CFA® SAMPLE QUESTION – LEVEL I

Portfolio Management

Q: A portfolio manager adds a new stock that has the same standard deviation of returns as the existing portfolio but has a correlation coefficient with the existing portfolio that is less than +1. Adding this stock will have what effect on the standard deviation of the revised portfolio's returns?

The standard deviation will:

CORRECT ANSWER:

ⓑ **decrease.**

If the correlation coefficient is less than 1, there are always benefits to diversification. Thus, adding the stock will reduce the portfolio's standard deviation.

CFA Society Hong Kong
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Date of issue:
1 Jan 2024