Learning Module 3: Portfolio Management: An Overview

Q.123 Which of the following statements is *least likely* accurate regarding a defined contribution plan?

A. Future benefits to the account are guaranteed.

B. Future benefits fluctuate based on investment earnings.

C. Individual accounts are set up for participants and benefits are based on the amounts credited to these accounts.

The correct answer is **A.**

In a defined contribution plan, only contributions to the account are guaranteed, not the future benefits. A defined contribution plan is a retirement plan in the employee's name usually funded by both the employee and the employer. With DC plans, individuals will invest part of their wages while working, expecting to draw on the accumulated funds to provide income during retirement. The employee accepts the investment and inflation risk and is responsible for ensuring that there are enough assets in the plan to meet their needs upon retirement.

B is incorrect. The fluctuation of benefits is a characteristic feature of these plans, as the retirement income depends on the performance of the investments chosen by the account holder. Therefore, while this statement is accurate, it does not fit the criteria of being the least accurate statement about defined contribution plans.

C is incorrect. This option accurately describes a feature of defined contribution plans, where individual accounts are set up for participants, and benefits are based on the amounts credited to these accounts, including both contributions and investment earnings.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (d): Describe defined contribution and defined benefit pension plans.

Q.124 Which of the following is the *best* definition of mutual funds?

A. Funds from many individual investors that are aggregated for the purposes of investment.

B. A type of professionally managed investment fund that pools money from many investors to purchase securities.

C. A limited partnership of investors that uses high-risk methods, such as investing with borrowed money, in hopes to realize large capital gains.

The correct answer is **B.**

A mutual fund is a type of professionally managed investment fund that pools money from many investors to purchase securities. Each investor in the fund has a pro-rata claim on the income and value of the fund.
A is incorrect. While this option highlights the pooling of funds from many individual investors for investment purposes, it lacks the specificity of mentioning the professional management aspect and the goal of purchasing securities. Mutual funds are not just any pooled investment; they are specifically structured to be professionally managed and to invest in a diversified portfolio of securities such as stocks, bonds, and other financial instruments. The definition provided in option A is too broad and could apply to various types of pooled investments, not distinctly identifying the unique characteristics of mutual funds.

C is incorrect. Hedge funds are indeed pooled investments, but they are distinct from mutual funds in several key aspects. Hedge funds often employ high-risk investment strategies, including the use of leverage (borrowed money), derivatives, and short-selling, with the aim of generating high returns. They are typically available only to accredited or qualified investors due to their riskier nature and higher minimum investment requirements. Mutual funds, on the other hand, are accessible to a broader range of investors and generally focus on a diversified portfolio to manage risk, rather than seeking high returns through high-risk methods.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.760 Which of the following statements is *most likely* accurate?

A. Insurance companies need to invest the premiums received for the policies written to allow them to pay bonuses to their investors and meet operational expenses.

B. Investment companies that manage mutual funds are collective financial institutions. Investors pool their capital to have it invested by professional managers with high liquidity needs to meet redemption requirements.

C. Banks need to invest their excess reserves (i.e., when deposits have not been used to make loans) more in equities and other relatively less liquid assets to earn a return on its services that exceeds the rate of interest it pays on its deposits.

The correct answer is **B.**

Investment companies that manage mutual funds are collective financial institutions. Investors pool their capital to have it invested by professional managers with high liquidity needs to meet redemption requirements.

A is incorrect. As insurance companies' main investment purpose is to meet claims rather than paying bonuses

C is incorrect. Banks need to be conservative while making investments of excess reserves.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.762 Which of the following is *least likely* a characteristic of open-ended mutual funds?

A. An open-end structure makes it easy to grow in size but creates pressure on the portfolio manager to manage the cash inflows and outflows.

B. In open-end funds, new shares are created and sold at a premium or a discount to net assets values depending on the demand for the shares.

C. Open-end funds accept new investment money and issue additional shares to existing or new investors. Therefore, the number of outstanding shares changes after every new investment.

