2009 Sample Exam 1 Questions

SS1-Ethics and Professional Standards

1. According to the CFA Institute Standards of Practice Handbook, insider trading is least likely to be prevented by establishing:

A. fire walls.
B. watch lists.
C. selective disclosure.

2. William Wong, CFA, is an equity analyst with Hayswick Securities. Based on his fundamental analysis, Wong concludes that the stock of a company he follows, Nolvec Inc., is substantially undervalued and will experience a large price increase. He delays revising his recommendation on the stock from "hold" to "buy" to allow his brother to buy shares at a lower price. According to the Standards of Practice Handbook, Wong is *least likely* to have violated the CFA Institute Standards of Professional Conduct that relate to:

A. duty to clients.
B. reasonable basis.
C. priority of transactions.

3. During an onsite company visit, Marsha Ward, CFA, accidentally overheard the Chief Executive Officer (CEO) of Stargazer, Inc., discussing the company's pending tender offer to purchase Dynamic Enterprises, a retailer of Stargazer products. According to the Standards of Practice Handbook, Ward may not use the information to take investment action because:

A. the information relates to a tender offer.
B. she does not have a reasonable and adequate basis for taking investment action.
C. acting on the information would breach a duty to both Stargazer and Dynamic

4. Ian O'Sullivan, CFA, is the owner and sole employee of two companies, a public relations firm and a financial research firm. The public relations firm entered into a contract with Mallory Enterprises to provide public relations services. According to the contract, O'Sullivan received 40,000 shares of Mallory stock in payment for his services. Over the next 10 days, the public relations firm issued several press releases that discussed Mallory's excellent growth prospects. O'Sullivan, through his financial research firm, also published a research report recommending Mallory stock as a "buy". According to the Standards of Practice Handbook, O'Sullivan is required to disclose his ownership of Mallory stock in the:

A. press releases only.
B. research report only.
C. both the press release and the research report

5. Jefferson Piedmont, CFA, a portfolio manager for Park Investments, plans to manage the portfolios of several family members in exchange for a percentage of each portfolio's profits. As his family members have requested that Piedmont provide the services outside his employment with Park, he notifies his employer in writing of his prospective outside employment. Two weeks later, Piedmont has received no response from his employer and begins managing the family members' portfolios. By managing these portfolios, did Piedmont violate any CFA Institute Standards of Professional Conduct?

A. No.
B. Yes, because he failed to obtain written consent from his employer.
C. Yes, because he failed to mention that the outside employment was with family members.

6. The eight major provisions of the Global Investment Performance Standards (GIPS) include all of the following except:

A. Input Data, Calculation Methodology, and Real Estate.
B. Fundamentals of Compliance, Composite Construction, and Disclosures.
C. Calculation Methodology, Composite Construction, and Alternative Assets.

7. Hui Chen, CFA, develops marketing materials for an investment fund he founded three years ago. The materials show the 3-, 2- and 1-year returns for the fund. He includes a footnote that states in small print, "Past performance does not guarantee future returns." He also includes a separate sheet showing the most recent semiannual and quarterly returns, which have been neither audited nor verified. According to the Standards of Practice Handbook, has Chen violated any Standards of Practice?

A. No.
B. Yes, because he included unaudited and unverified results.
C. Yes, because he did not adhere to the Global Investment Performance Standards.

8. Charlie Mancini, CFA, is the Managing Director for Business Development at VES Financial (VES), a large U.S.-based mutual fund organization. Mancini has been under pressure recently to increase revenues. In order to secure business from a large hedge fund manager based in Asia, Mancini recently approved unusual terms for the fund's client agreement. To allow for time zone differences, the agreement allows the hedge fund to trade in all of VES's mutual funds six hours after the close of

U.S. markets. According to the Standards of Practice Handbook, did Mancini violate any CFA Institute Standards of Professional Conduct?

A. No.
B. Yes, because he failed to inform his other clients of the unusual terms under the new client agreement, thus not treating clients equally.
C. Yes, because he failed to review regulations on late-trading and did not consult with VES's compliance director to determine if late-trading was acceptable.

9. Ron Dunder, CFA, is the CIO for Blind Trust (BT), an investment advisor. Dunder recently assigned one of his portfolio managers, Doug Cheetah, to manage several accounts that primarily invest in thinly traded micro-cap stocks. Dunder soon notices that Cheetah places many stock trades for these accounts on the last day of the month, towards the market's close. Dunder finds this trading activity unusual and speaks to Cheetah, who explains that the trading activity was completed at the client's request. Dunder doest not investigate further. Six months later regulatory authorities sanctions BT for manipulating micro-cap stock prices at month-end in order to boost account values. According to the Standards of Practice Handbook, did Dunder violate any CFA Institute Standards of Professional Conduct?

