**Jun. 2012 CFA Level 1 Mock Examination**

**Morning Session**

**Study Session 1 – Ethical and Professional Standards (1-18) Q=18**

1. Carlos Cruz, CFA, is one of two founders of an equity hedge fund. Cruz manages the fund's assets while the other co-founder, Brian Burkeman, is responsible for fund sales and marketing. Cruz notices that the most recent sales material used by Burkeman indicates the value of the assets under management in the fund is listed at a higher than actual value. Burkeman justifies the discrepancy by stating that the recent market decline accounts for the difference. To avoid violating the CFA Institute Standards of Professional Conduct, Cruz should least likely take which of the following actions?

A. Correct the asset information and provide the update to prospective clients.

B. Report the discrepancy to the Professional Conduct Program of CFA Institute.

C. Check with the firm's legal counsel to determine what action should be taken.

2. Linda Chin, CFA, is a member of a political group advocating lower governmental regulation in all aspects of life. She works in a country where local securities laws are minimal and insider trading is not prohibited. Chin's politics are reflected in her investment strategy, where she follows her country's mandatory legal and regulatory requirements. What steps should Chin most likely take to ensure she does not violate any CFA Institute Standards of Professional Conduct?

A. Continue current investment strategy.

B. Follow the CFA Institute Code and Standards.

C. Disclose to clients that she meets mandatory legal requirements.

3. Wouter Duyck, CFA, is the sole proprietor of an investment advisory firm serving a middle-class retail clientele. Duyck claims to be different from his competitors because he conducts his own independent research. Duyck has hundreds of clients. He fully discloses that to simplify the management of all these accounts he has created a recommended list of stocks, from which he selects investments for all of his clients. Duyck's recommended list of stocks is obtained from his primary broker, who has completed due diligence on each stock. Duyck's recommended list least likely violates which of the following CFA Institute Standards of Professional Conduct?

A. Fair Dealing.

B. Misrepresentation.

C. Diligence and Reasonable Basis.

4. Lisa Hajak, CFA, specialized in research on real estate companies at Cornerstone Bank (CB) for the past twenty years. Hajak recently started her own investment research firm, Hajak Advisory (HA). One of her former clients at CB asks Hajak to update a research report she wrote on a real estate company when she was at CB. Hajak updates the report, which she had copied to her personal computer, without the bank's knowledge, and replaces references to the bank with her new firm, HA. Hajak incorporates the conclusions of a real estate study conducted by the Realtors Association that appeared in the Wall Street Journal. She references the Journal as her source in her report. She provides the revision free of charge along with a request for the bank's client to become a client of her firm. Concerning the reissued research report, Hajak least likely violated the CFA Institute Standards of Professional Conduct because she:

A. solicited the bank's client.

B. did not obtain consent to use the bank report.

C. must cite the actual source of the real estate study.

5. Tonya Tucker, CFA, is a financial analyst at BC Corporation (BC). BC has numerous subsidiaries and is actively involved in mergers and acquisitions. Tucker analyzes HR Corporation (HR) and tells the CEO of BC that the acquisition of HR would be a good fit for BC. After her discussion with the CEO, Tucker purchases 100,000 shares of HR at $200 per share. BC does not have any pre-clearance procedures, so the next time she meets the CEO, Tucker mentions she is a stockowner of HR. The CEO thanks her for this information but does not ask for any details. Two weeks later, Tucker sees a company-wide email from the CEO announcing BC's acquisition of HR for $250 a share. Regarding her purchase of HR stock, Tucker most likely violated the CFA Institute Standards of Professional Conduct concerning:

A. Loyalty.

B. Market Manipulation.

C. Material Nonpublic Information.

6. When a client asks her how she makes investment decisions, Petra Vogler, CFA, tells the client she uses the mosaic theory. According to Vogler, the theory involves analyzing public and nonmaterial nonpublic information, including evaluating statements made to her by company insiders in one-on-one meetings discussing management's new earnings projections not known to the public. She also gathers general industry information not known to the public from industry experts and other contacts. Vogler most likely violates the CFA Institute Standards of Professional Conduct because of her use of:

A. industry contact information.

B. one-on-one meeting information.

C. nonmaterial nonpublic information in her analysis.

7. Lin Liang, CFA, is an investment manager and an auto industry expert. Last month, Liang requested securities regulators to open an investigation into accounting irregularities at Road Rubber Company (RRC) despite having no basis for the request. Shortly before he spoke to the regulators, Liang shorted RRC stock for his clients. Once the regulators opened an investigation, Liang leaked this information to multiple sources in the media. When news of the investigation became public, the share price of RRC immediately dropped 30%. Liang then covered the short positions and made $5 per share for his clients. Liang least likely violated which of the CFA Institute Standards of Professional Conduct?

