The answer to the question is highlighted in red. Explanations are highlighted in green.

13. Kimbes Karstore has fixed charges associated with the manufacture and sale of its inventory, including depreciation. As a result, if Kimbes’ sales increase by 5 percent, its ______ will increase by ______ 5 percent.
   a. earnings before interest and taxes (EBIT); less than
   b. EBIT; the same
   c. EBIT; greater than
   d. EPS; less than
   e. gross profit; greater than

Kimbes Karstre has operating leverage, thus DOL > 1.0. As a result, if sales increase by 5 percent, Karstore’s EBIT (or NOI) will increase by greater than 5 percent. Note that the firm’s net income will also increase by greater than 5 percent.

RETURN TO THE SAMPLE QUESTIONS