10.02 Basics Of Portfolio Planning And Construction

Question 1
A client's low willingness to take risk *most likely* results from which of the following?
A. The client has no current income and a short investment time horizon.
B. The client has a long investing time horizon and modest personal net worth.
C. The client is anxious about investing and unsure about the portfolio's returns.

Question 2
In an endowment's investment policy statement, which of the following is the *best* statement of a relative return objective?
A. Achieve an average annual return of 6%
B. Rank in the top third of the endowment peer group
C. Aim not to lose more than INR 20 million on an annual basis

Question 3
Within a client's investment policy statement, the rebalancing policy *most likely* addresses changes in which of the following?
A. The firm's best execution policy
B. The portfolio's strategic asset allocation
C. The process of minimizing transaction costs

Question 4
A new client interview reveals the following:
- Combined annual income exceeds living expenses and is expected to increase each year while employed
- Both the client and spouse are medical doctors, in good health, and expected to work for at least 20 more years
- Over the last 15 years, both client and spouse contributed the maximum allowed into retirement plans; this will continue
- The client has saved 80% of future college costs; the children are age 3 and 5
- Both the client and spouse prefer not to make investment decisions due to a lack of experience and knowledge
- Results from the client's risk questionnaire suggest that the client has a below-average risk attitude

Which of the following *best* describes the client?
A. The client has a low ability to take risk and a low willingness to take risk.
B. The client has a high ability to take risk and a low willingness to take risk.
C. The client has a low ability to take risk and a high willingness to take risk.

Question 5
In the portfolio construction process, which of the following *best* explains the focus on strategic asset allocation? Systematic risk:

A. cannot be allocated to meet risk and return objectives.
B. is attributable to most of the change in long-term value.
C. can be minimized by holding assets with offsetting risks.

Question 6
According to CFA Institute's curriculum, the impact of environment, social, and governance (ESG) factors on portfolio returns is *most often*:
A. positive.
B. negative.
C. inconclusive.

Question 7
In an investment policy statement, the client describes a goal that the portfolio will not underperform the FTSE 100 Index by more than 2% on an annual basis. This investment goal is *best* described as a(n):
A. relative risk objective.
B. absolute risk objective.
C. relative return objective.

Question 8
Which of the following actions is *most* useful for assessing a client's willingness to take risk?
A. Determining the client's net worth
B. Estimating the client's time horizon
C. Evaluating the client's risk questionnaire

Question 9
The Investment Guidelines section of an investment policy statement *most likely* specifies an appropriate:
A. benchmark.
B. use of leverage.
C. level of standard deviation.

Question 10
Which of the following *best* describes why an investment policy statement is prepared?
A. It guarantees that the manager will meet the stated objectives.
B. It is developed after portfolio construction to see the complete picture.
C. It allows the manager to quantify the client's risk and return objectives.

Question 11
A financial adviser meets with a new client to discuss investment strategies. During the meeting, the adviser learns that the client:
- has 25 years of experience investing in bonds and equities;
- has never invested in real estate, private equity, or hedge funds; and
- believes that, when investing, returns are more important than safety.

Given these facts, what would be the *most appropriate* investment recommendation for the client?
A. None, until the client's ability to bear risk is determined
B. A conservative portfolio given the client's inexperience with alternative investments
C. An aggressive portfolio given the client's years of investing knowledge and low risk aversion

Question 12

A manager collects the following data about a client:

Client age	42
Expected retirement age	72
Income	High and exceeds living costs
Dependent family members	• Spouse (age 39) • Twin sons (age 1)
Investment goals	• Retirement • Children's college
Employment (length of years)	Computer programmer (20 years)

The length of the client's time horizon is *most likely* considered to be:
A. long-term.
B. short-term.
C. medium-term.

Question 13

When developing the constraints for an Investment Policy Statement, which of the following would *most appropriately* be considered a "unique circumstance"?
A. An insurance company has more uncertain cash flows than its peers.
B. An individual's retirement plan is heavily invested in employer common stock.
C. A pension fund is legally restricted from holding more than 50% of its assets in equities.

Question 14

Which of the following *best* describes the Investment Guidelines section of the investment policy statement?
A. Defines the portfolio's tactical asset allocation
B. Discusses the use of leverage to meet investment objectives
C. Explains the client's process for hiring and firing external managers

Question 15

An institutional investor has an above average willingness to take risk and a below average ability to bear risk. The institution's investment adviser should *most* reasonably conclude that the institution's risk tolerance is:

A. below average.
B. average.
C. above average.

Question 16
Which of the following *best* describes the process of creating an investment policy statement (IPS)?
A. The client completes a risk questionnaire and the manager writes the IPS.
B. A manager writes a client's investment policy based solely on the client's current portfolio.
C. The manager generates the IPS through a cloud-based program to eliminate human error.

Question 17
In an individual investor's investment policy statement, which of the following is *least likely* characterized as a client objective?
A. Having a 35-year time horizon to retirement
B. Setting a minimum return above a benchmark
C. Identifying the largest acceptable loss per year

Question 18
A client's ability to take risk is *most likely* determined by the client's:
A. net worth.
B. risk attitude.
C. investing experience.

Question 19
With respect to constructing asset classes, pairwise correlations of assets in different asset classes *most likely* are:
A. lower than correlations within an asset class.
B. equal to correlations within an asset class.
C. higher than correlations within an asset class.

Question 20
Which of the following is *most likely* an advantage of using an investment policy statement?
A. Return objectives are expressed gross of fees.
B. The manager can assess the client's willingness to take risk.
C. The client receives assurance that the required rate of return will be met.