Quiz 04 for Sept 7

Quiz Instructions

Complete this quiz by 11:00 a.m. U.S. Central Time on Wednesday September 7.

Question 1	1 pts

Suppose the physical probability of state s is 0.02 but the risk-neutral probability of this state is 0.01. If the risk-free interest rate is r_f=0.05, what is the stochastic discount factor for this state, m_s?

0.476

Question 2	1 pts

If the physical probability of a state s is less than the risk-neutral probability of the state s, then

○ the stochastic discount factor for state s is less than the risk-free discount factor.

○ the value of receiving a payment of 1 in state s is less than the risk-free discount factor times the physical probability of state s.

○ the primitive security price for state s is less than the product of the physical probability of state s and the risk-free discount factor.

◉ state s is a likely to be a recession.

Question 3   1 pts

Using risk-neutral probabilities of events, rather than physical probabilities of events, will produce better forecasts of the true likelihood of future economic events.

○ True

◉ False

Question 4   1 pts

The consumption-based model predicts that the date 0 price of a risk-free annuity that makes equal payments of $100 at the end of each of the next 3 years will equal
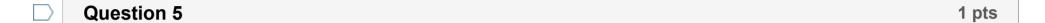
○ $100\delta \times E_0[\frac{U'(C_1)}{U'(C_0)} + \frac{U'(C_2)}{U'(C_0)} + \frac{U'(C_3)}{U'(C_0)}]$

◉ $\frac{100}{U'(C_0)} \times E_0[\delta U'(C_1) + \delta^2 U'(C_2) + \delta^3 U'(C_3)]$

$100 \times E_0 \left[\frac{\delta U'(C_1)}{U'(C_0)} + \frac{\delta^2 U'(C_2)}{U'(C_1)} + \frac{\delta^3 U'(C_3)}{U'(C_2)} \right]$

$100\delta \times E_0 \left[\frac{U'(C_1)}{U'(C_0)} + \frac{U'(C_2)}{U'(C_1)} + \frac{U'(C_3)}{U'(C_2)} \right]$

Question 5   1 pts

Ask one or more questions or make one or more comments on the material in Risk Neutral Valuation and Multiperiod Consumption-Based Valuation.

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