

**Economics 70, Personal Finance:
Making Better Decisions and Building a Better Financial System**

Assignment 11, due on Canvas by 11:59pm on Wednesday November 29

1. Choosing a health insurance plan

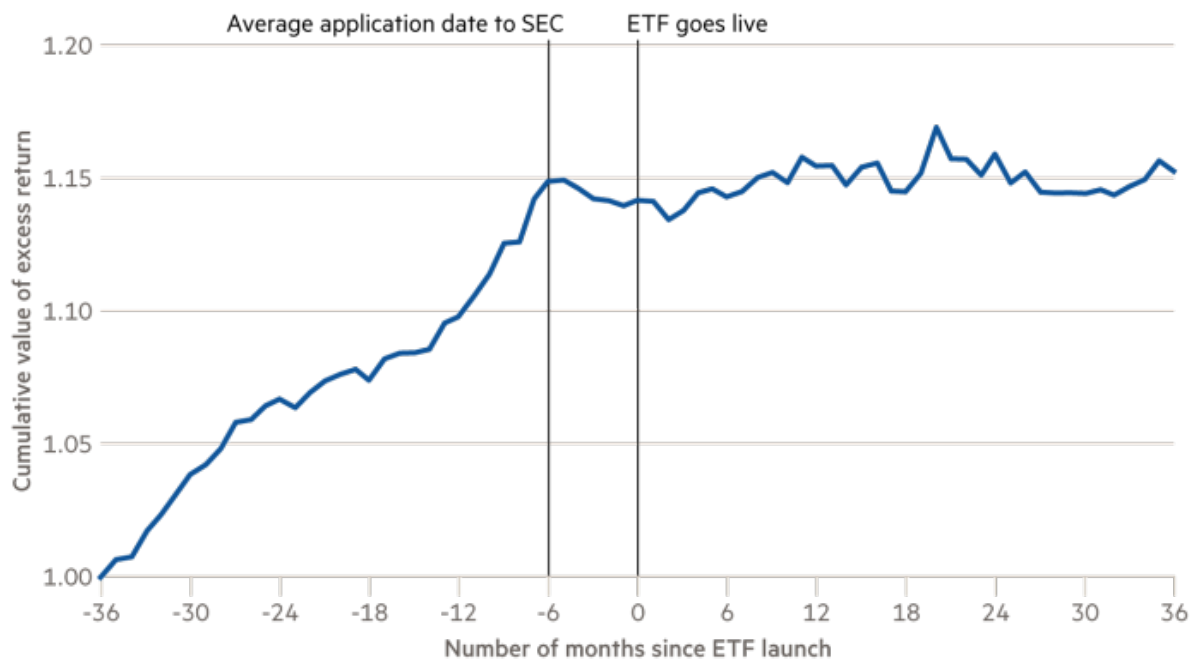
- Review the information on p.410 of Kapoor et al, immediately following question 6. (For clarification, the POS option c is an add-on to the HMO in option b.)
- Using this information, answer questions 7, 8, and 9 on p.410.
- Comment on the tradeoff Ron faces between medical costs and the flexibility to continue with his general physician.

2. Past performance and future results

A recent article in the Financial Times shows this figure:

Live performance of many ETFs fails to live up to model's promise

Relative performance vs indices three years before and after launch



Source: Research Affiliates
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- a) What is the average annualized excess return on the ETFs in this sample, relative to passive index investments, in the 30 months before their creators apply to register them with the SEC?
- b) What is the average annualized excess return on these ETFs in the 42 months after that date?
- c) What do you think accounts for the difference?
- d) Suppose a fund marketer shows you that the investment strategy used by an ETF has outperformed a passive index in the past, with an average excess return that is statistically significant given the standard deviation of the return. Comment on how you might interpret this if you know that some of the data come from a period before the ETF was established.
- e) Comment on how you might interpret the situation in part d) if you know that some of the data come from a period during which the ETF was in existence but with very low asset value, and that the marketer's fund family sponsors many different ETFs.

3. Looking carefully at a “can’t lose” investment product

Your elderly aunt tells you that a salesman has offered her a structured investment product that “can’t lose!” It requires investing for 5 years, at the end of which time you receive either your money back, or your money multiplied by 90% of the ratio of the S&P index level in 5 years to the S&P index level today, whichever is greater.

Your aunt says the salesman explained “If the stock market falls, you won’t lose any money. If it goes up, you’ll get most of the upside. So you can only make money, you can’t lose any!”

- a) Compare this product to a 5-year investment in a bank savings account or money market fund. Can this product do worse over 5 years? Explain.
- b) Compare this product to a 5-year investment in an S&P 500 index fund. If the S&P 500 index goes up, does the product deliver 90% of the return of the index fund? Explain.
- c) Are there other aspects of this product that should be considered when comparing it with a bank savings account or money market fund, or with an S&P 500 index fund?