A. Misconduct.

B. Market Manipulation.

C. Priority of Transactions.

8. Sanjay Gupta, CFA, has been hired by the First Faithful Church to manage the pension plan's equity portfolio. The plan trustees tell Gupta that stocks of companies involved in the sale of alcohol, tobacco, gambling, or firearms are not acceptable investments. Gupta believes that he can reasonably execute his strategy with this restriction. Does Gupta violate the CFA Institute Standards of Professional Conduct?

A. No.

B. Yes, because the restrictions provided in the guidelines are not in the best interest and objectives of the client.

C. Yes, because Gupta should construct the portfolio with these limitations since he can execute on the strategy.

9. Jorge Lopez, CFA, is responsible for his bank's proxy voting on behalf of the bank's asset management clients. Lopez recently performed a cost-benefit analysis, showing that voting all proxies might not benefit the bank's clients. Based on this analysis, Lopez changes the proxy voting policies and procedures without informing anyone else of the change. Lopez now votes client proxies on the side of management on all issues with the exception of major mergers where a significant impact on the stock price is expected. Lopez least likely violated the CFA Institute Standards of Professional Conduct regarding:

A. cost-benefit analysis.

B. voting with management.

C. proxy voting policy disclosures.

10. Henrietta Huerta, CFA, writes a free investment newsletter widely followed by individual investors. Huerta is not aware of who receives the newsletter but it is the primary marketing tool she uses to obtain investment management clients for those who contact her and are willing to pay management fees. For Huerta, the newsletter recommendations serve as the basis for most of her investment actions. Huerta recently completed research on East-West Coffee Roasters (ECR) and has decided to change her initial buy recommendation on ECR to a sell. To avoid violating the CFA Institute Standards of Professional Conduct, Huerta should *most likely* ensure that the changed investment recommendation reaches:

A. newsletter recipients first.

B. asset management clients first.

C. asset management clients and newsletter recipients simultaneously.

11. Danielle Deschutes, CFA, is a portfolio manager and part of a ten-person team managing an indexed stock portfolio for institutional accounts. A competing firm, South West Index Managers (SWIM), asks Deschutes to interview with them and to bring her performance history to the meeting. Deschutes informs her employer about the interview and receives written permission to bring the performance history of the stock portfolio with her. When Deschutes shows up for the interview at SWIM she discloses that the performance numbers represent the work of her team and describes the role of each member. To bolster her credibility, she also provides the names of institutional accounts and related assets constituting the portfolio. In her interview at SWIM, Deschutes *least likely* violated the CFA Institute Standards of Professional Conduct regarding:

A. her contribution to the portfolio's returns.

B. the stock portfolio's performance history.

C. providing details on the institutional accounts.

12. When Abdullah Younis, CFA, became a broker at a global financial services organization two years ago, he was told he could allocate his work hours as he saw fit. At this time, Younis served on the board of three non-public golf equipment companies and managed money for several members of his immediate family in a pooled fund. Younis was not compensated for his board service or for the investment pool management. Younis' outstanding returns attract interest from friends and co-workers who persuade him to include their assets in his investment pool. Younis recently retired from all board responsibilities and now spends more than 80% of his time managing the investment pool for which he charges non-family members a management fee. Younis has never told his employer about any of these activities. To comply with the CFA Institute Standards of Professional Conduct, regarding his business activities over the past two years, Younis should *least likely* disclose which of the following to his employer?

