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CHAPTER

Valuation of Real Options

Multiple Choice Questions

1. Procrastination can have a positive value for a company:
(a) True (b) False

2. Stock-options are real options:
(a) True (b) False

3. A call option gives the holder a right not to buy an underlying asset at a certain strike price:
(a) True (b) False

4. As far as equity shares of a given company is concerned, call options are more valuable than put options:
(a) True (b) False

5. Valuing financial options related to mining companies is easier than valuing real options:
(a) True (b) False

6. Black and Scholes model assumes that stock price is continuous and is distributed normally:
(a) True (b) False

7. Relative valuation models almost invariably views risk negatively unlike contingent claims valuation:
(a) True (b) False

8. In which of the following there is an unlimited downside risk?
(a) Buying a call option
(b) Writing a call option
(c) Buying a put option
(d) Writing a put option
(e) None of the above

9. Which one of the following is not an assumption underlying the Black-Scholes model:
(a) The call option is the American option
(b) The stock pays no dividend
(c) The risk-free interest rate is constant
(d) There are no transaction costs and taxes
(e) None of the above

10. Value of a call option increases when
(a) Stock price is low
(b) Volatility is high
(c) Time to expiration is near
(d) All the above
(e) None of the above

11. Which of the following is not a real option?
(a) Investment timing option.
(b) Exit option
(c) Flexibility option
(d) Growth option
(e) None of the above

12. There could be some value in delaying a project:
(a) True (b) False

13. Oil refineries are typically designed with:
(a) Wait and watch option.
(b) Output flexibility option
(c) Shut-down option
(d) Abandonment option
(e) None of the above

14. Shut down options are more valuable when:
(a) The variable costs are high
(b) The variable costs are low
(c) The fixed costs are high
(d) The contribution margin is high
(e) None of the above

15. The price of an option depends on the attitude of the investor towards risk:
(a) True (b) False

16. Black-Sholes model assumes that short-selling is freely permitted:
(a) True b. False