limited liability company
78. Beth purchased two May live-cattle futures contracts in January. One contract is 40,000 lbs. of live cattle. It is currently March. In March, Beth can fulfill her contract obligation by _____ .
- Purchasing two May live-cattle futures contracts
 - Selling two May live-cattle futures contracts
 - Delivering 80,000 lbs. of live cattle to a futures transaction point
 - Accepting delivery of 80,000 lbs. of live-cattle at a futures transaction point

Exhibit 6

	Open	High	Low	Settle	Chg.
CATTLE (CME)					
40,000 lbs. – cents per lb.					
Aug. 05	80.00	80.22	79.75	79.92	+12
Oct. 05	81.05	81.30	80.57	80.65	-.07
Dec. 05	83.80	84.15	83.50	83.62	-.12
Feb. 06	86.00	86.35	85.85	85.97	-.20
Apr. 06	84.50	84.75	84.15	84.42	-.12
Jun. 06	80.20	80.35	79.60	79.60	-.30
Aug. 06	79.52	79.52	79.52	79.52	-.27
Est. sales 11, 282. Mon’s sales 15, 866					
Mon’s open int. 131, 490. +309					

79. Refer to Exhibit 6. On August 10, 2005, what was the best prediction of live-cattle spot prices in February 2006?
- 85.97 cents per lb.
 - 8.597 cents per lb.
 - 1.59 cents per lb.
 - 0.8597 cents per lb.
80. Refer to Exhibit 6. On August 10, 2005, a buyer of live-cattle decides to execute a hedge for cattle they will purchase in April 2006. In April, she expects the basis to be \$2.25/cwt. If she hedges today, about what hedge price does she expect to receive?
- 0.8667/cwt
 - 8.667/cwt
 - 86.67/cwt
 - 866.7/cwt

Exhibit 7

	May 12, 2004	November 5, 2004
November 2004 Soybean Future Contract Price (one contract is 5,000 bushels)	\$6.23/bushel	\$7.50/bushel
Soybean Spot Price	\$7.15	\$7.35

81. Refer to Exhibit 7. On November 5, 2004, what was the soybean basis?
- 1.5
 - 0.15
 - 1.5
 - 0.15
82. Refer to Exhibit 7. On May 12, a speculator sells three November soybean futures contracts and off-sets those contracts on November 5. What are the speculator's profits?
- \$190.50
 - \$19,050
 - \$190.50
 - \$190,50
83. Refer to Exhibit 7. Soybean farmers plant in May and harvest in November. A soybean farmer hedges by _____ November soybean futures in May, _____ the same number of November soybean futures in November and selling their grain in the spot market.
- Buying, buying
 - Buying, selling
 - Selling, buying
 - Selling, selling

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84. Refer to Exhibit 7. If the soybean farmer hedged in 2004, what hedge price did she receive?
- \$608.00
 - \$0.608
 - \$60.80
 - \$6.08

Exhibit 8

Contract	Future Prices on February 6, 2003	Future Prices on March 1, 2003
	Settlement Price (\$ per bushel)	Settlement Price (\$ per bushel)
March 03 Corn Futures Contract (5,000 bushels)	2.38	2.50
February 04 Corn Futures Contract (5,000 bushels)	2.44	2.62

85. Refer to Exhibit 8. Suppose Dave Chappell bought two March corn contracts on February 6, 2003. It is currently March 1, 2003, the month in which the March contract expires. He can fulfill his contract obligation by _____ .
- Selling two March corn contracts at \$2.38/bushel
 - Buying two March corn contracts at \$2.50/bushel
 - Accepting delivery of corn and paying \$2.38/bushel
 - Accepting delivery of corn and paying \$2.50/bushel
86. More than 99% of all futures contract obligations are met by _____ .
- Offsetting
 - Accepting or making delivery
 - Cancelling the contract
 - NONE of the above

Exhibit 9

Date	July 2004 Winter Wheat Contract Futures Price (5,000 bushels/contract)	Spot Price in Your Town
	Settlement Price (\$ per bushel)	(\$ per bushel)
January 10, 2004	3.30	3.60
July 10, 2004	3.50	3.45

87. Refer to Exhibit 9. You are a wheat farmer who plans to harvest and sell wheat in July. You decide to hedge all of your wheat by selling wheat futures contracts on January 10, 2004. You expect the basis in July to be $-\$0.10$. What is your expected hedge price on January 10?
- $\$32.00$
 - $\$3.20$
 - $\$320.00$
 - $\$2.30$
88. Refer to Exhibit 9. You are a wheat farmer who plans to harvest and sell wheat in July. You decide to hedge all of your wheat by selling wheat futures contracts on January 10, 2004. You expect the basic in July to be $-\$0.10$. Come July 10, you offset your future position and sell in your local spot market. What is your realized hedge price?
- $\$3.25$
 - $\$2.35$
 - $\$32.50$
 - $\$23.50$
89. Refer to Exhibit 9. You purchase a put option for a July 2004 winter wheat futures contract at a price (the option premium) of $\$0.40$ per bushel. The strike price for this option is $\$4.00$ per bushel. If the expected basis in July is $\$0.25$ /bushel, what is the minimum expected price you will receive for your wheat by using this option?
- $\$38.50$
 - $\$83.50$
 - $\$3.85$
 - $\$8.35$

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Exhibit 10

Futures Contract	Futures Price on February 6, 2003	Futures Price on March 1, 2003
	Settlement Price (\$ per bushel)	Settlement Price (\$ per bushel)
March Corn (5,000 bushels)	2.38	2.50
December Corn (5,000 bushels)	2.44	2.62
July Wheat (5,000 bushels)	3.41	3.10

90. Refer to Exhibit 10. Suppose it is March 1, 2003. Between March and December, the spot price of corn is expected to _____ .
- Rise
 - Fall
 - Remain the same
 - Cannot tell from the information given
91. Refer to Exhibit 10. Suppose it is February 6, 2003. The best prediction of corn spot prices in March is _____ .
- \$23.80/bushel
 - \$2.38/bushel
 - \$32.80/bushel
 - \$3.28/bushel
92. Refer to Exhibit 10. If Pistol Pete purchases one July wheat contract on February 6 and offsets the contract on March 1, how much total money will he receive or pay?
- \$15.50
 - \$1,550
 - (-\$15.50)
 - (-\$1,550)

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Michigan Farm Business Management Test Bank #1 Key

1. B
2. B
3. A
4. C
5. D
6. B
7. C
8. A
9. A
10. B
11. D
12. C
13. C
14. C
15. B
16. B
17. C
18. C
19. B
20. D
21. A
22. C
23. A
24. B
25. B
26. B
27. D
28. C
29. A
30. C
31. A
32. A
33. C
34. D
35. A

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- 36. B
- 37. A
- 38. A
- 39. C
- 40. D
- 41. C
- 42. A
- 43. D
- 44. D
- 45. C
- 46. A
- 47. C
- 48. C
- 49. B
- 50. C
- 51. B
- 52. B
- 53. B
- 54. B
- 55. D
- 56. A
- 57. D
- 58. C
- 59. A
- 60. D
- 61. B
- 62. A
- 63. D
- 64. D
- 65. D
- 66. C
- 67. B
- 68. C
- 69. A
- 70. D
- 71. A
- 72. D
- 73. B

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74. A

75. B

76. D

77. A

78. B

79. A

80. C

81. B

82. B

83. C

84. D

85. C

86. A

87. B

88. A

89. C

90. A

91. B

92. D