A. No.
B. Yes, because he failed to reasonably supervise Cheetah.
C. Yes, because he did not report his findings to regulatory authorities.

SS2/3-Quantitative Methods

10. An increase in which of the following items is most likely to result in an increase in the width of the confidence interval for the population mean?

A. Sample size.
B. Reliability factor.
C. Degrees of freedom.

11. A random variable with a finite number of equally likely outcomes is best described by a:

A. Binomial distribution.
B. Discrete uniform distribution.
C. Continuous uniform distribution.

12. The joint probability of returns, for securities A and B, are as follows:

Joint Probability Function of Security A and Security B Returns

(Entries are joint probabilities)		
	Return on security B = 30%	Return on security B = 20%
Return on security A = 25%	0.60	0
Return on security A = 20%	0	0.40

The covariance of the returns between securities A and B is closest to:

A. 3%.
B. 12%.
C. 24%.

13. The bond-equivalent yield for a semi-annual pay bond is most likely:

    A. Equal to the effective annual yield.
    B. More than the effective annual yield.
    C. Equal to double the semiannual yield to maturity.

14. An analyst determines that approximately 99 percent of the observations of daily sales for a company are within the interval from $230,000 to $480,000 and that daily sales for the company are normally distributed. The standard deviation of daily sales for the company is closest to:

    A. $41,667
    B. $62,500
    C. $83,333

15. An analyst gathered the following information about a stock index:

Mean net income for all companies in the index	$2.4 million
Standard deviation of net income for all companies in the index	$3.2 million

If the analyst takes a sample of 36 companies from the index, the standard error of the sample mean is closest to:

A. $66,667.
B. $88,889.
C. $533,333.

16. The least accurate statement about measures of dispersion for a distribution is that the:

    A. Range provided no information about the shape of the data distribution.
    B. Arithmetic average of the deviations around the mean will always be equal to one.

C. Mean absolute deviation will always be less than or equal to the standard deviation.

SS4/5/6-Economics

17. if the prices of substitute resources decrease, the demand for a given resource will most likely:

A. Increase
B. Decrease
C. Remain unchanged

18. The free-rider problem, an obstacle to efficiency, is most likely associated with:

A. Monopolies
B. Public goods.
C. Subsidies and quotas.

19. An expansionary fiscal policy is most likely to include a(n):

A. Decrease in both interest rates and tax rates.
B. Increase in government expenditures and a decrease in tax rates.
C. Increase in both government expenditures and central bank's open market purchases.

20. The crowding-out effect suggests that the government borrowing to finance higher expenditures will most likely increase:

A. Inflation but reduce private saving.
B. The real interest rate and increase private saving.
C. The real interest rate and increase private investment.

21. In perfectly competitive industries, what is the most likely long-run effect of a permanent decrease in demand?

A. Price decreases.
B. Firms incur economic losses
C. The number of firms decreases.

22. As compared with acting independently, a group of oligopolistic companies operating with perfect cooperation will most likely experience an increase in:

A. Both output and prices.

B. Output and a decrease in prices.
C. Prices and a decrease in output.

SS7/8/9/10-Financial Statement Analysis

23. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

L'Eau Ltd. reports sales of €50,000,000 for the year ended 31 December 2008. Accounts receivable balances were €6,000,000 at 1 January 2008, and €7,500,000 at 31 December 2008. The company's cash collections from sales for 2008 is closest to:

A. €42, 500, 000.
B. €48, 500, 000.
C. €51, 500, 000.

24. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

On the cash flow statement, the payment of cash dividends during the year will most likely affect the cash flow from:

A. Operations
B. Investing activities
C. Financing activities

25. In the statement of cash flows, a company is allowed to classify interest paid:

A. In either the operating or financing section under IFRS.
B. In either the operating or financing section under U.S.GAAP.
C. Only in the financing section under both IFRS and U.S.GAAP.

26. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

Foreign currency translation adjustments are most likely reported in the company's:

A. Income statement.
B. Statement of cash flows.
C. Statement of stockholders' equity.

27. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

An analyst gathers the following information (U.S. $ millions) for two companies operating in the same industry during the same period:

	Butler Enterprises	Annandale Corporation
Net sales	$120	$300
Total assets	$70	$140
Total liabilities	$25	$40

If both companies achieved a return on equity of 15 percent for the period, which of the following statements is most likely correct? Compared to Annandale, Butler has a:

A. Higher net profit margin.
B. Higher total asset turnover.
C. Lower financial leverage multiplier.

28. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

An entry made to record an accrual, such as bad debt expense, that is not yet reflected in the accounting system is best described as a(n):

A. Ledger entry.
B. Adjusting entry.
C. Trial balance entry.

29. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

A company, with a tax rate of 40 percent, sold a capital asset with a net book value of $500,000 for $570,000 during the year. Which of the following amounts will most likely be reported on their income statement for the year related to the asset sale?

