

Practice Quiz 11: Risk, Leverage, and Retirement Planning

1. Discuss the concept of leverage and state the formula for leverage ratio. Explain how leverage relates to both risk and interest.
2. Discuss life-cycle investing as a retirement strategy.
3. For her town's annual summer festival, Abbey plans to open a hot dog stand with a \$4,000 investment. She contributes \$500 of her own money and borrows the remaining \$3,500 from her parents (with no interest). If the project returns 6% on the \$4,000 investment, what is the return on Abbey's equity?
4. Jack invests \$80,000 in a start-up, \$60,000 of which is borrowed at an interest rate of 12%. If the project returns 20%, what is Jack's return on equity?
5. Calculate the return that would cause Jack's start-up in problem 4 to go insolvent.