A. Board activity.

B. Family investment pool management.

C. Non-family member management fees.

13. Kim Klausner, CFA, manages several hundred employees as the head of research for a large investment advisory firm. Klausner is a former securities regulatory official who, until recently, ensured that his department's compliance program always met or exceeded those of its competitors. Klausner has delegated his supervisory responsibilities concerning compliance issues to Sue Chang. Klausner informed Chang that her responsibilities include ensuring that the firm has appropriate compliance procedures and is making reasonable efforts to detect and prevent violations of Rules, Regulations, and the Code and Standards. Klausner *most likely* violated the CFA Institute Standards of Professional Conduct by **not** telling Chang to consider:

A. firm policies.

B. legal restrictions.

C. industry standards.

14. Sheila Schleif, CFA, is an equity analyst at an investment bank. Schleif uses a data-driven computer model in making her stock recommendations. Schleif discovers the model contains a coding error. If the coding error were corrected, her most recent buy recommendation would change to a sell. Schlief corrects the coding error, issues a bank-wide revision of her recommendation changing the buy to a sell, and then forwards the revision to all bank clients who received the initial recommendation. Concerning her actions related to the coding error, Schlief *most likely* violated which of the following CFA Institute Standards of Professional Conduct?

A. Fair Dealing.

B. Priority of Transactions.

C. Diligence and Reasonable Basis.

15. Rodney Rodrigues, CFA, is responsible for identifying managers to manage specific asset classes for his firm. In selecting external advisers or subadvisers, Rodrigues reviews the adviser's investment process, established code of ethics, the quality of their published return information, and their compliance and internal control procedures. In completing his review, Rodrigues *most likely* violated the CFA Institute Standards of Professional Conduct regarding his due diligence on:

A. adherence to strategy.

B. performance measures.

C. internal control procedures.

16. Jackson Barnes, CFA, provides financial planning services to his local community for a fee. Barnes has developed a network of specialists including accountants, lawyers, and brokers who contribute their expertise to the financial planning process. Each of the specialists is an independent contractor. Each contractor bills Barnes separately for the work they perform, providing a discount based upon the number of clients Barnes has referred. What steps should Barnes *most likely* take to ensure he does **not** violate any CFA Institute Standards of Professional Conduct?

A. Check with his firm's legal counsel to determine what action should be taken.

B. Disclose to clients on their bills the consideration he receives from the specialists.

C. Inform clients about his arrangement with the contractors before they agree to hire him.

17. Millicent Plain, CFA, has just finished taking Level II of the CFA examination. Upon leaving the examination site, she meets with four other Level III candidates who also just sat for their exams. Curious about their examination experience, Plain asks the other candidates how difficult the Level III exam was and how they did on it. The candidates say the examination was very difficult but do not speak about specific questions. However, the candidates tell Plain about broad topic areas that were tested and complain about specific formulas, which they prepared for but which did not appear on the exam. The Level III candidates *least likely* violated the CFA Institute Standards of Professional Conduct by discussing:

A. specific formulas.

B. broad topic areas.

C. difficulty of the examination.

18. On a flight to Europe, Romy Haas, CFA, strikes up a conversation with a fellow passenger, Vincent Trujillo. When Trujillo learns Haas is in the investment profession, he asks about the CFA designation. Haas tells him the following about the CFA designation:

|  |  |
| --- | --- |
| Statement 1: | Individuals who have completed the CFA Program have the right to use the CFA designation. |
| Statement 2: | Use of the designation must be accompanied by an accurate explanation of the requirements to earn and use the designation. |
| Statement 3: | Once granted the right to use the designation, an individual must also satisfy the CFA Institute membership requirements to maintain their right to use the designation. |

In explaining the use of the CFA designation, Haas *least likely* violated the CFA Institute Standards of Professional Conduct concerning which of the following statements?

A. Statement 1.

B. Statement 2.

C. Statement 3.

**Study Session 2, 3 – Quantitative Methods (19-32) Q=14**

19. The nominal (quoted) annual interest rate on an automobile loan is 10%. The effective annual rate of the loan is 10.47%. The frequency of compounding periods per year for the loan is closest to:

A. weekly.

B. monthly.

C. quarterly.

20. A U.S. Treasury bill (T-bill) has 90 days to maturity and a bank discount yield of 3.25%. The effective annual yield (EAY) for the T-bill is closest to:

