



Price, Risk, and Return Relations

[Questions]

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1. Any 2 assets with identical risks and rewards must be priced equally.
 - a. True
 - b. False

2. Which ONE of the following describes an “arbitrage” opportunity?
 - a. A case where you can use funds attained from the sale of one stock to buy another stock.
 - b. A scenario where you can bet on the price of any stock to go up, without any risk.
 - c. A case where 2 assets with identical risks and payoffs trade at considerably different prices.
 - d. A scenario where 2 assets with significantly different risks and rewards trade at significantly different prices.
 - e. A case where one can earn money with very large investments albeit at a relatively low risk.

3. Knots & Bolts Plc’s stock has a 12% expected return with a 18% risk. The stock currently trades at £11.93. Nuts & Crosses Plc, a similar firm with identical risk and rewards should trade at
 - a. £10.65
 - b. £10.11
 - c. £11.93
 - d. £13.36
 - e. £14.08

4. Watson Inc. and Sherstock Plc operate in similar industries with identical risks and rewards. If Sherstock Plc’s stock trades at €100 and Watson Inc.’s trades at €90, then an arbitrage opportunity is very likely to exist.
 - a. True
 - b. False

5. Moondog Inc.'s stock maintains a 16% annual expected return and 27% risk with a current price of \$73.59. What is its competitor, Starcat Inc.'s expected return if its stock is priced similarly and its risk is identical to Moondog Inc.?
 - a. Approximately equal to 16%
 - b. Relatively more than 16%
 - c. Relatively less than 16%
 - d. Significantly more than 16%
 - e. Significantly less than 16%

6. Which ONE of the following is FALSE?
 - a. Generally speaking, safer assets are worth more than riskier assets.
 - b. Generally speaking, riskier assets are worth less than safer assets.
 - c. Generally speaking, the expected return on safer assets is lesser than the expected return on riskier assets.
 - d. Generally speaking, the expected return on safer assets is greater than the expected return on riskier assets.
 - e. Generally speaking, two assets trading at the same price will have identical risks and rewards.

7. The value of an asset...
 - a. Increases as the risk increases and decreases as the expected return increases.
 - b. Decreases as the risk increases and increases as the expected return increases.
 - c. Increases as the risk decreases and decreases as the expected return increases.
 - d. Decreases as the risk decreases and decreases as the expected return decreases.

8. Risk and expected return maintain a proportional relationship so that as risk increases, expected return increases.

- a. True
- b. False

9. Of the 3 stocks below, which one is likely overvalued?

	Bit Plc	Fit Plc	Watch Inc.
Expected Return	12%	12%	10%
Risk	19%	16%	23%
Price	\$793.53	\$742.97	\$814.58

- a. Bit Plc
- b. Fit Plc
- c. Watch Inc.
- d. None of the above

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- d. None of the above