Topic in CFA Level III

Session	Content
Study Session 1-2	ETHICS & PROFESSIONAL STANDARDS (1)&(2)
Study Session 3	BEHAVIORAL FINANCE
Study Session 4	**CAPITAL MARKET EXPECTATIONS【NEW】**
Study Session 5	ASSET ALLOCATION AND RELATED DECISIONS IN PORTFOLIO MANAGEMENT
Study Session 6	DERIVATIVES AND CURRENCY MANAGEMENT 【NEW】
Study Session 7-8	FIXED-INCOME PORTFOLIO MANAGEMENT (1)&(2)
Study Session 9-10	EQUITY PORTFOLIO MANAGEMENT (1)&(2)
Study Session 11	ALTERNATIVE INVESTMENTS FOR PORTFOLIO MANAGEMENT 【NEW】
Study Session 12-13	PRIVATE WEALTH MANAGEMENT (1)&(2) 【NEW】
Study Session 14	PORTFOLIO MANAGEMENT FOR INSTITUTIONAL INVESTORS 【NEW】
Study Session 15	TRADING, PERFORMANCE EVALUATION, AND MANAGER SELECTION 【NEW】
Study Session 16	CASES IN PORTFOLIO MANAGEMENT AND RISK MANAGEMENT 【NEW】

Framework

Applications of Capital Market Expectations

- **SS4: Capital Market Expectations**
  - R10 Capital Market Expectations, Part 1: Framework and Macro Considerations
  - R11 Capital Market Expectations, Part 2: Forecasting Asset Class Returns

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Framework

Equity Portfolio Management

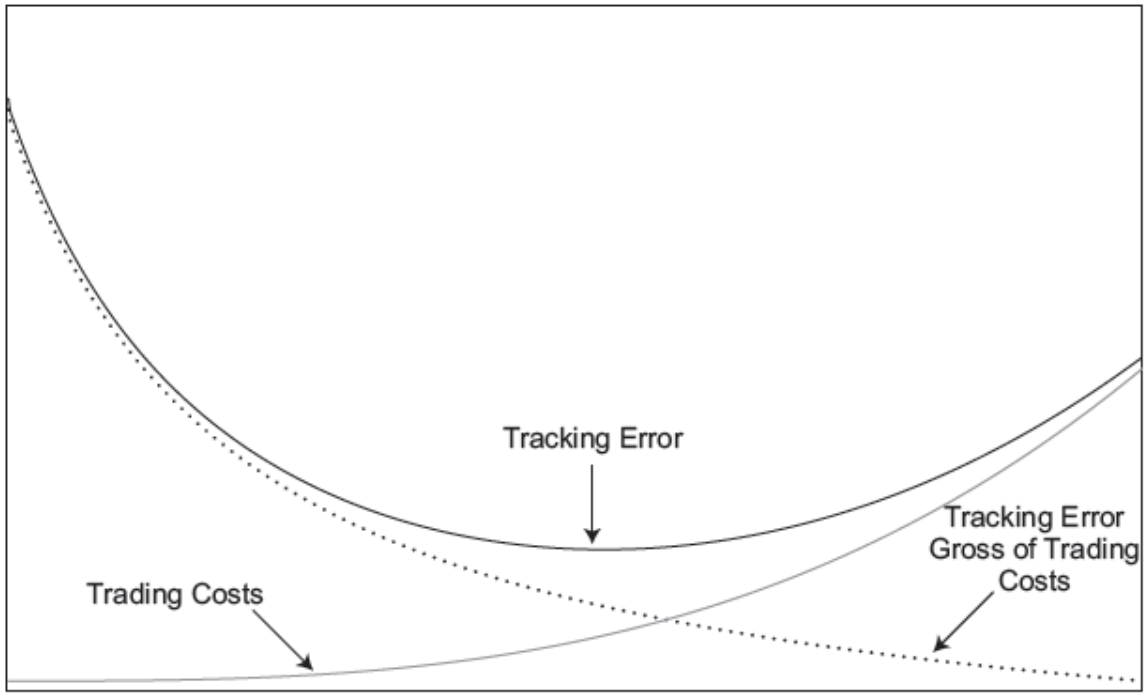
- **SS9: Equity Portfolio Management (1)**
  - R22 Overview of Equity Portfolio Management
  - R23 Passive Equity Investing
- **SS10: Equity Portfolio Management (2)**
  - R24 Active Equity Investing: Strategies
  - R25 Active Equity Investing: Portfolio Construction

Factor-Based Strategies

Factor	Description
Growth	stocks with high P/E, high P/B and above-average net income growth.
Value	stocks of mature companies with low P/E, low P/B, stable net income, and/or high dividend yield.
Size	stocks with low floating-adjusted market caps.
Yield	high dividend-yield stocks may provide higher excess returns in low interest rate environments like during the market collapse in 2008 and 2009.
Momentum	stocks with recent above-average returns.
Quality	stocks with consistent earnings and dividend growth, high cash flow-to-earnings and low debt-to-equity.
Volatility	stocks with low standard deviation of returns.

Portfolio Construction

- Full replication can be costly when there are large numbers of stock and liquidity is limited.
  - The portfolio must be regularly reconstituted and rebalanced.
  - The **advantage** of full replication is that it closely matches the index return (before transaction costs).



Approaches to Active Management

➢ Differences between Fundamental and Quantitative Approaches

	Fundamental	Quantitative
Style	Subjective	Objective
Decision-making process	Discretionary	Systematic, non-discretionary
Primary resources	Human skill, experience, judgment	Expertise in statistical modeling
Information used	Research (company/industry/economy)	Data and statistics
Analysis focus	Conviction (high depth) in stock-, sector-, or region-based selection	A selection of variables, subsequently applied broadly over a large number of securities
Orientation to data	Forecast future corporate parameters and establish views on companies	Attempt to draw conclusions from a variety of historical data
Portfolio construction	Use judgment and conviction within permissible risk parameters	Use optimizers

Equity style analysis - Comparison of 2 tech.

	Advantages	Disadvantages
Return-based	● Does not require information on holdings. ● Can be easily and universally applied	● Generally more accurate because it uses actual portfolio holdings. ● Assesses each individual holding's contribution to style.
Holding-based	● Constraints on outputs can limit detection of extreme styles.	● Requires the availability of all portfolio constituents and style attributes of each. ● Limited derivatives data may hinder analysis if derivatives are used. ● Different systems with different definitions of style will classify the same portfolio in different ways.

Approaches to Portfolio Construction

A Summary of the Different Approaches

	Top-Down		
Systematic	• Emphasizes macro factors • Factor timing • Diversified	• Emphasizes macro factors • Factor timing • Diversified or concentrated depending on strategy and style	Discretionary
	• Emphasizes security specific factors • No factor timing • Diversified	• Emphasizes firm specific characteristics or factors • Potential factor timing • Diversified on concentrated depending on strategy and style	
	Bottom-Up		

The Implementation Process

- Portfolio construction can be viewed as an optimization problem with a goal and a set of constraints. Objectives and constraints may be stated in absolute terms or relative to a benchmark.

	Absolute Framework	**Relative Framework**
Objective Function	Maximize Sharpe Ratio	Maximize Information Ratio
Constraints		
Sector/security weights	Maximum size in portfolio	Maximum deviation from benchmark
Risk	Maximum portfolio volatility specified as multiple (e.g., 0.9) of benchmark volatility	Maximum tracking error (active risk)
Market capitalization	Maximum/minimum set by mandate	Maximum/minimum set by mandate