

### Question #1 of 16

Question ID: 1210885

A trader that places numerous false orders on one side of the market in order to incite other market participants into trading with a real order on the other side of the market is *most likely* to be accused of:

A) layering.



B) gunning the market.



C) wash trading.



#### Explanation

Layering (also known as spoofing) is a quote stuffing strategy intended to use sham orders to trick other market participants into trading with real orders on the other side of the market. Gunning the market is a strategy used by market manipulators to cause other traders to enter into disadvantageous trades. In wash trading, a trader will rapidly buy and sell the same security in an attempt to artificially inflate the demand for the security.

(Study Session 17, Module 48.4, LOS 48.j)

#### Related Material

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### Question #2 of 16

Question ID: 1210880

The results of liquidity aggregation are *most likely* to be referred to as a:

A) "dark pool".



B) "super book".



C) "parent order".



#### Explanation

Liquidity aggregation refers to the process of monitoring a number of trading venues and then compiling the data into a "super book" that summarizes price and liquidity across these markets. This allows trades to be routed appropriately. A dark pool is a trading venue that is only open to certain clients, and that does not publish its liquidity. A parent order is a large order (e.g. buy 1 million shares of Facebook) that is divided up by an execution algorithm into smaller child orders that are less likely to move the market.

(Study Session 17, Module 48.2, LOS 48.e)

#### Related Material

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### Question #3 of 16

Question ID: 1210872

Which of the following trading costs is *NOT* an explicit cost?

A) Market impact costs.



B) Commissions.



C) Stamp duties.



#### Explanation

The explicit costs in a trade are readily discernable and include commissions, taxes, stamp duties, and fees. Implicit costs sometimes cannot be measured as easily but do exist. They include the bid-ask spread, market or price impact costs, opportunity costs, and delay costs (a.k.a. slippage costs).

(Study Session 17, Module 48.1, LOS 48.a)

#### Related Material

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### Question #4 of 16

Question ID: 1210877

Which of the following trading costs results when an order is not filled?

A) Price impact costs.



B) Market impact costs.



C) Delay costs.



#### Explanation

When an order is not filled, delay or slippage costs result. These costs can be substantial if information regarding the security is released while the order sits unfilled.

(Study Session 17, Module 48.1, LOS 48.b)

#### Related Material

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### Question #5 of 16

Question ID: 1210881

Algorithms are *least likely* to adapt to market fragmentation by incorporating:

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A) intelligent smart order routing capabilities



B) liquidity aggregation capabilities



C) basket trading capabilities



#### Explanation

Basket trading is not a solution to market fragmentation, but rather is an algorithm used for statistical arbitrage. Algorithms can adapt to market fragmentation if the algorithm includes intelligent smart order routing capabilities and/or liquidity aggregation capabilities.

(Study Session 17, Module 48.2, LOS 48.e)

#### Related Material

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### Question #6 of 16

Question ID: 1210876

If the volume-weighted average price (VWAP) during a day was \$21 and 100 shares were bought at \$20.40, which of the following statements regarding the costs of trading is *most* accurate?

A) The explicit costs are -\$60.



B) The implicit costs are \$60.



C) The implicit costs are -\$60.



#### Explanation

Implicit costs are usually measured using some benchmark, such as the VWAP. VWAP is a weighted average of security prices during a day, where the weight applied is the proportion of the day's trading volume. If the VWAP during a day was \$21 and 100 shares were bought at \$20.40, then the estimate of the implicit cost would be  $100 \times (\$20.40 - \$21.00) = -\$60$ . The explicit costs in a trade are the commissions, taxes, stamp duties, and fees.

(Study Session 17, Module 48.1, LOS 48.b)

#### Related Material

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### Question #7 of 16

Question ID: 1210884

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A trader that arranges for the same security to be traded among several commonly controlled accounts to create the impression of market activity at a particular price is *most likely* to be accused of:

**A)** quote stuffing.



**B)** gunning the market.



**C)** wash trading.



#### Explanation

Gunning the market is a strategy used by market manipulators to cause other traders to enter into disadvantageous trades. In wash trading, a trader will rapidly buy and sell the same security in an attempt to artificially inflate the demand for the security. Quote stuffing refers to a trader distracting and disadvantaging other algorithms by placing a great quantity of fictitious orders and then cancelling them almost immediately.

(Study Session 17, Module 48.4, LOS 48.j)

#### Related Material

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### Question #8 of 16

Question ID: 1210883

An electronic trading strategy that is common when dealers are willing to trade at better prices than they quote, *most* accurately describes:

**A)** flickering quotes.



**B)** leapfrogging.



**C)** hidden orders.



#### Explanation

Quote leapfrogging occurs when a dealer quotes a wide spread, but then offers a better price in response to other traders offering better prices. Flickering quotes are exposed limit orders that electronic traders submit and then cancel shortly thereafter. Larger traders submit hidden orders when they do not want to reveal their standing orders to the markets.

(Study Session 17, Module 48.3, LOS 48.g)

#### Related Material

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Which of the following implementation shortfall components is *NOT* influenced by market-wide movements?

- A) Explicit costs. 
- B) Realized profit and loss. 
- C) Missed trade opportunity cost. 