A. 3.29%.

B. 3.32%.

C. 3.36%.

21. The following ten observations are a sample drawn from an approximately normal population:

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Observation** | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
| **Value** | –3 | –11 | 3 | –18 | 18 | 20 | –6 | 9 | 2 | –16 |

The sample standard deviation is closest to:

A. 11.92.

B. 12.50.

C. 13.18.

22. Assume that a stock's price over the next two periods is as shown below.

|  |  |  |
| --- | --- | --- |
| Time = 0 | Time = 1 | Time = 2 |
| S0 = 80 | Su = 88 | Suu = 96.8 |
| Sd = 72 | | Sud,du = 79.2 |
| Sdd = 64.8 | | |

The initial value of the stock is $80. The probability of an up move in any given period is 75% and the probability of a down move in any given period is 25%. Using the binomial model, the probability that the stock's price will be $79.20 at the end of two periods is closest to:

A. 18.75%.

B. 37.50%.

C. 56.25%.

23. If the stated annual interest rate is 20% and the frequency of compounding is monthly, the effective annual rate (EAR) is *closest* to:

A. 20%.

B. 21%.

C. 22%.

24. A two-tailed test of the null hypothesis that the mean of a distribution is equal to 4.00 has a p-value of 0.0567. Using a 5% level of significance (i.e., α = 0.05), the best conclusion is to:

A. reject the null hypothesis.

B. accept the null hypothesis.

C. increase the level of significance to 5.67%.

25. A stock is declining in price and reaches a price range wherein buying activity is sufficient to stop the decline. This is best described as a:

A. support level.

B. resistance level.

C. change in polarity points.

26. A borrower is considering three competing mortgage loan offers from her bank. The amount borrowed on the mortgage is $100,000 with monthly compounding.

|  |  |  |
| --- | --- | --- |
| **Mortgage type** | **Nominal (stated) annual interest rate at initiation of the loan** | **Year in which rate first adjusts** |
| 30-year fixed rate | 5% | N/A |
| 15-year fixed rate | 4.385% | N/A |
| 30-year 3/5 adjustable rate mortgage (ARM) | 3.75% | 3 |

The rate on the ARM resets at the end of the year 3. Assuming the ARM is reset at 5.5% (i.e. the remaining balance on the loan will now be repaid with 5.5% nominal annual interest), which of the three loans will have the *smallest* monthly payment after the rate reset, at the end of year 3?

A. 30-year ARM.

B. 15-year fixed-rate loan.

C. 30-year fixed-rate loan.

27. Equity returns series are *best* described as, for the most part:

A. platykurtotic (less peaked than a normal distribution).

B. leptokurtotic (more peaked than a normal distribution).

C. mesokurtotic (identical to the normal distribution in peakedness).

28. By definition, the probability of any event *E* is a number between:

A. zero and positive one.

B. zero and positive infinity.

C. minus one and positive one.

29. X and Y are independent events. The probability of X is 0.2 (P(X) = 0.2) and the probability of Y is 0.5 (P(Y) = 0.5). The joint probability of X and Y (P(X, Y) is *closest* to:

A. 0.1.

B. 0.3.

C. 0.7.

30. A variable is normally distributed with a mean of 5.00 and a variance of 4.00. Calculate the probability of observing a value of negative 0.40 or less. That is, calculate P (Xi ≤ –0.40) given X is distributed as N(5, 4). Use this excerpt from the cumulative distribution function for the standard normal random variable table to calculate your answer.

