## Question #1 of 9

Question ID: 1574514

In order to value an option with a one-period binomial model, three things an analyst would need to know are:

**A)** the risk-adjusted discount rate, the volatility of the price of the underlying asset, and option exercise price.

**B)** the risk-free rate, the volatility of the price of the underlying, and the current asset price.

**C)** the probability of an up-move, the option exercise price, and the current asset price.

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## Question #2 of 9

Question ID: 1577434

If a European put option is trading at a higher price than that implied from the binomial model, investors can earn a return in excess of the risk-free rate by:

**A)** buying the underlying, selling the call, and investing at the risk-free rate.

**B)** selling the underlying, buying the call, and investing at the risk-free rate.

**C)** buying the underlying, buying the call, and borrowing at the risk-free rate.

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## Question #3 of 9

Question ID: 1574515

We can use the risk-free rate to value an option with a one-period binomial model because:

**A)** combining options with the underlying asset in a specific ratio will produce a risk-free future payment.

**B)** combining put and call options in specific ratio can produce a risk-free future payment.

**C)** options investors are risk-neutral, on average.

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## Question #4 of 9

Question ID: 1574517

Consider a stock that will have a value of either 22 or 14 one year from now. If the risk-free rate is 5%, what is the ratio of shares to short call options with an exercise price of 18 for a portfolio that will have the same value at expiration regardless of the stock price at the end of the year?

**A)** 0.48.

**B)** 0.53.

**C)** 0.50.

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## Question #5 of 9

Question ID: 1574516

One method of valuing a call option with a one-period binomial model involves:

**A)** using the probabilities of an up-move and a down-move to get the expected value of the payment at expiration.

**B)** discounting the average call value at expiration by the risk-free rate.

**C)** finding a combination of the call option and the underlying that will have the same value regardless of the price of the underlying at expiration.

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## Question #6 of 9

Question ID: 1577435

An option's value is affected by:

**A)** expected probabilities of underlying price increases or decreases only.

**B)** actual probabilities of underlying price increases or decreases only.

**C)** both actual and expected probabilities of underlying price increases or decreases.

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## Question #7 of 9

Question ID: 1577431

Which of the following statements best describes the effect on the no-arbitrage price of a call option on Drinsky Inc. (Drinsky) shares? A decrease in the risk-free rate will:

**A)** increase Drinsky's call option price.

**B)** have no effect on Drinsky's call option price.

**C)** decrease Drinsky's call option price.

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## Question #8 of 9

Question ID: 1577433

A stock's price is currently $30 and at the end of three months when its options expire, the stock price is expected to either go up or down by 10%. What is the value of a call option with a strike price of $31?

**A)** $0.70.

**B)** $1.30.

**C)** $1.00.

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## Question #9 of 9

Question ID: 1577432

Which of the following statements regarding risk-neutrality is *most accurate*?

**A)** Risk-neutral pricing requires using expected return to price an option.

**B)** Risk-neutral probabilities are determined by investor views on risk and the risk-free rate.

**C)** Risk-neutral pricing can be applied to any model that uses future underlying asset price movements.