Quiz

1. Which one of the following statements is correct?

A. The total return on an investment is based solely on the return investors' expect to earn.
B. If an announcement is expected, the news contained in that announcement never affects the price of the stock to which it refers.
C. The market discounts information as soon as that information is expected.
D. Only news specifically about ABC stock will affect the price of ABC stock.
E. Whenever a firm announces quarterly earnings that reflect an increase from a prior period, the stock of that firm will increase in value.

International, national, political, and financial news of any kind can affect the price of ABC stock.

2. Which one of the following is most apt to cause the price of Toyland stock to decrease significantly?

A. a speech by the Federal Reserve Chairman wherein he states that holiday sales for the retail sector are running as predicted
B. an announcement by Toyland's CFO that the dividend this quarter will match expectations and increase by two percent over last quarter's dividend
C. a surprise announcement that the CFO of Toyland, who was disliked by Wall Street, has resigned
D. a written report by a respected Wall Street analyst that the growth rate of Toyland's sales is slowing more than anticipated previously
E. a news announcement that consumers' income rose sharply in the last quarter

Any news that is expected is already included in the stock price.

3. Which two of the following are most apt to be included in the expected part of a stock's return?
I. the seasonal effect of a company's sales
II. a fire at a firm's distribution center
III. the discovery of gold in a playground
IV. the passage of a new trade law increasing taxes on imported goods

A. I and II
B. III and IV
C. I and IV
D. II and III
E. I and III

Fires are not expected. Likewise, you generally wouldn't expect to find gold in a playground

4. Which one of the following is the most essential if the actual return of a security is going to equal the security's expected return?

A. an unexpected return of zero
B. the lack of any news announcements concerning the company which issued the security
C. an inflation beta of zero
D. any news announcement related to the security's issuer must be unexpected
E. an expected return equal to the expected market return

Unexpected news will most likely cause the actual return to vary from the expected return

5. Risk can be defined as:
I. the actual return minus the expected return.
II. the surprise portion of an announcement.
III. both systematic and unsystematic.

IV. the discounted portion of an announcement.

A. I and IV only
B. II and III only
C. **I, II, and III only**
D. II, III, and IV only
E. I, II, III, and IV

The discounted portion was expected.

6. The risk of an investment is most related to the:

A. total return.
B. return anticipated by investors.
C. expected return.
D. surprise portion of an event.
E. announcement of the long-anticipated retirement of an executive.

Risk is most related to unanticipated events or surprises.

7. Which of the following terms refer to the same type of risk?

I. systematic
II. specific
III. idiosyncratic
IV. unsystematic

A. I and II only
B. III and IV only
C. I and III only
D. I, II, and III only
E. II, III, and IV only

Specific and idiosyncratic refer to unsystematic risk.

8. Which one of the following would generally be considered systematic risk?

A. an increase in employment by toy manufacturers
B. a decrease in the growth rate of the GDP
C. the loss of a key company executive
D. an increase in the price of a pain medication
E. a concession by a teacher's union

This is an example of unsystematic risk.

9. Which one of the following is an example of unsystematic risk?

A. an increase in inflation
B. a reduction in the value of the dollar as compared to other key currencies
C. a decrease in interest rates by the Federal Reserve
D. a shortage of oil
E. a labor strike against a plastics firm

This is an example of systematic risk.

10. Which one of the following defines unsystematic risk?

A) $\bar{A} + \varepsilon$
B) $\varepsilon + R$
C) $m + \varepsilon$
D) $U + m + \varepsilon$
E) $\varepsilon - r$

Unsystematic risk can be defined as *m* + ε.