The correct answer is **B.**

In open-end funds, new shares are issued at the net asset value of the fund at the time of investment. An open-end fund is a collective investment scheme that can issue and redeem shares at any time. An investor will generally purchase shares in the fund directly from the fund itself rather than from the existing shareholders.

It contrasts with a closed-end fund, which typically issues all the shares it will issue at the outset, with such shares usually being tradable between investors thereafter. Unlike open-end funds in which new shares are created and sold at the current net asset value per share, closed-end funds can sell for a premium or discount to net asset value depending on the demand for the shares.
A is incorrect. The open-end structure allows for the fund to grow in size as new investments are made, with the fund issuing new shares to accommodate this growth. However, this can indeed create challenges for the portfolio manager, who must manage cash inflows and outflows effectively to maintain the fund's investment strategy and performance. Managing these cash flows is a critical aspect of operating an open-ended fund, as significant inflows or outflows can impact the fund's asset allocation and potentially its returns.

C is incorrect. This option also accurately describes a feature of open-ended mutual funds. Open-end funds are designed to accept new investment money at any time, issuing additional shares to accommodate new or existing investors. This flexibility is a key advantage of open-ended funds, allowing investors to enter or exit the fund according to their investment needs. The number of outstanding shares in an open-ended fund is not fixed and changes with each new investment or redemption, reflecting the fund's ability to adapt to investor demand while maintaining its investment objectives.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.763 Which of the following best describes all of the major types of mutual funds differentiated by the asset type they invest in?

A. Money market funds and stock mutual funds.

B. Money market funds, stock mutual funds, and hybrid or balanced funds.

C. Money market funds, stock mutual funds, bond mutual funds and hybrid or balanced funds.

The correct answer is **C.**

There are four different types of mutual funds classified based on the type of assets they invest in: money market funds, stock mutual funds, bond mutual funds, and hybrid or balanced funds.
A is incorrect. This option only mentions money market funds and stock mutual funds, omitting bond mutual funds and hybrid or balanced funds. By excluding these two types, it fails to capture the full spectrum of mutual funds differentiated by asset type. Bond mutual funds play a crucial role in providing income and reducing portfolio volatility, while hybrid or balanced funds offer a diversified investment strategy that can adapt to changing market conditions. Therefore, this option does not accurately describe all the major types of mutual funds.

B is incorrect. Although this option includes money market funds, stock mutual funds, and hybrid or balanced funds, it neglects to mention bond mutual funds. Bond mutual funds are a significant category that invests in various debt securities, offering investors a source of regular income and typically lower risk compared to stock mutual funds. The absence of bond mutual funds in this option means it does not fully represent the range of mutual funds classified by the asset types they invest in. Bond mutual funds are essential for investors seeking to diversify their portfolios, reduce risk, and secure a steady income stream, making their omission a critical oversight.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.764 Which of the following is considered as the major difference between a bond mutual fund and a money market fund?

A. The taxability of these two funds.

B. The maturity of the underlying assets.

C. The nature of the assets they invest in.

The correct answer is **B.**

In a money market fund, the maturity is as short as overnight and rarely longer than 90 days. However, a bond mutual fund holds bonds with maturities as short as one year and as long as 30 years.

A is incorrect. While the taxability of bond mutual funds and money market funds can differ, especially if a money market fund qualifies as a tax-exempt fund by investing in municipal securities, taxability is not the major distinguishing factor between these two types of funds. Both types of funds can have variations in tax implications based on the specific assets they hold. Therefore, the primary difference is not in their taxability but in the maturity of the underlying assets they invest in.

C is incorrect. Although bond mutual funds and money market funds invest in different types of assets, with bond mutual funds typically investing in a broader range of debt securities and money market funds focusing on short-term, high-quality instruments, the nature of the assets is not the most significant difference. The key distinction lies in the maturity of these assets rather than their nature. Both types of funds invest in debt instruments, but the duration and risk profiles of these instruments vary significantly, which is a critical factor for investors to consider when choosing between these funds.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.765 Which of the following is *least likely* accurate in the context of actively managed stock mutual funds?

A. Tax implications are lower in actively managed funds than in index funds.

B. Higher fees are charged for actively managed funds (reflecting its goal to outperform the index).

C. More research is conducted in actively managed funds to select the best securities, and they are traded more often than index funds.

The correct answer is **A.**

Mutual funds are required to distribute all income and capital gains realized in the portfolio, so the actively managed fund tends to have more opportunity to realize capital gains. This results in higher taxes relative to an index fund, which uses a buy-and-hold strategy. In addition, management fees for actively managed funds are higher to reflect their goal of outperforming an index. The higher fees are required to pay for the research conducted to actively select securities.

B is incorrect. The statement that higher fees are charged for actively managed funds, reflecting its goal to outperform the index, is accurate. Actively managed funds incur additional costs due to the intensive research and frequent trading activities undertaken by fund managers in an attempt to achieve superior returns. These costs are passed on to investors in the form of higher management fees or expense ratios. The rationale behind the higher fees is to compensate for the expertise and efforts of the fund managers and their research teams who analyze market trends, economic conditions, and individual securities to make informed investment decisions.

C is incorrect. The statement that more research is conducted in actively managed funds to select the best securities, and they are traded more often than index funds, accurately describes the nature of actively managed funds. The primary objective of these funds is to outperform a benchmark index, which necessitates a proactive investment strategy. This strategy involves conducting extensive research to identify securities that are expected to provide superior returns. Thus, this option accurately reflects the operational differences between actively managed funds and index funds.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.766 In which of the following investment products are creation units *most likely* issued?

A. Open-end mutual funds.

B. Closed-end mutual funds.

C. Exchange-traded funds (ETF).

The correct answer is **C.**

ETFs use a mechanism involving creation units, which are large blocks of ETF shares (typically between 50,000 and 100,000 shares). Authorized participants, usually large institutional investors, deposit a specified portfolio of securities and other assets with the ETF sponsor, and in return, they receive creation units of the ETF. This process facilitates the ETF's liquidity and price tracking of the underlying assets or index.

A is incorrect. In open-end mutual funds, shares are directly issued to investors by the fund itself and are not traded between investors on an exchange. The number of shares is not fixed and can vary as investors buy into or redeem shares from the fund. Therefore, the concept of creation units, which are specific large blocks of shares, is not applicable.

B is incorrect. Closed-end mutual funds do not utilize creation units. These funds issue a fixed number of shares through an initial public offering (IPO), after which these shares are traded between investors on an exchange. Unlike ETFs, the closed-end fund does not continuously issue new shares or redeem them. The number of shares remains constant, except in certain cases like secondary offerings, but this does not involve the creation unit process.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.768 Which of the following is *least likely* a similarity between buyout funds and venture capital funds?

A. They both seek to only acquire a minority stake in the firms they invest in.

B. They both take control of the board of the companies in which they invest.

C. They both make investments with finite investment horizons (usually 3 to 5 years).

The correct answer is **A.**

Similar to buyout funds, venture capital funds typically have finite investment horizons (usually 3 to 5 years). Also, they both take control of the board of the companies in which they invest. However, buyout funds almost always buy 100% of a company, whereas venture capital firms only acquire a minority stake - less than 50%. Therefore, option A is the least likely answer.
B is incorrect. It states that both types of funds take control of the board of the companies in which they invest. While this is generally true for buyout funds due to their majority or full ownership, venture capital funds, despite often holding a minority stake, may still seek board representation or control as part of their investment terms. However, the extent of control can vary significantly between the two types of funds, with buyout funds typically having a more dominant influence due to their larger equity stakes.

