

FINA1303 Introduction to Financial Markets

Fall 2015

Mock Examination Questions

There are 50 multiple choice questions. Please choose the best answer for each question.

Question 1

Which of the following items is consistent with the cash flow concept in finance?

- I. The initial investment of a long-term asset that a company pays for its purchase.
 - II. The book value of a long-term asset that a company records in its financial statements.
 - III. The proceeds from the sale of a long-term asset that a company receives.
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- A. III only
 - B. I and II only
 - C. I and III only
 - D. I, II and III

Explanation

I is a cash outflow and III is a cash inflow. The book value of a long-term asset is an accounting concept, which may not be consistent with the cash flow concept in finance. Hence, C is the best answer.

Question 2

Mary borrows a one-year loan of \$50,000 that she has to pay the principal plus interest in year 1. The annual flat rate is quoted as 12%, but actually it is compounded on a monthly basis. What will be the interest payment that Mary has to make in a year's time?

- A. \$6,000.00
- B. \$6,275.44
- C. \$6,341.25
- D. \$6,373.73

Explanation

Principal plus interest in a year's time = $\$50,000 * (1 + 12\%/12)^{12} = \$56,341.25$

Interest payment = $\$56,341.25 - \$50,000 = \$6,341.25$

C is the best answer.

Question 3

Mary won a talent competition and the organizing entity gave her the following choices.

- I. To receive \$100,000 in three year's time.
- II. To receive \$32,000 in each of the coming three years.
- III. To receive \$86,000 now.
- IV. To receive \$30,000, \$32,500 and \$35,000 in years 1, 2 and 3 respectively.

Given that the interest rate is 5%, which of the choices will give Mary the highest present value?

- A. I.
- B. II.
- C. III.
- D. IV.

Explanation

I : $PV = \$100,000 / (1+5\%)^3 = \$86,383$

II : $PV = \$32,000 / (1+5\%) + \$32,000 / (1+5\%)^2 + \$32,000 / (1+5\%)^3 = \$87,144$

III: $PV = \$86,000$

IV: $PV = \$30,000 / (1+5\%) + \$32,500 / (1+5\%)^2 + \$35,000 / (1+5\%)^3 = \$88,284$

The best answer is D.

Question 4

Which of the following is a systematic risk factor that affects the financial market as a whole?

- I. The economic growth rate.
- II. The inflation rate.
- III. The quality of the management team of a company.
- IV. The business nature of a company.

- A. II only
- B. I and II only
- C. III and IV only
- D. I, II, III and IV

Explanation

Both I and II are macroeconomic factors that affect all companies and securities, i.e. the

financial market as a whole. Hence, they are systematic risk factors.

Both III and IV are firm-specific factors that affect a particular company and hence they are unsystematic risk factors.

The best answer is B.

Question 5

Borrowers are usually better informed about their credit standing than lenders. If lenders just charge an average interest rate on borrowers of different risk types, they may end up lending money mainly to high risk borrowers. This type of asymmetric information problem in the financial system is known as:

- A. the moral hazard problem.
- B. the risk sharing problem.
- C. the transaction cost problem.
- D. the adverse selection problem.

Explanation

This type of asymmetric information problem arises before a loan is made. It is known as the adverse selection problem. D is the best answer.

Question 6

A security analyst has gathered the following financial data:

- The yield on the government bonds: 3%
- The return on the stock market index: 8%
- The beta of the stock of company ABC: 0.9

What is the required rate of return on the stock of company ABC based on the capital asset pricing model?

- A. 4.5%
- B. 7.5%
- C. 10.2%
- D. 12.9%

Explanation

required rate of return = $3\% + 0.9 \times (8\% - 3\%) = 7.5\%$

The best answer is B.

Question 7

Which of the following is a primary market activity in the financial system?

- I. A company issues new shares to be bought by a selective group of investors.
 - II. Newly issued bonds are offered to the investors through a public offering.
 - III. The majority shareholder of a company sells his shares to the general public.
-
- A. I only
 - B. I and II only
 - C. I and III only
 - D. II and III only

Explanation

A primary market is a market for trading newly issued securities. Hence, both I and II are primary market activities. III involves trading of already-issued securities and hence it is a secondary market activity. The best answer is B.

Question 8

Which of the following statements about a financial market is correct?

- I. The maturity of a capital market instrument is more than one year.
 - II. An organized exchange has a central market place for buyers and sellers to conduct trades.
 - III. Companies issue new securities in the secondary market.
-
- A. I only
 - B. I and II only
 - C. I and III only
 - D. II and III only

Explanation

Both I and II are correct. Companies issue new securities in the primary market. Hence, III is not correct. The best answer is B.

Question 9

Which of the following is considered as a financial intermediary activity under indirect finance?

- I. An insurance company collects premiums from the insurance policies held by the insured and buy securities in the financial markets.
 - II. A private equity fund solicits capital commitment from investors and buys the ownership interests in start-up companies.
 - III. A hedge fund issues partnership interests to investors and makes high-leveraged investments in the financial markets.
 - IV. A pension fund collects contributions from employees and employers and constructs a portfolio of financial instruments.
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- A. I only.
 - B. I, III and IV only.
 - C. II, III and IV only.
 - D. I, II, III and IV.

Explanation

All of them are financial intermediary activities. The best answer is D.

Question 10

A broker _____ and it usually earns the _____.

- A. trades securities on behalf of the investors; bid-ask spread
- B. provides the market to the investors to trade securities; bid-ask spread
- C. trades securities on behalf of the investors; commission
- D. provides the market to the investors to trade securities; commission

Explanation

A broker trades securities on behalf of the investors and it usually earns the commission. The best answer is C.

Question 11

When a company records its transactions in monetary terms in the accounting system, money serves the function as:

- A. a unit of value.
- B. a medium of exchange.
- C. a store of wealth.
- D. a source of finance.

Explanation

Under the specified situation, money serves as a unit of value. The best answer is A.

Question 12

When an investor tries to determine the liquidity of a financial market, he can make use of a measure known as the resiliency. Which of the following statements best describes the situation that a financial market is resilient?

- A. There are minimal price effects associated with block trades in the financial market.
- B. There are a large number of buyers and sellers in the financial market.
- C. The bid-ask spreads provided by the dealers are narrow in the financial market.
- D. Securities can be traded very quickly in the financial market.

Explanation

When a financial market has minimal price effects associated with block trades, it is said to be resilient. The best answer is A.

Question 13

Which of the following is a statutory regulator in Hong Kong?

- I. The Securities and Futures Commission
 - II. The Hong Kong Exchanges and Clearing Limited
 - III. The Office of the Commissioner of Insurance.
 - IV. The Mandatory Provident Fund Schemes Authority.
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- A. I and II only.
 - B. I, III and IV only.
 - C. II, III and IV only.
 - D. I, II, III and IV.

Explanation

The Hong Kong Exchanges and Clearing Limited is a self-regulatory body and the others are statutory regulators. The best answer is B.

Question 14

Which of the following regulators is responsible for monitoring the fund management sector in Hong Kong?

- A. The Hong Kong Monetary Authority.
- B. The Securities and Futures Commission.
- C. The Mandatory Provident Fund Schemes Authority.
- D. The Office of the Commissioner of Insurance.

Explanation

The Hong Kong Monetary Authority is responsible for monitoring the banking sector. The Mandatory Provident Fund Schemes Authority is responsible for monitoring the mandatory provident fund sector. The Office of the Commissioner of Insurance is responsible for monitoring the insurance sector. The Securities and Futures Commission is responsible for monitoring the securities and futures sector and the fund management sector. The best answer is B.

Question 15

Which of the following is usually considered as a regulated activity under the supervision of the Securities and Futures Commission according to the Securities and Futures Ordinance?

- I. Dealing in futures contracts.
 - II. Advising on corporate finance.
 - III. Providing asset management services.
 - IV. Providing bank loans.
-
- A. I and II only.
 - B. II and III only.
 - C. I, II and III only
 - D. I, II, III and IV only.

Explanation

I, II and III are regulated activities while IV is not. The best answer is C.

Question 16

When a central bank carries out an expansionary monetary policy by buying government securities in the open market, the money supply _____ and the interest rates _____.

- A. increases; rise
- B. increases; fall
- C. decreases; rise

D. decreases; fall

Explanation

When a central bank carries out an expansionary monetary policy by buying more government securities in the open market, the money supply increases and the interest rates fall. The best answer is B.

Question 17

Which of the following is a characteristic of the money market?

- I. Foreign currencies are traded in the money market.
 - II. The maturity of a money market instrument is one year or less.
 - III. Money market instruments are actively traded in the secondary market.
 - IV. Money market instruments involve relative low default risk.
-
- A. I and II only
 - B. III and IV only
 - C. II, III and IV only
 - D. I, II, III and IV

Explanation

Foreign currencies are traded in the foreign exchange market while mainly short-term debt securities are traded in the money market. Hence, I is incorrect. II, III and IV are all characteristics of the money market. The best answer is C.

Question 18

An investor is considering the purchase of a 182-day euro-denominated money market instrument with a face value of €1,000,000. Its price is quoted at 99 and the day count convention is ACT/360. Given that there are 365 days in the year, what is the annualized discount rate for this money market instrument?

- A. 1.00%
- B. 1.98%
- C. 2.01%
- D. 2.04%

Explanation

discounted price = €1,000,000*99% = €990,000

discount rate = $(€1,000,000 - €990,000) / €1,000,000 * 360/182 = 1.98\%$

The best answer is B.

Question 19

A large commercial bank, acting as a dealer, quotes HIBID and HIBOR for a 3-month interbank loan as 0.34% and 0.39% respectively. The day count convention is ACT/365 and the number of calendar days in three months is 90 days. If another commercial bank wants to borrow \$20 million from this dealer bank, which of the following statements is correct with respect to this transaction?

- I. The interest payment is \$16,767.12.
 - II. The interest payment is \$19,232.88.
 - III. The interbank loan is traded on an interest to maturity basis.
 - IV. The interbank loan is traded on a discount basis.
-
- A. I and III only
 - B. I and IV only
 - C. II and III only
 - D. II and IV only

Explanation

Interbank loans are traded on an interest to maturity basis. Hence, IV is not correct.

The interest rate for the interbank loan is HIBOR (0.39%).

Interest payment = $\$20,000,000 * 0.39\% * 90/365 = \$19,232.88$.

Hence, I is not correct.

The best answer is C.

Question 20

The Hong Kong Monetary Authority provides a credit facility, known as the discount window, to commercial banks. Usually, this credit facility is arranged through:

- A. an interbank loan.
- B. a repurchase agreement.
- C. a commercial paper.
- D. a bill of exchange.

Explanation

The discount window is usually arranged through a repurchase agreement. The best answer is

B.

Question 21

An investor bought a 10-year floating rate note at a coupon rate equal to the three-month HIBOR plus 0.25%, paid in arrears. The three-month HIBOR three months ago was 1% while the current three-month HIBOR is 1.5%. What is the applicable coupon rate for determining the coupon payment for the current period?

- A. 1.00%
- B. 1.25%
- C. 1.50%
- D. 1.75%

Explanation

applicable coupon rate = 1% + 0.25% = 1.25%

B is the best answer.

Question 22

Which of the following statements is correct with respect to the common stocks and bonds issued by a company?

- I. Both interest expenses and dividends paid by a company are tax deductible.
 - II. The bondholders are a company's creditors while common stockholders are its owners.
 - III. The bondholders of a company have higher priority than its stockholders over the proceeds from sale of assets upon its liquidation.
 - IV. A company has contractual obligations to provide regular cash flows to both its bondholders and stockholders.
- A. I and III only
 - B. I and IV only
 - C. II and III only
 - D. II and IV only

Explanation

Interest expenses are tax-deductible while dividends are not. Hence, I is not correct. The company has contractual obligations to provide regular cash flows to the bondholders, but the dividends to the stockholders are at the discretion of the company. Hence, IV is not correct. The best answer is C.

Question 23

Which of the following factors is likely to lead to a higher yield for a bond?

- I. The credit standing of the bond issuer is deteriorating.
 - II. The bond includes an embedded option granted to the bondholders.
 - III. The maturity of the bond increases.
-
- A. I and II only
 - B. I and III only
 - C. II and III only
 - D. I, II and III

Explanation

When a bond includes an embedded option granted to the bondholders, the bondholders are willing to pay a higher bond price resulting in a lower yield. The best answer is B.

Question 24

Which of the following statements is **NOT** correct with respect to a bond?

- I. With respect to the conversion right (embedded option) attached to a convertible bond, the bondholder effectively buys a stock call option from the bond issuer.
 - II. The holder of a bullet bond will receive both the coupon payment and part of the principal repayment in every interest payment period until the maturity date of the bond.
 - III. The coupon rate of an already-issued fixed rate bond is determined by the prevailing demand and supply conditions in the bond market.
 - IV. If a provision in the bond agreement states that the bond issuer must maintain a current ratio of 1.5 or above, it is a negative covenant.
-
- A. I, II and III only.
 - B. I, II and IV only.
 - C. II, III and IV only.
 - D. I, II, III and IV.

Explanation

I, II and III are incorrect while IV is correct. The best answer is C.

Question 25

John bought a 10-year \$50,000 par 5% bond two years ago. The annual coupon payment is made on 31 December every year. The day count convention for this bond is ACT/360. The actual number of calendar days in this year is 365. As an emergency arises, John has to sell the bond before the next coupon payment date at a yield of 6%. The actual number of calendar days from the last coupon date up to the trading date is 95 days. What is the accrued interest that John should receive from the sale of the bond?

- A. \$650.68
- B. \$659.72
- C. \$780.82
- D. \$791.67

Explanation

accrued interest = $\$50,000 \times 5\% \times 95/360 = \659.72

The best answer is B.

Question 26

A supranational organization issues two bonds as follows:

- Bond 1: a renminbi-denominated bond issued and traded in Hong Kong
- Bond 2: a renminbi-denominated bond issued and traded in Mainland China.

Bond 1 is a _____ and bond 2 is a _____.

- A. foreign bond; domestic bond
- B. Eurobond; domestic bond
- C. Eurobond; foreign bond
- D. foreign bond; foreign bond

Explanation

Bond 1 is a Eurobond and bond 2 is a foreign bond. The best answer is C.

Question 27

Which of the following statements is correct with respect to derivatives?

- I. The buyer of a futures contract has the right, but not the obligation, to decide whether to exercise it while the seller of the futures contract has to fulfill the obligations once it is exercised.

- II. The buyer of an option contract has the right, but not the obligation, to decide whether to exercise it while the seller of the option contract has to fulfill the obligations once it is exercised.
 - III. The buyer of a futures contract has to pay a premium to the seller at the inception of the contract.
 - IV. The buyer of an option contract has to pay a premium to the seller at the inception of the contract.
-
- A. I and III only
 - B. I and IV only
 - C. II and III only
 - D. II and IV only

Explanation

Both the buyer and seller of a futures contract have the obligations to execute the contract as specified upon maturity. Hence, I is not correct. No money changes hand between the buyer and seller of a futures contract at the inception of the contract. Hence, III is not correct. The best answer is D.

Question 28

An investor sold a Hang Seng Index (HSI) futures contract at the market close of 22,000 through a brokerage house yesterday. The dollar multiplier is \$50 per index point. The initial margin and maintenance margin have been and are still set at \$72,000 and \$57,600 respectively. Today, the settlement price for the HSI futures contract is 22,300. Which of the following statements is correct?

- A. The investor has earned a profit of \$15,000 from his position in the HSI futures contract.
- B. The brokerage house will issue a margin call to the client.
- C. The investor holds a long position in the HSI futures contract.
- D. After being adjusted for today's profit and loss, the margin account balance of the client is \$58,000.

Explanation

The investor has incurred a loss of $(22,000 - 22,300) * \$50 = -\$15,000$ (loss). Hence, A is not correct. When an investor sells the HSI contracts, he holds a short position. Hence, C is not correct. The adjusted margin account balance is $\$72,000 - \$15,000 = \$57,000$. Hence, D is not correct. As the adjusted margin account balance falls short of the maintenance margin level, the brokerage issue will issue a margin call to the client. The best answer is B.

Question 29

The strategy that an investor uses derivative products to reduce or eliminate an existing risk exposure faced by him is known as:

- A. hedging.
- B. speculation.
- C. investment.
- D. arbitrage.

Explanation

This is the definition of hedging. The best answer is A.

Question 30

Which of the following statements is correct regarding the margining system in the exchange-traded derivative market?

- I. The initial margin and the maintenance margin of a derivative position are set by the Exchange.
 - II. When the specified maintenance margin of a client's derivative position falls below his adjusted margin balance, the broker will issue a margin call to the client to ask for additional margin.
 - III. The marking to market procedure refers to the adjustment of the profit and loss of a derivative position to the margin balance on a daily basis.
 - IV. When a client fails to post the additional margin upon a margin call, the broker has the right to force-liquidate his derivative position.
- A. II and IV only.
 - B. I, II and III only.
 - C. I, III and IV only.
 - D. I, II, III and IV.

Explanation

When the adjusted margin balance of a client's derivative position falls below the specified maintenance margin, the broker will issue a margin call to the client to ask for additional margin. Hence, II is not correct. The best answer is C.

Question 31

Which of the following is a commodity derivative?

- I. A gold forward contract.
- II. A crude oil futures contract
- III. A Hang Seng Index option contract.
- IV. An interest rate swap contract.

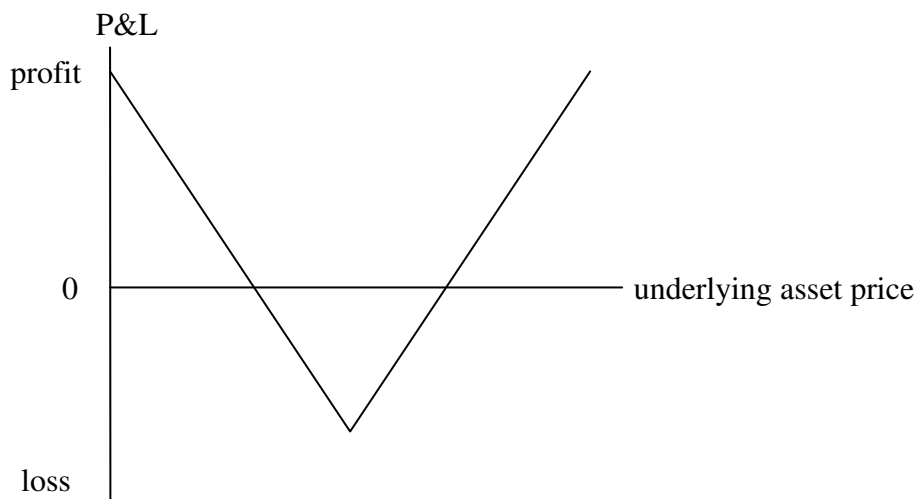
- A. I and II only.
- B. I, II and III only.
- C. I, III and IV only.
- D. II, III and IV only.

Explanation

I and II are commodity derivatives while III and IV are financial derivatives. The best answer is A.

Question 32

An investor simultaneously buys a call option and a put option with the same underlying asset, exercise price and maturity date. Based on the profit and loss diagram of this strategy below, which of the following statements is correct about the investor's expectation of the underlying asset price?



- A. The investor bets on the low volatility of the underlying asset price.
- B. The investor bets on the high volatility of the underlying asset price.
- C. The investor bets on the upward price movement of the underlying asset.

D. The investor bets on the downward price movement of the underlying asset.

Explanation

This strategy is known as a long straddle which bets on the high volatility of the underlying asset price. In other words, the investor can make profits when there is a sharp change (upward or downward) in the underlying asset price. The best answer is B.

Question 33

Which of the following is a characteristic of preferred stocks?

- I. Preferred stockholders have priority over creditors and common stockholders in receiving the proceeds from sale of assets upon liquidation.
 - II. Preferred stock issuers have mandatory obligations to provide dividends to their shareholders.
 - III. Preferred stockholders of a company receive fixed dividends even through the company performs very well.
 - IV. Preferred stockholders can generally vote in the annual general meetings of the issuing companies.
- A. None of the above
 - B. III only
 - C. I and II only
 - D. I, III and IV only

Explanation

Preferred stockholders have priority over common stockholders, but not creditors, upon liquidation. Hence, I is not correct. The dividend announcements to preferred stockholders are at the discretion of the board of directors of the issuing companies. Hence, II is not correct. In general, preferred stockholders cannot vote in the annual general meetings. Hence IV is not correct. The best answer is B.

Question 34

A company does not have any significant assets or operations, but it maintains the listing status in Hong Kong. This company is usually known as:

- A. a small-cap company.
- B. a penny company.
- C. a B share company.

D. a shell company.

Explanation

It is the definition of a shell company. The best answer is D.

Question 35

If the cum-dividend stock price and dividend per share of a company are \$12.5 and \$1.5 respectively, the net assets of the company will _____ because of the dividend payment and the ex-dividend price is expected to be _____ on the ex-dividend date.

- A. increase; \$11
- B. decrease; \$11
- C. increase; \$14
- D. decrease; \$14

Explanation

As the company pays dividends in cash, its net assets will decrease. The ex-dividend price is $\$11 = \$12.5 - \$1.5$. B is the best answer.

Question 36

A company announces a five-for-two bonus issue. The cum-bonus stock price is \$25. What is the ex-bonus price?

- A. \$3.57
- B. \$7.14
- C. \$12.36
- D. \$17.86

Explanation

$\text{ex-bonus price} = (\$25 \times 2) / (5 + 2) = \7.14

The best answer is B.

Question 37

Fatima wants to buy 10,000 shares of company XYZ at a price of \$80 per share. She has only \$300,000 and decides to borrow the rest from a securities margin financier. Calculate the rate of return on her margined position if the stock price rises to \$90.

- A. 11.11%

- B. 12.50%
- C. 20.00%
- D. 33.33%

Explanation

$$\text{profit} = (\$90 - \$80) \times 10,000 = \$100,000$$

$$\text{rate of return} = \$100,000 / \$300,000 = 33.33\%$$

The best answer is D.

Question 38

An investor just received an annual dividend of \$2.5 from a company. He expects that its stock dividends will grow at a constant rate of 4% indefinitely. The required rate of return on the stock is 15%. What is the fair value of the stock based on the constant growth model?

- A. \$13.16
- B. \$13.68
- C. \$22.72
- D. \$23.64

Explanation

$$\text{Fair value of stock} = \$2.5 \times (1 + 4\%) / (15\% - 4\%) = \$23.64$$

The best answer is D.

Question 39

When the exchange rate of GBP/HKD rises, it means that GBP _____ against HKD. GBP is said to be the _____ currency.

- A. appreciates; base
- B. appreciates; quoted
- C. depreciates; base
- D. depreciates; quoted

Explanation

When the exchange rate of GBP/HKD rises, it means that GBP appreciates against HKD. GBP is said to be the base currency. The best answer is A.

Question 40

When the currency of country X depreciates against that of country Y, the imports from

country X appear to be _____ to the residents of country Y and the imports from country Y appears to be _____ to the residents of country X.

- A. cheaper; cheaper
- B. cheaper; more expensive
- C. more expensive; cheaper
- D. more expensive; more expensive

Explanation

When the currency of country X depreciates against that of country Y, the imports from country X appear to be cheaper to the residents of country Y and the imports from country Y appears to be more expensive to the residents of country X. The best answer is B.

Question 41

If USD/JPY has gone up from 93.44 to 98.38, which of the following statements best describes the change in the exchange rate?

- A. USD depreciates against JPY by 5.02%.
- B. USD appreciates against JPY by 5.02%.
- C. USD depreciates against JPY by 5.29%.
- D. USD appreciates against JPY by 5.29%.

Explanation

USD appreciates against JPY by $(98.38-93.44)/93.44 = 5.29\%$. The best answer is D.

