

2006 Level 1 Sample Exam Volume 3

SS1-Ethics and Professional Standards

1 James campo, CFA, is a bank loan officer and receives US\$50 from his employer for every client campo refers to the bank's investment advisory department. According to the Standards of Practice Handbook, which of the following best describes Campo's responsibility with respect to disclosing this arrangement? Campo is:

- A not required to disclose the arrangement
- B required to disclose the arrangement to all clients whether or not they are referred.
- C required to disclose the nature and value of the benefit to every client being referred.
- D required to disclose the arrangement to clients at the time of referral, but is not required to disclose the value of the benefit because it is less than US\$100

3 According to the Standards of Practice Handbook, which of the following is NOT a form of plagiarism?

- A Using charts and graphs retrieved from the Internet without specific reference.
- B Presenting factual materials supplied by Standard and Poor's or Moody's without acknowledgment
- C Citing quotations said to be attributable to "leading analysts" or "investment experts" without specific reference.
- D Presenting statistical forecasts prepared by another author with the sources identified but without the qualifying statements that the original author used.

5 Miranda Grafton, CFA, purchased a large block of stock on behalf of specific accounts she managed. The stock realized a significant gain in value before the close of business, so Grafton reviewed her accounts again to determine where the block shares should be allocated. According to the Standards of Practice Handbook, Grafton's most appropriate action is to allocate the shares to:

- A all underperforming accounts she manages.
- B all accounts for which she has discretionary authority.
- C only those accounts for which the block shares were originally intended.
- D only those underperforming accounts for which she has discretionary authority.

9 According to the Global Investment Performance Standards (GIPS), are disclosures related to the definition of firm and the calculation method used, respectively, mandatory or recommended disclosures?

	Disclosures related to definition of "firm"	Disclosures related to calculation method used
A	Mandatory	Mandatory

B	Mandatory	Recommended
C	Recommended	Mandatory
D	Recommended	Recommended

SS2/3-Quantitative Methods

11 An analyst acidulated the following holding period returns for the common stock of Reston., Inc, and Yau Corporation.

Year	Reston	Yau
2000	15.3%	11.3%
2001	-8.2%	9.6%
2002	22.8%	8.6%

For the three-year period, did Yau or Reston achieve the lower.

	Arithmetic mean return?	Geometric mean return
A	Yau	Yau
B	Yau	Reston
C	Reston	Yau
D	Reston	Reston

12 All else equal, would a well-diversified Investor most likely prefer a portfolio with:

	Positive or negative skewness?	A high or low Sharpe ratio?
A	Postive	Low
B	Positive	High
C	Negative	Low
D	Negative	High

13 An analyst creates a nominal scale to categorize the investment style of a sample of managers. The most appropriate measure of central tendency for the analyst to use is the;

- A mean
- B mode
- C median
- D weighted mean

16 An analyst devised three independent screens for a universe of 500 stocks. Of the 500 sticks, 40 percent pass through the first screen, 20 percent pass through the second screen, and 30 percent pass through the third screen, Of the 500 stocks, the number of stocks that would be expected to pass through all three screens is closest to;

- A 2
- B 12

C 90
D 100

SS4/5/6-Economics

20 An analyst is considering investing in the following bonds;

Bond	Description	Time to Maturity
1	Government Security	10 Years
2	AA Corporate	10 Years
3	AA Corporate	15 Years

If investors expect the rate of inflation to remain constant over the next 15 years, will the risk premium for Bond 2 most likely be the same, higher, or lower compared to the risk premium for;

	Bond 1?	Bond 3?
A	Same	Same
B	Same	Lower
C	Higher	Same
D	Higher	Lower

21 With respect to discretionary changes in both monetary and fiscal policy, the time period necessary to gather and tabulate reliable information about an economy's performance is best described as the;

- A impact lag
- B recognition lag
- C administrative period
- D destabilization period

22 Will the short-run effects of an unanticipated expansionary monetary policy most likely include an increase in:

	The real interest rate?	Real output?
A	No	No
B	No	Yes
C	Yes	No
D	Yes	Yes

SS7/8/9/10-Financial Statement Analysis

23 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted. The most detailed information about changes in a company's auditors is found in the company's

- A Form 8-K
- B Form 10-Q
- C registration statement
- D footnotes to the financial statements

26 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted. Which type of risk is most directly measured by the coefficient variation of:

	Operating earnings?	Sales?
A	Business	Business
B	Business	Financial
C	Financial	Business
D	Financial	Financial

27 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted. A company collected \$20,000 in accounts receivable and repaid \$15,000 in short-term loans. The combined effect of these two transactions is to change the company's cash flow from operations by an amount closest to;

- A -\$5,000
- B \$5,000
- C \$20,000
- D \$35,000

31 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted. When construction-in-progress exceeds billings, is a company with continuing flow of profitable long term contracts most likely to have lower total assets and lower total liabilities, respectively, if the company uses the completed contract method or the percentage-of-completion method?

