**PRACTICE TEST KEY**

**Objective A**

1. Being risk-tolerant means being a risk-taker or having a positive attitude toward risk. (1 point)

2. Being risk-averse means being a risk-avoider or having a negative attitude toward risk. (1 point)

3. People risk money on investments for the possibility of earning a return. (1 point)

4. The three factors that determine an investor’s risk tolerance are goals (what s/he is trying to accomplish by investing), time frame (how long s/he has to accomplish these goals), and personality (attitude toward risk). (6 points; 2 points each)

5. One way for investors to put investment risk in perspective is to look at the risk pyramid, a graphic way of comparing investments. With high-, moderate-, and low-risk categories, the pyramid helps them to see which investments are more or less risky than others. Near the peak are the most risky investments, while at the base are the most reliable returns. If an investment is located near the middle of the pyramid—but the investor thinks s/he can handle more risk—s/he might select an investment closer to the peak. If s/he feels that s/he can’t   
afford any large losses right now, s/he might choose an investment closer to the base. When investors visualize how likely it is that they’ll receive a particular return, they can see which selection is the best choice to move them toward their goals. (2 points)

6. Investors who can’t handle much risk put their money into lending investments. With a lending investment,you allow someone to borrow your money for a period of time—for a price. The extra money you receive provides the motivation for lending. (3 points)

7. A savings account is a lending investment in which an individual lends money to a bank to earn interest. (3 points)

8. Answers will vary but should include at least one advantage and one disadvantage of investing in savings accounts: (6 points; 3 points each)

• Advantages:

◦ Easy access

◦ Interest (return)

◦ Indefinite time period

◦ FDIC insured

• Disadvantages:

◦ Low rate of return

◦ Rate of return even lower than inflation

◦ Limited to six withdrawals per month

**PRACTICE TEST KEY** (cont’d)

9. A money market account is a lending investment in which an individual lends a minimum amount of money to a bank to earn interest. It is similar to a savings account. (3 points)

10. Answers will vary but should include at least one advantage and one disadvantage of investing in money market accounts: (6 points; 3 points each)

• Advantages:

◦ Interest (return)

◦ Indefinite time period

◦ FDIC insured

◦ Check writing

◦ *Should* have a better return than savings account

• Disadvantages:

◦ May be allowed fewer withdrawals than savings account

◦ May have a minimum balance requirement

◦ Often, no better return than savings account

11. A certificate of deposit is a lending investment in which an individual lends money to a bank to earn a set rate of interest for a specified period of time. (3 points)

12. Answers will vary but should include at least one advantage and one disadvantage of investing in certificates of deposit: (6 points; 3 points each)

• Advantages:

◦ Guaranteed rate of return

◦ Higher return than savings or money market account

• Disadvantage—Can’t access money before the end of the time period without penalty

13. A bond is a lending investment in which an individual lends money to a government, municipality, or corporation to earn a set rate of interest for a specified time period. (3 points)

14. Answers will vary but should include at least one advantage and one disadvantage of investing in bonds: (6 points; 3 points each)

• Advantages:

◦ Very low risk

◦ Guaranteed rate of return

◦ No penalty for early withdrawal

• Disadvantages:

◦ Loss of interest upon early withdrawal

◦ May take a long time to receive full return

**PRACTICE TEST KEY** (cont’d)

**Objective B**

15. Investors who are not afraid of risk often put their money into ownership investments—   
investments that provide owners’ rights in return. Each ownership investment provides an opportunity for a return by letting the investor own something of significance. (3 points)

16. A stock is a share or unit of ownership in a corporation. (3 points)

17. Answers will vary but should include at least one advantage and one disadvantage of investing in stocks: (6 points; 3 points each)

• Advantages:

◦ Ownership rights such as voting

◦ May be able to sell stock for profit

• Disadvantages:

◦ May *not* be able to sell stock for profit

◦ May even lose initial investment

18. A mutual fund is an ownership investment in which a variety of securities from different corporations or agencies (usually from different industries) are combined into one investment. (3 points)

19. Answers will vary but should include at least one advantage and one disadvantage of investing in mutual funds: (6 points; 3 points each)

• Advantages:

◦ Less risk than owning individual stocks or securities

◦ Expertise of fund managers

• Disadvantages:

◦ Potential fund manager mistakes

◦ Fees

20. Real estate is an ownership investment in which individuals purchase property in buildings and land. (3 points)

21. Answers will vary but should include at least one advantage and one disadvantage of investing in real estate: (6 points; 3 points each)

• Advantage—potential appreciation

• Disadvantage—potential depreciation

22. Entrepreneurship is starting, building, and owning a business. (3 points)

**PRACTICE TEST KEY** (cont’d)

23. Answers will vary but should include at least one advantage and one disadvantage of entrepreneurship as an investment: (6 points; 3 points each)

• Advantage—potential for huge return on investment

• Disadvantage—potential for huge loss/failure, not just financially

24. Collectibles are objects or items collected by someone who has an interest in the sport,   
activity, etc.; in investing, the collector hopes to eventually resell the items at a profit. (3 points)

25. Answers will vary but should include at least one advantage and one disadvantage of investing in collectibles: (6 points; 3 points each)

• Advantages:

◦ Personal interest/hobby

◦ Potential for high return

• Disadvantages:

◦ No guarantee people will want to buy the item(s)

◦ No guarantee people will pay more for them in the future than now

26. Individuals aren’t the only ones who make investments. Businesses and other organizations do as well, and why wouldn’t they? They want to grow their wealth just as individuals do. Most businesses’ main form of investment is investing back into the company itself—researching and developing new products, purchasing the latest and most efficient technologies, expanding into new markets, etc. However, businesses also participate in other forms   
of investing—they may put cash into savings or money market accounts, purchase bonds or stocks, or buy real estate. Sometimes, businesses invest money that isn’t their own. A common example is a non-profit organization’s endowment fund. Funds obtained from donors are pooled together and invested to create additional income. A great number of colleges   
and universities have endowment funds. (2 points)

**Suggested** Criterion Level**:** 80 points