A. $ 42,000.
B. $ 70,000
C. $570,000

30. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

A company issued bonds in 2006 that mature in 2016. The measurement basis used for the bonds on the 2008 balance sheet will be:

A. Market value

B. Historical cost
C. Amortized cost

31. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

Which of the following transaction is least likely to increase a company's reported cash from operations?

A. Securitizing accounts receivable
B. Delaying payments made to suppliers
C. Using short-term debt to reduce an existing account payable.

32. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

An analyst makes the appropriate adjustments to the financial statements of retail companies that are lessees using a substantial number of operating leases. Compared to ratios computed from the unadjusted statements, the ratios computed from the adjusted statements would most likely be higher for:

A. The debt-equity ratio but not the interest coverage ratio.
B. The interest coverage ratio but not the debt-equity ratio.
C. Both the debt-equity ratio and the interest coverage ratio.

33 Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

To gain insight into what position of the company's assets is liquid, an analyst will most likely use:

A. The cash ratio
B. The current ratio
C. Common-size balance sheets

34. Assume U.S. GAAP (generally accepted accounting principles) applies unless otherwise noted.

Two manufacturing companies operating in the same industry have different net fixed asset turnover ratios. The difference most likely occurs because the company with the higher ratio:

A. had significantly lower amortization expense for the year.
B. was operating with older equipment that had a low cost basis.

C. recently invested a substantial amount in new plant and equipment.

35. The five-component DuPont analysis of a company's ROE for 2008 is as follows:

Operating profit margin	Effect of non-operating items	Tax effect	Total asset turnover	Financial leverage
7.5%	0.95	0.67	2.2	1.2

For 2009, the company is considering increasing its financial leverage to 1.5, but the increased borrowing costs would reduce the effect of nonoperating items to 0.85. Incorporating these changes, the company's expected ROE for 2009 would be closest to:

A. 11.28%
B. 12.60%
C. 14.09%

SS11-Corporate Finance

36. An analyst is estimating the cost of capital for her firm. She has estimated the before-tax costs of the current sources of capital to be 8 percent for debt and 9 percent for equity. If the firm's marginal tax rate is 40 percent, the costs of debt and equity she should use in her calculation are closest to:

A. 4.8% for debt and 5.4% for equity.
B. 4.8% for debt and 9.0% for equity.
C. 8.0% for debt and 5.4% for equity.

37. As part of working capital management, the short-term investment strategy that has the highest degree of risk for an entity and requires very accurate and reliable forecasts of cash flows is:

A. A matching strategy.
B. A laddering strategy.
C. A mismatching strategy.

38. The internal rate of return (IRR) method of evaluating investment projects:

A. Is the preferred method for evaluating mutually exclusive projects.
B. Is not sensitive to the pattern or timing of the cash flows from the project.
C. Assumes that all cash flows from the project will be reinvested at the computed IRR.

39. An analyst gathered the following information about a company and the company's industry:

	Company	**Industry**
Accounts receivable turnover	5.6 times	6.5 times
Inventory turnover	4.2 times	4.0 times
Number of days of payables	28 days	36 days

Relative to the industry, the company's operating cycle:

A. And the cash conversion cycle are both longer.
B. Is longer, but the cash conversion cycle is shorter.
C. Is shorter, but the cash conversion cycle is longer.

40. An analyst gathered the following information about the company:

	2001	2008
Sales	$128.4 million	$220.0 million
Return on equity (ROE)	10 percent	10 percent
Net profit margin (NPM)	6 percent	7 percent
Number of shares outstanding	5 million	6 million

The analyst expects sales in 2009 to grow at the historical compound annual growth rate from the year 2001 to 2008. For the year 2009, the net profit margin and the number of shares outstanding are expected to remain unchanged from the year 2008. The company's earnings per share (EPS), for the year 2009, is closest to:

A. $2.77
B. $2.83
C. $3.96

41. The most likely motivation for a speculator to sell a security short is based on the investor's belief that the

A. Security is overpriced.
B. Required rate of return on the security will decline.
C. Short sale proceeds could be invested for extra returns.

42. An analyst gathered the following information for a company whose common stock is currently priced at $40 per share:

	2004	2005	2006	2007	2008
Earnings per share ($)	1.16	0.62	1.28	1.60	(1.30)
Book value per share ($)	8.48	8.92	16.04	19.28	16.30

Return on equity(ROE)	14%	7%	8%	8%	

Because of the severe cyclical contraction that occurred in 2008 for a major segment of the company's operations, the analyst decides to normalize earnings (adjusted for business cycle effects) using the 2004-2007 period. If the analyst also decides to account for changes in the company's size over time, the most appropriate estimate of the company's 2008 price/earnings (P/E) ratio based on normalized earnings is:

A. 26.5.
B. 32.8.
C. 34.2.

SS13/14-Equity Investments

43. Which of the following most accurately describes the computation of nearly all bond market indexed, U.S. and global?

A. Model priced.
B. Trader priced.
C. Market priced.

44. Which of the following is most directly associated with secondary capital markets?

A. Source of liquidity.
B. Security underwriting.
C. Shelf registration of securities.

45. All else equal, a decrease in the expected rate of inflation will most likely result in a decrease in:

A. The real risk-free rate
B. The nominal risk-free rate
C. Both real and nominal risk free rate

SS17-Derivative Investments

46. A company is long an interest rate swap with a current market value of $ 125,000. The company wants to terminate this swap before the expiration date. From a credit risk perspective, which of these is the least attractive way to terminate the swap?

A. Sell the swap to a third party.
B. Short an offsetting swap with a third party.

C. Agree to terminate the swap and receive its market value from the counterparty.

47. A European stock index call option has a strike price of $1160 and a time to expiration of 0.25 years. Given a risk-free rate of 4 percent, if the underlying index is trading at $1200 and has a multiplier of 1, then the lower bound for the option price is closest to:

A. $28.29.
B. $40.00.
C. $51.32.

48. Which of these is best classified as a forward commitment derivative?

A. A swap agreement
B. A convertible bond
C. An asset-backed security

SS18-Alternative Investments

49. Hedge funds that contain infrequently traded assets would most likely exhibit a downward bias with respect to:

A. Measured risk but not correlations with conventional equity investments
B. Correlations with conventional equity investments but not measured risk
C. Both measured risk and correlations with conventional equity investments

50. Which of the following statements is least accurate with respect to the advantages of open-end exchange traded funds (ETFs)? Open-end ETFs:

A. Provide for more immediate reinvestment of dividends than do index mutual funds.
B. Provide a more cost-effective way for large institutions to invest in emerging markets.
C. Provide lower exposure to capital gains distribution taxes than traditional mutual funds.

51. A real estate investment has the following characteristics:

Annual rental income	$1,800,000
Annual operating expenses	$1,200,000
Available mortgage rates	6%
Financing percentage	90%
Required rate of return	15%
Estimated holding period	5 years

Investor's tax rate	25%

Based on the income approach, the value of the investment is closest to:

A. $4,000,000.
B. $5,455,000.
C. $6,133,000.

SS15/16-Fixed Income Investments

52. An analyst determines that an 8 percent option-free bond, maturing in 2015, would experience a 3 percent change in price if market interest rates rise by 50 basis points. If market interest rates instead fall by 50 basis points, the bond's price would increase by:

A. exactly 3%.
B. less than 3%.
C. more than 3%.

53. Holding all other factors constant, an increase in expected yield volatility will cause the price of:

A. A putable bond to increase.
B. A callable bond to increase.
C. Embedded put and call options to decrease.

54. The table below summarizes the yields and corresponding prices for a hypothetical 15-year option-free bond that is initially priced to sell at 7percent yield:

Yield(%)	Price($)
6.90%	100.9254
7.00%	100.0000
7.10%	99.0861

Using a 10 basis point rate shock, the effective duration for this bond is closest to:

A. 4.6 years.
B. 7.5 years.
C. 9.2 years.

55. According to the market segmentation theory, an upward sloping yield curve is most likely due to:

A. Investor expectations that short-term interest rates will rise in the future.

B. Different levels of supply and demand for short-term and long-term funds.
C. An increasing yield premium required by investors for bearing interest rate risk.

56. An 8 percent coupon bond with a par value of $100 matures in 6 years and is selling at $95.51 with a yield of 9 percent. Exactly one year ago this bond sold at a price of $90.26 with a yield of 10 percent. The bond pays annual interest. The change in price attributable to the change in maturity is closest to:

A. $1.03.
B. $4.22.
C. $5.25.

57.A fixed income portfolio manager owns a $5 million par value noncallable bond . The bond's duration is 5.6 and the current market value is $5,125,000. The dollar duration of the bonds is closest to:

A. $280,000.
B. $287,000.
C. $700,000.

SS12-Portfolio Management

58. Portfolios located to the right of the market portfolio on the capital market line are:

A. Lending portfolios.
B. Optimal portfolios.
C. Borrowing portfolios.

59. An important reason for consulting an investment policy statement is that it:

A. Minimizes the costs of portfolio construction.
B. Ensures that managers outperform the performance benchmark.
C. Includes a performance benchmark to judge manager performance.

60. An analyst gathered the following information about two common stocks:

- Variance of returns for the Libby Company = 15.5
- Variance of returns for the Metromedia Company = 22.3
- Covariance between returns of Libby Company and Metromedia Company=8.65

The correlation coefficient between returns for the two common stocks is closest to:

A. 0.025

B. 0.388
C. 0.465