#### Explanation

The realized profit and loss and missed trade opportunity cost are all affected by market movements that the manager should not be held accountable for. For example, if the security increases due to market-wide movements, the trader should not be held responsible for this non-security specific change in price. Market-wide movements can be adjusted for by the market model.

(Study Session 17, Module 48.1, LOS 48.c)

#### Related Material

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### Question #10 of 16

Question ID: 1210886

A trader that has advance information about a large buy-side order is *most likely* to attempt to profit from the large trade's market impact through the market manipulation known as:

- A) quote stuffing. 
- B) front running. 
- C) gunning the market. 

#### Explanation

Front running orders refers to a situation where a trader that has advance information about a large buy-side order, and trades ahead of that order in an attempt to profit from the large trade's market impact. Gunning the market is a strategy used by market manipulators to cause other traders to enter into disadvantageous trades. Quote stuffing refers to a trader distracting other algorithms by placing a great quantity of fictitious orders and then cancelling them almost immediately.

(Study Session 17, Module 48.4, LOS 48.j)

#### Related Material




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## Question #11 of 16

Question ID: 1210878

Which of the following is *least* accurate regarding VWAP? VWAP:

- A) does not account for market movements or trade volume. 
- B) is applicable to small and large trades. 
- C) does not evaluate delayed or unfilled orders. 

### Explanation

The advantages of VWAP are that it is easily understandable, computationally simple, can be applied quickly to enhance trading decisions, and is most appropriate for small trades in nontrending markets. The disadvantages of VWAP are that it is not informative for trades that dominate trading volume, it can be gamed by traders, it does not evaluate delayed or unfilled orders, and does not account for market movements or trade volume.

(Study Session 17, Module 48.1, LOS 48.b)

### Related Material




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## Question #12 of 16

Question ID: 1210874

Suppose a trader is quoted a market bid price of \$16.00 and an ask of \$16.10. The execution price of a sell order is \$16.03. What is the effective spread?

- A) \$0.02. 
- B) \$0.03. 
- C) \$0.04. 

### Explanation

If a trader placed a sell order, a dealer may offer a better bid price than the previous bid to earn the trader's business. The midquote of the quoted bid and ask prices is \$16.05. The effective spread for this sell order would then be calculated as:  $2 \times (\$16.05 - \$16.03) = \$0.04$ , which is 6 cents better than the quoted spread of \$0.10 (\$16.10 - \$16.00).

(Study Session 17, Module 48.1, LOS 48.b)

### Related Material

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## Question #13 of 16

Question ID: 1210873

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Suppose a trader is quoted a market bid price of \$40.40 and an ask of \$40.49. The execution price of a buy order is \$40.47. What is the effective spread?

A) \$0.025.



B) \$0.090.



C) \$0.050.



#### Explanation

If a trader placed a buy order, a dealer may offer a better ask price than the previous ask to earn the trader's business. The midquote of the quoted bid and ask prices is \$40.445. The effective spread for this buy order would then be calculated as:  $2 \times (\$40.47 - \$40.445) = \$0.05$ , which is 4 cents better than the quoted spread of \$0.09 (\$40.40 - \$40.49).

(Study Session 17, Module 48.1, LOS 48.b)

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### Question #14 of 16

Question ID: 1210882

An electronic trader that tries to profit by exploiting the option value of standing orders is *most* accurately categorized as an electronic:

A) arbitrageur.



B) front runner.



C) quote matcher.



#### Explanation

Electronic quote matchers attempt to exploit the option values of standing orders (i.e. limit orders waiting to be filled.) Standing orders allow quote matchers to limit the losses on positions they take. If prices move in the quote matcher's favor, they profit. If prices move against the quote matcher, they can exit by trading using the standing orders.

(Study Session 17, Module 48.2, LOS 48.f)

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### Question #15 of 16

Question ID: 1210875

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Suppose a trader is quoted a market bid price of \$30.00 and an ask of \$30.07. The execution price of a buy order is \$30.04. What is the effective spread?

A) \$0.01.



B) \$0.06.



C) \$0.02.



#### Explanation

If a trader placed a buy order, a dealer may offer a better ask price than the previous ask to earn the trader's business. The midquote of the quoted bid and ask prices is \$30.035. The effective spread for this buy order would then be calculated as:  $2 \times (\$30.04 - \$30.035) = \$0.01$ , which is 6 cents better than the quoted spread of \$0.07 ( $\$30.07 - \$30.00$ ).

(Study Session 17, Module 48.1, LOS 48.b)

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### Question #16 of 16

Question ID: 1210887

Suppose that a market manipulator sells a particular security quickly to push prices down in order to trigger stop-loss sell orders that other market participants have in place, in order for the manipulator to profit by repurchasing that security at lower prices. This abusive trading practices is *most likely* to be classified as:

A) gunning.



B) squeezing.



C) cornering.



#### Explanation

Gunning the market is a strategy where a manipulator tries to push prices down, in order to trigger stop-loss sell orders that will allow the manipulator to purchase the security at lower prices. In a squeeze or corner, the manipulator obtains control over resources necessary to settle trading contracts, then unexpectedly withdraws those resources from the market.

(Study Session 17, Module 48.4, LOS 48.j)

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