

## Risk and Return: Practice Problems

### Questions

#### Multiple Choice Questions

1. Which of the following best describes the risk-return tradeoff?
  - a) Higher risk guarantees higher returns.
  - b) Higher risk potentially leads to higher returns.
  - c) Risk and return are unrelated.
  - d) Lower risk always leads to higher returns.
2. The CAPM formula calculates:
  - a) Risk-free rate.
  - b) Expected return of a security.
  - c) Market return.
  - d) Actual return of a security.
3. A portfolio with beta = 1 indicates
  - a) The portfolio is risk-free.
  - b) The portfolio has the same risk as the market.
  - c) The portfolio has double the risk of the market.
  - d) The portfolio has no systematic risk.

#### True/False Questions

1. The Security Market Line (SML) is a graphical representation of the CAPM equation.
2. Beta measures both systematic and unsystematic risk of a security.
3. A stock with a beta of 1.5 is riskier than the market.
4. Systematic risk can be eliminated through diversification.
5. The Security Market Line (SML) is a graphical representation of the CAPM equation.
6. The Sharpe Ratio uses beta to measure risk-adjusted performance.
7. The market risk premium is always positive.
8. The risk-free rate is typically represented by short-term government securities.

### Answers

#### Multiple Choice Questions

1. b
2. b
3. d
4. b

### True/False Questions

1. True
2. False
3. True
4. False
5. True
6. False
7. True
8. True