#1-12A

EASY INTERMEDIATE HARD

CFA® SAMPLE QUESTION – LEVEL I

Derivatives

Q: The motivation for selling a stock short is MOST LIKELY to:

CORRECT ANSWER:

ⓐ Profit from an expected decline in the stock's price.

The typical motivation of an investor in selling a stock short is the expectation that the stock price will decline. The investor can profit from the expected price decline by selling at a higher price now and then covering his or her position by purchasing the stock later at a lower price.

Choice "b" is incorrect. This would close out a position. Short selling involves selling a security that is not owned.

Choice "c" is incorrect. Downside risk is not limited by selling a stock short. The upside potential for a stock is theoretically unlimited. Thus, the short seller has unlimited downside risk, as he or she loses money when the stock price rises.

CFA Society Hong Kong Candidate Services

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