	Lower total assets	Lower total liabilities
A	Completed contract method	Completed contract method
B	Completed contract method	Percentage-of-completion method
C	Percentage-of-completion method	Completed contract method
D	Percentage-of-completion method	Percentage-of-completion method

33 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted. An analyst made the following estimates for a company's next operating period;

Sales	\$275 million
Total assets	\$110 million
Total liabilities	\$60 million

To achieve a return on equity of 30.0 percent for the period, the company must earn a net profit margin closest to

- A 5.5%

- B 6.5%
C 21.8%
D 26.7%

SS11-Corporate Finance

35 An analyst gathered the following information about a company;

Target (optimal) capital structure	
Long term debt	50%
Preferred Stock	10%
Common Equity	40%
After tax component costs:	
Long term debt	6%
Preferred Stock	10%
Retained earnings	14%
New common stock	15%
Expected total earnings (net income) for the year in millions	\$120
Target dividend payout ration	45%

If the company raises \$150 million in new capital, the company's marginal cost of capital is closest to;

- A 9.6%
B 10.0%
C 14.0%
D 15.0%

36 An analyst estimated the following data for a company

Debt/Assets Ratio	Earnings Per Share	Before-tax Cost Debt	Component Cost of Equity	Weighted-average cost of Capital
30%	\$2.00	10.0%	15.8%	11.9%
40%	\$2.10	10.8%	15.5%	11.3%
50%	\$2.25	12.0%	14.9%	11.6%
60%	\$2.20	15.0%	14.6%	11.8%

The trend in the company's debt/assets ratio is least consistent with the trend in;

- A earnings per share
B before-tax cost of debt
C component cost equity
D weighted-average cost of capital

37 Is the argument that, all other factors being equal, investors would be willing to pay more for the common stock of companies with low dividend payouts than for the common stock of companies with high dividend payouts consistent with the

	Tax preference theory?	Bird in the hand theory?
A	No	No
B	No	Yes
C	Yes	No
D	Yes	Yes

SS13/14-Equity Investments

43 In an informationally efficient securities market, new information results in profit-maximizing investors making price adjustments that are best described as;

- A unbiased but not predictable
- B predictable but not unbiased
- C both unbiased and predictable
- D neither unbiased nor predictable

44 An investor who must pay an amount equal to a particular security's dividend to another investor is most likely using;

- A. margin
- B. a short sale
- C. a limit order
- D. a market order

SS17-Derivative Investments

47 An investor paid \$10 for a call option with an exercise price of \$105. If the underlying stock is currently trading at \$102, the call option is best described as being;

- A in-the-money by \$3
- B in-the-money by \$13
- C out-of-the-money by \$3
- D out-of-the-money by \$13

SS18-Alternative Investments

50 For hedge funds that use arbitrage strategies, is the true risk of losses most likely to be understated if that risk is measured by:

	Standard deviation?	Traditional value at risk (VaR) measures?
A-	No	No

B	No	Yes
C	Yes	No
D	Yes	Yes

51 Compared to other exchange traded funds (ETFs), which of the following types of risk is unique to ETFs that are exposed to counterparty credit risk?

- A Market risk
- B Trading risk
- C Derivatives risk
- D Tracking error risk

SS15/16-Fixed Income Investments

52 For option-free bonds, greater interest rate risk is exhibited by bonds with;

- A longer maturity and a lower coupon rate
- B longer maturity and a higher coupon rate
- C shorter maturity and a lower coupon rate
- C shorter maturity and a higher coupon rate

54 For a fixed-rate, option-free bond, as yields decrease, the price of the bond;

- A increases at a constant rate
- B increases at a decreasing rate
- C decreases at a decreasing rate
- D increases at an increasing rate

57 The yield on an industrial bonds 8.59 percent while the yield on a benchmark bond with the same maturity is 6.83 percent. The relative yield spread is closest to;

- A 1.8%
- B 20.5%
- C 25.8%
- D 79.5%