Question 42

Which of the following is a current account transaction in the balance of payments of a country?

- I. A domestic company of that country buys the raw materials from a foreign supplier.
 - II. A national of that country incurs the travelling expenses when he stays abroad.
 - III. A domestic investor of that country receives the dividends from a foreign stock.
 - IV. A domestic investor of that country buys a bond issued by an overseas company in a foreign market.
-
- A. I and II only.
 - B. III and IV only.
 - C. I, II and III only.

D. I, II and IV only.

Explanation

I, II and III are current account transactions while IV is a capital account transaction. The best answer is C.

Question 43

Which of the following items are included in the monetary base which is fully backed up by US dollar reserves under the Hong Kong Linked Exchange Rate System?

- I. The aggregate balance of the clearing accounts maintained by banks with the Hong Kong Monetary Authority.
 - II. Currency in circulation
 - III. Bank deposits.
 - IV. Exchange Fund Bills and Notes
-
- A. I, II and III only.
 - B. I, II and IV only.
 - C. I, III and IV only.
 - D. II, III and IV only.

Explanation

Bank deposits are not included in the monetary base. The best answer is B.

Question 44

If an investor buys a 3-month USD/CHF forward contract at 0.9463 with USD 1,000,000 and he liquidates his position at a forward rate of 0.9563, what is his profit and loss on this trade?

- A. A profit of CHF 10,000
- B. A loss of CHF 10,000
- C. A profit of USD 10,000
- D. A loss of USD 10,000

Explanation

$P\&L = (0.9563 - 0.9463) \times \text{USD } 1,000,000 = \text{CHF } 10,000$ (profit)

The best answer is A.

Question 45

Which of the following represents the bid-ask spread in the fee structure of a managed fund?

- A. The switching fee.
- B. The redemption fee.
- C. The annual management fee.
- D. The front-end fee.

Explanation

The front-end fee represents the bid-ask spread. The best answer is D.

Question 46

The _____ determines a managed fund's long-term mix of asset classes which are groups of securities with similar investment characteristics.

- A. strategic asset allocation
- B. investment objective
- C. investment constraint
- D. benchmark index

Explanation

The strategic asset allocation determines a managed fund's long-term mix of asset classes which are groups of securities with similar investment characteristics. The best answer is A.

Question 47

The market values of the assets and liabilities of a managed fund are \$100 million and \$40 million respectively. The fund has 10 million shares outstanding. What is the net asset value per share of the fund?

- A. \$4
- B. \$6
- C. \$10
- D. cannot be determined with the information provided

Explanation

NAV per share = $(\$100 - \$40) / 10 = \$6$

The best answer is B.

Question 48

Which of the following is an advantage of fund investment?

- I. It involves a small initial investment with a variety of choices.
 - II. It gets access to professional management services.
 - III. It gets access to worldwide investment opportunities.
 - IV. It involves minimal transaction costs.
-
- A. I and IV only
 - B. I, II and III only
 - C. II, III and IV only
 - D. I, II, III and IV

Explanation

The transaction costs associated with fund investment are not minimal. Hence, IV is not correct. The best answer is B.

Question 49

Which of the following statements is correct with respect to a unit trust and a mutual fund?

- I. Both a unit trust and a mutual fund are formed as a corporation.
 - II. The trustee of a unit trust is legally liable to the investors of the unit trust.
 - III. The trustee of a unit trust holds the assets of the unit trust on behalf of the investors.
 - IV. The beneficiaries of a mutual fund are the shareholders of the mutual fund.
-
- A. I, II and III only
 - B. I, II and IV only
 - C. I, III and IV only
 - D. II, III and IV only

Explanation

A unit trust is formed as a trust while a mutual fund is formed as a corporation. Hence, I is not correct. The best answer is D.

Question 50

The _____ determines a managed fund's long-term mix of asset classes which are groups of securities with similar investment characteristics.

- A. strategic asset allocation

- B. investment objective
- C. investment constraint
- D. benchmark index

Explanation

The strategic asset allocation determines a managed fund's long-term mix of asset classes which are groups of securities with similar investment characteristics. The best answer is A.

- The End -