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Cumulative Probabilities for a Standard Normal Distribution P(Z ≤ x) = N(x) for x ≥ 0 or P(Z ≤ z) = N(z) for z ≥ 0** | | | | | | | | | | |
| x or z | 0 | 0.01 | 0.02 | 0.03 | 0.04 | 0.05 | 0.06 | 0.07 | 0.08 | 0.09 |
| 1.10 | 0.8643 | 0.8665 | 0.8686 | 0.8708 | 0.8729 | 0.8749 | 0.8770 | 0.8790 | 0.8810 | 0.8830 |
| 1.20 | 0.8849 | 0.8869 | 0.8888 | 0.8907 | 0.8925 | 0.8944 | 0.8962 | 0.8980 | 0.8997 | 0.9015 |
| 1.30 | 0.9032 | 0.9049 | 0.9066 | 0.9082 | 0.9099 | 0.9115 | 0.9131 | 0.9147 | 0.9162 | 0.9177 |
| 1.40 | 0.9192 | 0.9207 | 0.9222 | 0.9236 | 0.9251 | 0.9265 | 0.9279 | 0.9292 | 0.9306 | 0.9319 |
| . . . |  |  |  |  |  |  |  |  |  |  |
| 2.50 | 0.9938 | 0.9940 | 0.9941 | 0.9943 | 0.9945 | 0.9946 | 0.9948 | 0.9949 | 0.9951 | 0.9952 |
| 2.60 | 0.9953 | 0.9955 | 0.9956 | 0.9957 | 0.9959 | 0.9960 | 0.9961 | 0.9962 | 0.9963 | 0.9964 |
| 2.70 | 0.9965 | 0.9966 | 0.9967 | 0.9968 | 0.9969 | 0.9970 | 0.9971 | 0.9972 | 0.9973 | 0.9974 |
| 2.80 | 0.9974 | 0.9975 | 0.9976 | 0.9977 | 0.9977 | 0.9978 | 0.9979 | 0.9979 | 0.9980 | 0.9981 |
| 2.90 | 0.9981 | 0.9982 | 0.9982 | 0.9983 | 0.9984 | 0.9984 | 0.9985 | 0.9985 | 0.9986 | 0.9986 |
| 3.00 | 0.9987 | 0.9987 | 0.9987 | 0.9988 | 0.9988 | 0.9989 | 0.9989 | 0.9989 | 0.9990 | 0.9990 |
| 3.10 | 0.9990 | 0.9991 | 0.9991 | 0.9991 | 0.9992 | 0.9992 | 0.9992 | 0.9992 | 0.9993 | 0.9993 |

The calculated value is *closest* to:

A. 0.35%.

B. 0.62%.

C. 8.85%.

31. Which of the following statements of null and alternative hypotheses requires a two-tailed test?

A. H0: θ =θ0 versus Ha: θ ≠ θ0

B. H0: θ ≤ θ0 versus Ha: θ > θ0

C. H0: θ ≥ θ0 versus Ha: θ < θ0

32.

|  |  |  |
| --- | --- | --- |
| Population | 1 | 2 |
| Sample size | *n*1 = 5 | *n*2 = 5 |
| Sample variance |  |  |
| The samples are drawn independently and both populations are assumed to be normally distributed. | | |

Using the above data, an analyst is trying to test the null hypothesis that the population variances are equal against the alternative hypothesis that the variances are not equal at the 5% level of significance. The table of the F-Distribution is provided below.



|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Table of the F-Distribution Panel A: Critical values for right-hand tail areas equal to 0.05** | | | | | | |
|  | df1 (read across) | 1 | 2 | 3 | 4 | 5 |
| Df2 (read down) | 1 | 161 | 200 | 216 | 225 | 230 |
|  | 2 | 18.5 | 19.0 | 19.2 | 19.2 | 19.3 |
|  | 3 | 10.1 | 9.55 | 9.28 | 9.12 | 9.01 |
|  | 4 | 7.71 | 6.94 | 9.59 | 6.39 | 6.26 |
|  | 5 | 6.61 | 5.79 | 5.41 | 5.19 | 5.05 |
| **Panel B: Critical values for right-hand tail areas equal to 0.025** | | | | | | |
|  | df1 (read across) | 1 | 2 | 3 | 4 | 5 |
| Df2 (read down) | 1 | 648 | 799 | 864 | 900 | 922 |
|  | 2 | 38.51 | 39.00 | 39.17 | 39.25 | 39.03 |
|  | 3 | 17.44 | 16.04 | 15.44 | 15.10 | 14.88 |
|  | 4 | 12.22 | 10.65 | 9.98 | 9.60 | 9.36 |
|  | 5 | 10.01 | 8.43 | 7.76 | 7.39 | 7.15 |

Which of the following statements is *most appropriate*? The critical value is:

A. 6.39 and reject the null.

B. 7.15 and accept the null.

C. 9.60 and accept the null.

**Study Session 4, 5, 6 – Economics (33-44) Q=12**

33. A college student's monthly demand for pizza is given by the equation:

|  |  |
| --- | --- |
| QDPizza = 11 – 0.70 PPizza + 0.009 I – 0.20 PCola | |
| where | QDPizza is the number of pizzas ordered per month |
| PPizza is the price of a pizza |
| I is her monthly food budget |
| PCola is the price of cola per bottle |

The student's current monthly food budget is $500, the price of a pizza is $5, and the price of a bottle of cola is $1.25/bottle. If the student's monthly food budget were to increase to $700, the slope of her demand curve for pizza would be closest to:

A. –2.42.

B. –1.43.

C. –0.70.

34. Partial information on three baskets (1, 2, and 3) containing goods A and B is given in the table below. The marginal rate of substitution of B for A, (MRSBA), at basket 2 is also provided.

|  |  |  |  |
| --- | --- | --- | --- |
| **Basket** | **Units of A** | **Units of B** | **MRSBA** |
| 1 |  | 30 |  |
| 2 | 50 | 35 | 4.0 |
| 3 | 40 | 40 |  |

A consumer claims that he is indifferent between baskets 2 and 3 and his indifference curves are strictly convex. If he is also indifferent between baskets 1 and 3, the number of units of A in basket 1 is most likely:

A. equal to 60.

B. less than 60.

C. greater than 60.

35. Three firms operate under perfect competition, producing 900 units of the same product but using different production technologies. Each company's cost structure is indicated below:

|  |  |  |  |
| --- | --- | --- | --- |
| **Company** | **X** | **Y** | **Z** |
| **Total Variable Costs** | $2,700 | $3,600 | $4,500 |
| **Total Fixed Costs** | 2,700 | 1,800 | 900 |
| **Total Costs** | $5,400 | $5,400 | $5,400 |

Which of the following statements is most accurate? If the unit selling price is:

A. $6.00, all firms should exit the market in the long run.

B. $3.00, firm X should continue to operate in the short run, but firms Y and Z should shut down production.

C. $4.50, all firms should continue to operate in the short run, but exit the market in the long run if these conditions are expected to persist.

36. The total output in units and average selling prices in a hypothetical economy producing only two products, X and Y, is provided below:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Product X** | | **Product Y** | |
| **Year** | **Output (units)** | **Selling Price/unit** | **Output (units)** | **Selling Price/unit** |
| 2010 | 2,800 | €9 | 2,000 | €47 |
| 2011 | 3,000 | €11 | 1,800 | €52 |

If the implicit price deflator for GDP in 2010 was 100, for 2011 it is closest to:

A. 106.2.

B. 106.8.

C. 113.4.

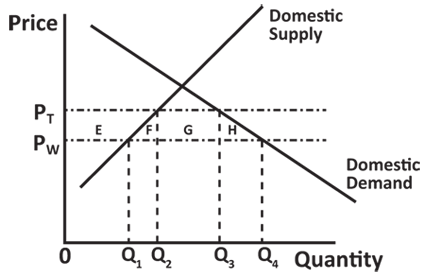
37. In an economy, consumption is 70% of pre-tax income and the average tax rate is 25% of total income. If planned government expenditures are expected to increase by $1.25 billion, the increase in total incomes and spending, in billions, is *closest* to:

A. $1.3.

B. $2.6.

C. $4.2.

38.



The above diagram shows the domestic demand and supply curves for a country that imports a commodity, where PW is its world price and PT is its domestic price after the imposition of a tariff. The reduction in the net national welfare of this country as a result of the tariff is best described by the area(s):

A. E.

B. G.

C. F + H.

39. The market demand function for item X is a function of its price, household income, and the price of item Y.

|  |  |
| --- | --- |
| Own-price elasticity of demand for X | –0.8 |
| Income elasticity of demand for X | 1.5 |
| Cross-price elasticity of demand for X with respect to the price of Y | 0.4 |

Given the above elasticity coefficients for the two items, which of the following statements is *most accurate*?

A. X and Y are substitutes.

B. Demand for X is elastic.

C. Item X is an inferior good.

40. The monthly demand curve for playing tennis at a particular club is given by the following equation: PTennis Match = 9 – 0.20 x QTennis Match. The club currently charges members $4.00 to play a match, but is considering a new flat rate monthly membership fee for unlimited play. The most fee that the club will be able to charge for this membership is *closest* to:

A. $40.00.

B. $62.50.

C. $162.50.

41. With its existing production facilities, a monopolist firm can produce up to 100 units. It faces the following demand and cost schedules:

|  |  |  |
| --- | --- | --- |
| **Output (units)** | **Price ($/unit)** | **Total Cost ($/unit)** |
| 0 | 3,000 | 600 |
| 20 | 2,800 | 10,600 |
| 40 | 2,600 | 32,600 |
| 60 | 2,400 | 66,600 |
| 80 | 2,200 | 112,600 |
| 100 | 2,000 | 170,600 |

The optimal output level for this producer (in units) is *closest* to:

A. 20.

B. 60.

C. 100.

42. The following information has been gathered for a hypothetical economy:

|  |  |
| --- | --- |
| Total Population | 1,100 |
| Working Age Population | 975 |
| Labor Force | 750 |
| Underemployed | 120 |
| Unemployed | 95 |
| Discouraged Workers | 80 |
| Frictionally Unemployed | 25 |
| Voluntarily Unemployed | 40 |

The unemployment rate is *closest* to:

A. 9.7%.

B. 12.6%.

C. 16.0%.

43 Which of the following would be *most* useful as a leading indicator to signal the start of an economic recovery?.

A. An increase in aggregate real personal incomes (less transfer payments).

B. A decrease in average weekly initial claims for unemployment insurance.

C. The narrowing of the spread between the 10-year Treasury yield and the federal funds rate.

44. In early 2011, the British pound (GBP) to New Zealand dollar (NZD) spot exchange rate was 2.0979. The LIBOR interest rates, quoted on a 360-day year basis, were 1.6025% for the British pound and 3.2875% for the New Zealand dollar. The 180-day forward points (scaled up by four decimal places) in GBP/NZD would be *closest* to:

A. –343.

B. –173.

C. 176.

**Study Session 7, 8, 9, 10 – Financial Reporting and Analysis (45-68) Q=24**

45. Information about management compensation and any potential conflicts of interest that may exist between management and shareholders is most likely found in the:

A. proxy statement.

B. notes to the financial statements.

C. management discussion and analysis.

46. The following information is available about a company:

|  |  |
| --- | --- |
| Contributed capital, beginning of the year | $  50,000 |
| Retained earnings, beginning of the year | 225,000 |
| Sales revenues earned during the year | 450,000 |
| Investment income earned during the year | 5,000 |
| Expenses paid during the year | 402,000 |
| Dividends paid during the year | 10,000 |
| Total assets, end of the year | 800,000 |

Total liabilities at the end of the year are closest to:

A. $472,000.

B. $482,000.

C. $487,000.

47. According to the International Accounting Standards Board's Conceptual Framework for Financial Reporting, the two fundamental qualitative characteristics that make financial information useful are best described as:

A. timeliness and accrual accounting.

B. understandability and verifiability.

C. relevance and faithful representation.

48. The following information is available from a company's accounting records:

|  |  |
| --- | --- |
|  | **€millions** |
| Revenues for the year | 12,500 |
| Total expenses for the year | 10,000 |
| Gains from available-for-sale securities | 1,475 |
| Loss on foreign currency translation adjustments on a foreign subsidiary | 325 |
| Dividends paid | 500 |

The company's total comprehensive income (in millions) is closest to:

A. €1,150.

B. €3,150

C. €3,650

**49.**

|  |  |  |
| --- | --- | --- |
| **£ millions** | **2011** | **2010** |
| Accounts receivables, gross | 6,620 | 4,840 |
| Allowance for doubtful accounts | 92 | 56 |
| Write-offs during the year | 84 | 42 |

Based on the above information about a company, the bad debt expense (in millions) for 2011 is closest to:

A. £36.

B. £84.

C. £120.

50. An analyst has gathered the following information about a company:

|  |  |
| --- | --- |
|  | Cdn $ millions |
| Cash flow from operating activities | 105.9 |
| Cash flow from investing activities | (11.8) |
| Cash flow from financing activities | 46.5 |
| Net change in cash for the year | 140.6 |
| Interest paid (included in CFO) | 22.4 |
| Taxes paid (tax rate of 30%) | 18.0 |
| