

## Money Smarts Quiz

ADAPTED FROM: <http://www.sec.gov/investor/tools/quiz.htm>

1. If you buy a company's stock,
  - a. you own a part of the company
  - b. you have lent money to the company
  - c. you are liable for the company's debts
  - d. the company will return your original investment to you with interest
  
2. Over the past 70 years, the type of investment that has earned the most money, or the highest rate of return, for investors has been
  - a. stocks
  - b. corporate bonds
  - c. savings accounts
  - d. Certificates of Deposit
  
3. If you buy the stock of a new company,
  - a. you cannot lose money
  - b. you can lose all the money you used to buy the stock
  - c. you can lose only a portion of the money you used to buy the stock
  - d. don't know
  
4. Monique owns a wide variety of stocks, bonds, and mutual funds to lessen her risk of losing money. This is called
  - a. saving
  - b. compounding
  - c. diversifying
  - d. don't know
  
5. Carlos has saved some cash and faces these choices. What would be the best thing for him to do?
  - a. put it in his savings account
  - b. invest in a mutual fund
  - c. buy a U.S. Savings bond
  - d. pay off the balance on his credit card that charges 18% interest
  
6. Maria wants to have \$100,000 in 20 years. The sooner she starts to

save, the less she'll need to save because

- the stock market will go up
- interest rates will go up
- interest on her savings will start compounding
- Inflation historically decreases over time

7. Jamal is 22 years old and wants to start saving now for his retirement in 43 years. Of these choices, where should Jamal put most of his money now for this long-term goal?
- a savings account at the bank
  - a checking account at the bank
  - a mutual fund that invests in stocks
  - the stock of one company

8. Federal and state laws protect investors by requiring companies to
- show profits before they can sell stock
  - give investors important information
  - pay dividends
  - repay investors who have lost money

### **Money Smarts Quiz Answer Key**

**1. - A.** When you own stock, you own a part of the company. There are no guarantees of profits, or even that you will get your original investment back, but you might make money

in two ways. First, the price of the stock can rise if the company does well and other investors want to buy the stock. If a stock's price rises from \$10 to \$12, the \$2 increase is called a *capital gain* or *appreciation*. Second, a company sometimes pays out a part of its profits to stockholders – that's called a *dividend*. If the company doesn't do well, or falls out of favor with investors, your stock can fall in price and the company can stop paying dividends, or make them smaller.

**2. - A.** If you had invested \$1 in the stocks of large companies in 1925 and you reinvested all dividends, your dollar would be worth \$2,350 at the end of 1998. If the same dollar had been invested in corporate bonds, it would be worth \$61, and if it had been invested in U.S. Treasury bills, it would be worth \$15. (This information came from Ibbotson Associates, Inc.)

**3. - B.** One of the riskiest investments is buying stock in a new company. New companies go out of business more often than companies that have been in business for a long time. If you buy stock in small, new companies, you could lose it all. Or the company could turn out to be a success. You'll have to do your homework and learn as much as you can about small companies before you invest. If you decide to buy stock in a new or small company, only invest money that you can afford to lose.

**4. - C.** One of the most important ways to lessen the risk of losing money when you invest is to *diversify* your investments. It's common sense – don't put all your eggs in one basket. If you buy a mixture of different types of stocks, bonds, or mutual funds, your entire savings will not be wiped out if one of your investments fails. Since no one can accurately predict how our economy or one company will do, diversification helps you to protect your savings.

**5. - D.** Most advisers suggest that before you start to invest, you should save cash for emergencies and pay down any debt you have. If Carlos has money in a savings account or buys a U.S. savings bond, he'll earn 3 to 5% on his savings. Mutual funds are not guaranteed, and they may earn or lose money. But if Carlos pays off his credit card, it's like earning 18% because that's how much he's paying now to maintain the balance. If you owe money on your credit cards, you save money if you pay off the balance in full or as quickly as possible.

**6. - C.** When you leave the interest in your account or reinvest the money you earn on your investments, the money you earn starts to earn money too. Over time, the magic of *compounding* works, allowing your money to grow with dramatic results. The more time you have to save, the less money you need to save because of compounding. And the longer you wait to start saving, the more you have to spend to reach your goal. For example, let's assume that Maria's savings grow by 5% a year. If she starts to save \$243 a month now, it will cost her \$58,320 to have \$100,000 in twenty years. If she waits 10 years to start saving, she will have to save \$644 a month for 10 years, and it will cost her \$77,280 to reach \$100,000 in twenty years.

**7. - C.** As you read in the answer to question three, over the long term, stocks have earned more money than any other investment. Since Jamal doesn't need his money for a long time, he can afford to take on the risk of investing in stocks. Even if the stocks in his fund go up and down in value, chances are his savings will grow in value over the long term. He lessens the risk of losing money by choosing a diversified mutual fund rather than the stock of one company.

**8. - B.** Most businesses that raise money from the public must register with the SEC or the states and publicly report important information about their businesses on a regular basis. Federal and state laws protect you by requiring that the people who seek your investment dollars must tell you the truth about their businesses, and the people who sell securities must be licensed and treat you fairly and honestly, putting your interests first.