C is incorrect. It correctly identifies a similarity between buyout funds and venture capital funds. Both types of investment funds operate with finite investment horizons, usually ranging from 3 to 5 years, after which they seek to exit their investments through various means such as an initial public offering (IPO), sale to another company, or sale to another investor. This finite investment horizon is a characteristic of private equity investing, which includes both buyout and venture capital strategies, as investors aim to realize a return on their investments within a specific timeframe.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.1265 The government of Canada and the government of Turkey want to establish a fund that will invest in small-medium enterprises in Turkey. Which of the following funds will they choose?

A. Mutual Fund.

B. Sovereign Fund.

C. Endowment Fund.

The correct answer is **B.**

Sovereign funds are established by governments for investment purposes. They are state-owned investment funds or entities that invest in financial or real assets and have varying investment horizons and objectives based on funding the government's goals. Mutual funds and endowment funds are not established by countries.
A is incorrect. Mutual funds are investment vehicles that pool money from many investors to purchase a diversified portfolio of stocks, bonds, or other securities. They are typically managed by private entities and cater to individual investors rather than serving as a tool for governmental strategic investments. While mutual funds can invest in a wide range of assets, including those in emerging markets or specific sectors, they do not have the sovereign backing or the strategic focus on national economic development that a sovereign wealth fund would have in the context of the governments of Canada and Turkey looking to invest in SMEs in Turkey.

C is incorrect. They are not established by governments for national investment purposes. The goal of investing in SMEs in Turkey to foster economic development aligns more closely with the objectives and capabilities of a sovereign wealth fund.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.1266 Which of the following *most likely* has the highest risk tolerance and lowest liquidity needs?

A. Banks.

B. Endowment funds.

C. Insurance companies.

The correct answer is **B.**

Endowment funds have a higher risk tolerance and lower liquidity needs than insurance companies and banks.
Usually, endowment funds have long-term horizons with relatively low liquidity needs. For this reason, funds can tolerate short- and intermediate-term volatility provided that long-term returns meet or exceed investment objectives. Consequently, endowment funds may take advantage of less liquid investments, such as private equity, hedge funds, and other partnerships vehicles, which typically offer higher risk-adjusted return potential as compensation for forfeiture of liquidity.

A is incorrect. Banks operate in a highly regulated environment and are required to maintain a certain level of liquidity to meet the withdrawal demands of their depositors. Additionally, banks face strict capital requirements that limit their ability to engage in high-risk investments. While banks do invest in a variety of assets to generate returns, their risk tolerance is significantly lower than that of endowment funds, primarily due to the need to ensure the safety and availability of depositor funds.

C is incorrect. Insurance companies, similar to banks, are subject to regulatory requirements that influence their investment strategies. They need to maintain sufficient liquidity to pay out claims, which can arise unpredictably. This requirement constrains their ability to lock funds into long-term, illiquid investments. While insurance companies do invest in a diversified portfolio to manage risk and generate returns, their investment decisions are heavily influenced by the need to match assets with liabilities, both in terms of duration and liquidity. Consequently, their risk tolerance is lower than that of endowment funds, which do not face the same immediate financial obligations.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.1267 Liquidity needs of defined benefit plans are *most likely*:

A. Low.

B. High.

C. Uncertain.

The correct answer is **A.**

Defined benefit plans (DB plans) are company-sponsored plans that offer employees a predefined benefit on retirement. They have a high-risk tolerance, a long horizon, and low liquidity needs.
B is incorrect. Suggesting that liquidity needs are high contradicts the fundamental characteristics of defined benefit plans. High liquidity needs are more characteristic of defined contribution plans, where the participants may choose to change their investment allocations or withdraw funds based on changing market conditions or personal circumstances.

C is incorrect. While it's true that market conditions and changes in workforce demographics (like unexpected early retirements or layoffs) can introduce some level of uncertainty in liquidity needs, defined benefit plans are designed with mechanisms to mitigate such uncertainties. Actuarial calculations and conservative funding strategies are employed to ensure that the plans can meet their obligations without requiring high levels of liquidity on short notice. Therefore, describing the liquidity needs as uncertain overlooks the structured and predictable nature of these plans' obligations and funding strategies.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (d): Describe defined contribution and defined benefit pension plans.

Q.1269 Which of the following parties *most likely* assumes the investment risk of a defined benefit plan?

A. The employer.

B. The employees.

C. The investment managers.

The correct answer is **A.**

Defined benefit plans are plans in which the company promises to pay a certain annual amount (defined benefit) to the employee after retirement. Since the future value or benefits of the plan are promised, the investment risk of a defined benefit plan is assumed by the employer.
B is incorrect. Employees under a defined benefit plan do not bear the investment risk. The promise of a specific benefit upon retirement is made by the employer, who is also responsible for managing the plan's assets to ensure that this promise can be fulfilled. Employees' benefits are determined by the plan's formula and are not directly affected by the plan's investment performance. This arrangement shields employees from the risk associated with fluctuating market conditions and investment returns.

C is incorrect. While investment managers are responsible for making investment decisions on behalf of the defined benefit plan, they do not assume the investment risk. Their role is to manage the plan's assets according to the investment policy and objectives set forth by the employer or the plan's trustees. If the investments underperform, the responsibility to cover the shortfall and ensure that promised benefits can be paid rests with the employer, not the investment managers. Investment managers may be evaluated based on their performance and could be replaced for poor performance, but the ultimate financial risk remains with the employer.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (d): Describe defined contribution and defined benefit pension plans.

Q.1270 Which of the following portfolio management steps *most likely* requires a detailed investment policy statement?

A. Planning step.

B. Feedback step.

C. Execution step.

The correct answer is **A.**

The planning step is the first in the investment process. Its aim is to understand the client’s needs and develop an investment policy statement (IPS). An investment policy statement (IPS) details the analysis of the investor's objectives and constraints. The IPS should be reviewed regularly.

B is incorrect. The feedback step involves portfolio monitoring and rebalancing, performance measurement and reporting.

C is incorrect. The executive step involves asset allocation, security analysis and portfolio construction.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (b): Describe the steps in the portfolio management process.

Q.1271 Roy Smith wants to invest in equities of emerging markets to buy a new car with the returns. Which of the following will *most likely* provide these details about Smith?

A. The investment policy statement.

B. The prospectus of the investment fund.

C. The brochure of the investment company.

The correct answer is **A.**

The investment policy statement (IPS) is a detailed analysis of the investor's objectives and constraints.

B is incorrect. The fund prospectus is a legal disclosure document that provides information about an investment offering to the public, contains information about the company, its management team, recent financial performance, and other related information that investors would like to know.

C is incorrect. A brochure of the investment company is simply a pamphlet giving information about the investment company.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (b): Describe the steps in the portfolio management process.

Q.1274 Shares of a mutual fund are valued on which of the following bases?

A. The opening price of the fund's shares.

B. The present value of future cash-flows.

C. The net asset value of the fund's shares.

The correct answer is **C.**

Shares of a mutual fund are valued at their net asset value (NAV). It is valued as the total assets minus total liabilities. This amount is then divided by the number of shares that are outstanding.
A is incorrect. Valuing mutual fund shares based on the opening price of the fund's shares does not accurately reflect the fund's value throughout the trading day. Mutual funds consist of a portfolio of various assets, and the value of these assets can fluctuate throughout the day due to market movements. Therefore, relying solely on the opening price would not provide an accurate valuation of the fund's shares by the end of the trading day.

B is incorrect. While the present value of future cash flows is a valuation method used for assessing the value of individual securities or investment projects, it is not the basis for valuing shares of a mutual fund. Mutual funds are valued based on their current net asset value (NAV), which reflects the current market value of the fund's holdings rather than an estimation of future cash flows. This method ensures that the valuation of mutual fund shares is grounded in the present market conditions and the actual value of the fund's assets and liabilities.

CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.1275 MZJ Income Fund is a mutual fund that does not issue new shares, and its shares can only be bought or sold like equity on the over-the-counter (OTC) market. Identify this type of mutual fund.

A. Open-end fund.

B. Closed-end fund.

C. Exchange-traded fund.

The correct answer is **B.**

Closed-end funds are pooled investments that do not take new investments once the fund is established or funded.

A is incorrect. Open end funds accept new investment money and issue additional shares at a value equal to the net asset value of the fund at the time of investments.

C is incorrect. Exchange-traded funds (ETFs) are investment funds that trade on exchanges (similar to individual stocks) and are generally structured as open-end funds.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.1276 Identify the type of funds that invests in US Treasury bills.

A. Open-end fund.

B. Bond mutual fund.

C. Money market funds.

The correct answer is **C.**

US Treasury bills have maturities of less than one year. Money market funds invest in instruments that have maturities of 1 year or less.

A is incorrect. Open end funds are a category of mutual funds that accent new investments and issue additional shares at a value equal to the net asset value of the fund at the time of investment.

B is incorrect. A bond mutual fund is an investment fund consisting of a portfolio of individual bonds and, occasionally, preferred shares. A bond mutual fund holds bonds with maturities as short as one year and as long as 30 years (or more).
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (f): Describe mutual funds and compare them with other pooled investment products.

Q.1277 Which of the following funds are passively managed?

A. Index funds.

B. Stock mutual funds.

C. Money market funds.

The correct answer is **A.**

Index funds match the performance of their benchmark index, i.e.: the S&P 500. These funds do not require active management.

B is incorrect. There are two types of stock mutual funds: actively managed and passively managed.

C is incorrect. Money market funds are mutual funds that invest in short-term money market instruments such as treasury bills, certificates of deposit, and commercial paper.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.1279 Which of the following fund is formed to invest in IPOs and initial stages of new companies and start-ups?

A. Index fund.

B. Hedge fund.

C. Venture capital fund.

The correct answer is **C.**

Venture capital funds are specialized in investing in IPOs and early stages of new companies.

A is incorrect. Index funds match the performance of their benchmark index, i.e.: the S&P 500. These funds do not require active management.

B is incorrect. A hedge fund is a private investment vehicles that typically use leverage, derivatives, and long and short investment strategies.
CFA Level I, Portfolio Management, Learning Module 3: Portfolio Management: An Overview. LOS (e): Describe aspects of the asset management industry.

Q.1332 Investors who believe market prices are informationally efficient will *most likely* follow which of the following investment strategy?

A. Passive investment strategy

B. Bottom-up strategy

C. Active investment strategy

The correct answer is **A.**

Investors who believe that market prices are informationally efficient are more likely to follow a passive investment strategy. This approach involves investing in a diversified portfolio of securities and maintaining that portfolio over the long term without attempting to beat the market through frequent buying and selling. The passive strategy assumes that market prices already reflect all available information, so attempting to outperform the market through active management is seen as futile or inefficient.

B is incorrect. A bottom-up strategy involves selecting stocks based on the analysis of individual companies, with less emphasis on macroeconomic factors or market cycles. This approach is fundamentally at odds with the belief in informational efficiency, as it assumes that through detailed analysis, an investor can identify undervalued stocks and achieve superior returns. However, if markets are truly informationally efficient, as passive investors believe, then all known information about companies would already be reflected in their stock prices, rendering the bottom-up strategy ineffective at consistently outperforming the market.

C is incorrect. An active investment strategy seeks to outperform market benchmarks through stock selection, market timing, and other tactics based on forecasting and analysis. This approach directly contradicts the premise of informational efficiency, as it is predicated on the belief that it is possible to identify mispriced securities or predict market movements better than the collective market. For investors who believe in the Efficient Market Hypothesis, an active investment strategy would be considered both inefficient and unlikely to yield consistent excess returns, given that all available information is presumed to be already factored into stock prices.

CFA Level I, Portfolio Management, Learning Module 4: Basics of Portfolio Planning & Construction. LOS (g): Describe the principles of portfolio construction and the role of asset allocation in relation to the IPS.