Questions on the Final from the Last Two Weeks of Instruction (After Exam #4)

A security that gives the holder the right to buy or sell a certain amount of an underlying financial asset at a specified price for a specified period of time is called a(n) ___________.
a) futures contract b) index contract c) options contract d) arbitrage contract

The value of an options contract comes solely from the ability of the options contract holder to participate in the price behavior of the underlying asset for a set period of time. (A=True, B=False)

Purchasers of stock options have ___________________.
a) the right to dividends paid on the underlying stock
b) a claim on the profits of the firm issuing the underlying securities
c) the obligation to buy or sell an undetermined amount of shares at the strike price
d) the right to buy or sell a certain number of underlying shares at a predetermined price

The greatest disadvantage of options is their __________________. Most options expire worthless.
a) short life span b) cost c) lack of liquidity d) difficult execution process

The seller (a.k.a. writer, maker) of a call option or a put option is the investor who _____________.
a) brokers the contract to a third party
b) sells the contract on the floor of an options exchange
c) receives the option premium and promises to buy or sell the security if the option is exercised
d) exercises the option

One reason that selling (writing) options can be a viable and profitable investment strategy is that _____.
a) the option writer collects the quarterly dividends
b) most options expire worthless and the seller gets to keep the proceeds from the sale of the option
c) an option writer determines when the option is exercised
d) an option writer can exercise the option to avoid a potential loss

The purchaser of a call option will profit if _______________.
a) the underlying security raises in price past the strike price plus the cost of the option
b) the underlying security falls in price past the strike price plus the cost of the option
c) the underlying security does not raise in price past the strike price
d) the call option expires

The purchaser of a put option will profit if _______________.
a) the underlying security raises in price past the strike price plus the cost of the option
b) the underlying security falls in price past the strike price plus the cost of the option
c) the underlying security does not fall in price past the strike price
d) the put option expires

The price of the underlying asset at which the purchaser of an options contract can make money by exercising the option is called the ____________.
a) option price b) premium price c) out-of-the-money price d) break-even price

Purchasing stock options is riskier than purchasing stocks because _______________.
a) stocks are volatile
b) option prices rise and fall
c) most options expire worthless
d) most options are exercised

In general, those who *always* make money on options are the _______________.
a) investors who purchase call options
b) investors who purchase put options
c) investors who purchase call & put options
d) (sleazy) brokers who sell the options (commissions)

One of the least riskiest ways to make money using options is to ______________. It is the only options transaction that is permitted in a retirement account. With these, you can only lose opportunity costs.
a) purchase uncovered calls on stocks you don't already own
b) sell (write) uncovered calls on stocks you don't already own
c) purchase covered calls on stocks you already own
d) sell (write) covered calls on stocks you already own

A long-lived option that gives the holder the right to buy a stock at a specified priced is called a ______.
a) warrant b) futures contract c) stock index option d) preferred stock

Futures contracts ___________________.
a) allow producers and consumers of commodities to lock in profits and costs
b) create opportunities for tremendous gains and tremendous losses with very little capital
c) are now available for various currencies, interest rate indexes and stock indexes
d) all of the above

The seller (usually the producer of the commodity) of a futures contract _______________.
a) has the option of canceling the contract the following day if the price is not acceptable to him/her
b) is legally bound to make delivery of the specified item on the specified date at the specified price
c) receives the entire contract amount at the time the contract is made
d) must make delivery before receiving any monies on the contract

The purchaser (usually the consumer of the commodity) of a futures contract _______________.
a) has the option of canceling the contract the following day if the price is not acceptable to him/her
b) is legally bound to take delivery of the specified item on the specified date at the specified price
c) receives the entire contract amount at the time the contract is made
d) must take delivery before receiving any monies on the contract

The buying and selling of options on futures contracts is now available, insuring numerous opportunities for more commissions for brokers and more losses for speculating investors. (A=True, B=False)

The type of account in which all transactions are made on a strictly cash basis is called a __________.
a) margin account b) short account c) cash account d) long account

The type of account in which transactions can be performed using money borrowed from the brokerage firm and securities can be bought and sold on credit is called a __________.
a) margin account b) short account c) cash account d) long account

Which one of the following is an advantage of a margin account?
a) the reduction in potential diversification
b) the ability to borrow from your investments
c) the possibility of magnified losses
d) the high rate of interest charged on the loans

The purchase of stock with 50% cash and 50% borrowed money in the hope of magnifying profits if the stock goes up is known as taking a _____________________.
a) long position in the stock
b) short position in the stock
c) long, margined (a.k.a. leveraged) position in the stock
d) short, margined (a.k.a. leveraged) position in the stock.

Which one of the following is the *greatest* disadvantage of long margined positions?
a) the reduction in potential diversification
b) the ability to borrow from your investments
c) the possibility of magnified losses
d) the high rate of interest charged on the loans

Assume that the amount of equity in Luke Busy's margin account has dipped below the maintenance margin. Mr. Busy's brokerage firm has called to tell him that he has three business days in which to bring the equity up to the initial margin. If Mr. Busy cannot do so, the brokerage firm will then sell enough of Mr. Busy's leveraged holdings to bring his account back into line. In this situation, Mr. Busy is said to have received ___________.
a) a margin call b) a restriction warning c) an excess margin alarm d) a margin warning

Anne Egg recently purchased XYZ stock on 60 percent margin. This information indicates that _____.
a) 60 percent of the investment was financed with Anne's own capital
b) Anne has limited her losses by 40 percent
c) Anne can not lose more than 60 percent of the money she has invested
d) Anne can not lose more than 40 percent of the money she has invested

Which of the following are characteristics of short selling?
I. Borrowing shares of stock from other investors through your brokerage firm.
II. Selling shares of stock you do not own.
III. Hoping the stock price will increase.
IV. Hoping the stock price will decrease.
a) I and II only b) III and IV only c) I, II and IV only d) I, II, and III only

The *major* advantage of selling a stock short is that the investor ______________.
a) eliminates his or her risk exposure
b) earns the security's dividend or interest income
c) can profit from a drop in the stock's price
d) can eliminate capital gain taxes on realized profit

The *major* disadvantage of selling a stock short is that ______________.
a) the investor must purchase the stock back
b) the investor does not get the entire sale proceeds
c) the short investor must use a margin account
d) there is no limit to how much money can be lost!

The major difference(s) between regular taxable accounts and retirement tax-qualified accounts is / are:
I. Taxable accounts pay taxes each year; retirement accounts are either tax-deferred or tax-free.
II. There are restrictions on how much can be contributed per year to a retirement account.
III. There are restrictions on what type of financial assets can be held in a retirement account.
IV. There are no restrictions on how much or what type of asset can be held in a taxable account.
a) I and II only b) III and IV only c) I, II and IV only d) I, II, III & IV

An ______ is an insurance product that guarantees an income for life or a certain period. The insurance company usually purchases mutual funds on your behalf and charges very high fees for their service.
a) stock b) bond c) option d) annuity e) Roth IRA

Gold and other precious metals, diamonds and precious gems, and art and other collectibles should be only a small portion of an investor's portfolio unless the investor is intimately involved with the items. Long term capital gains taxes are higher for these items than they are for financial investments. (A=True, B=False)

A ______ is a company that develops, owns, and manages commercial or residential real estate. All the earnings of the company are passed through to the investors. Liquidity and diversification are not a problem with these investments (as they are when you directly own the real estate investment).
a) real estate mutual fund
b) real estate investment trust (REIT)
c) real estate brokerage firm
d) real estate options contract