25/01 560 FINANCIAL MARKETS

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FM Practice Quiz M3

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QUESTIONS

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Question 1

What does a correlation of 0 between two securities indicate?

- (•) The movement of one security provides no information about the other
- ( ) The securities have identical returns
- ( ) The securities always move in the same direction
- ( ) The securities always move in opposite directions

Question 2

What is the primary challenge in calculating returns for illiquid assets in a portfolio?

- ( ) They cannot be included in diversified portfolios
- (•) Obtaining reliable and frequent price data
- ( ) They are more volatile than liquid assets
- ( ) They have higher transaction costs

Question 3

What is the implication of increased correlations during high volatility periods for portfolio diversification?

- ( ) Diversification benefits remain constant
- (•) Diversification benefits decrease
- ( ) Diversification becomes irrelevant
- ( ) Diversification benefits increase

Question 4

If an ETF's NAV is $50 and it has 1 million shares outstanding, what are its total assets if liabilities are $2 million?

- ( ) $50 million
- ( ) $48 million
- ( ) $54 million
- (•) $52 million

Question 5

How might the increasing popularity of ETFs affect individual stock prices?

- (•) It can increase demand for stocks included in popular indices, potentially inflating their prices
- ( ) It only affects small-cap stocks
- ( ) It has no effect on individual stock prices
- ( ) It always decreases the volatility of individual stocks

Question 6

Calculate the expected return of a portfolio with 60% in Stock A (return 5%) and 40% in Stock B (return 11%).

- ( ) 9.60%
- ( ) 8.00%
- ( ) 6.40%

- [x] 7.40%

Question 7

If an investor bought 100 shares of Meta at $320 before the drop and sold after the 26% decline what would be their total loss?

- [ ] $6,240
- [ ] $9,360
- [ ] $7,800
- [x] $8,320

Question 8

If a portfolio consists of two assets with standard deviations of 3% and 8% respectively and a correlation of 1 what is the portfolio standard deviation for equal weights?

- [ ] 4.27%
- [ ] 3.50%
- [x] 5.50%
- [ ] 2.50%

Question 9

What is the primary goal of diversification in investing?

- [ ] To concentrate capital in a limited number of investments
- [ ] To maximize portfolio returns
- [x] To manage risk
- [ ] To achieve perfect correlation between assets

Question 10

What is the key factor in determining a portfolio's volatility?

- [ ] Number of stock shares outstanding
- [x] Correlation between assets
- [ ] Individual stock prices
- [ ] Expected returns

Question 11

What is the primary benefit of asset allocation ETFs?

- [ ] Lower management fees
- [x] Extra level of diversification with professional management
- [ ] Higher returns guaranteed
- [ ] Extra level of diversification

Question 12

What is the main difference between passively managed and actively managed ETFs?

- [ ] Passively managed ETFs have higher fees than actively managed ETFs
- [ ] Passively managed ETFs are only available to institutional investors
- [ ] Actively managed ETFs are always more profitable than passively managed ETFs
- [x] Passively managed ETFs seek to track an index, while actively managed ETFs aim to outperform a benchmark

Question 13

What is the main limitation of using correlation coefficients with sample data rather than population data?

- ( ) They always underestimate the true correlation
- ( ) They cannot be calculated for samples
- (•) They become random variables requiring statistical tests for significance
- ( ) They can only be used with large samples

Question 14

How does the use of leverage in a portfolio typically affect its risk-return profile?

- ( ) It has no effect on the risk-return profile
- ( ) It increases return but decreases risk
- (•) It amplifies both potential returns and risks
- ( ) It always decreases both risk and return

Question 15

Which of the following is true about asset allocation ETFs?

- ( ) They have no management fees
- ( ) They are always managed by BlackRock
- ( ) They only invest in equities
- (•) They invest in different asset classes

Question 16

What is the primary benefit of ETFs in terms of market exposure?

- ( ) Guaranteed high returns
- ( ) Ability to predict market trends
- ( ) Elimination of all investment risk
- (•) Access to broad market diversification

Question 17

In finance what is meant by a "perfect hedge"?

- ( ) A portfolio with 0 standard deviation
- (•) A correlation of -1 between two securities
- ( ) A portfolio with equal weights of all assets
- ( ) A portfolio with maximum returns

Question 18

Which of the following is NOT a property of portfolio return?

- (•) It is always less volatile than the most volatile asset
- ( ) It can exceed individual asset returns with leverage
- ( ) It is always between the returns of the individual assets (for long-only portfolios)
- ( ) It is a linear combination of individual asset returns

Question 19

If a bond's yield rises from 2% to 3% what typically happens to its price?

- ( ) The price remains unchanged
- ( ) The price becomes zero

- [x] The price decreases
- [ ] The price increases

Question 20

What is the primary difference between sector selection and stock selection in ETF investing?

- [ ] Stock selection is less risky than sector selection
- [ ] Sector selection only applies to international markets
- [ ] Sector selection is always more profitable than stock selection
- [x] Sector selection focuses on macro-economic factors, while stock selection involves company-specific analysis

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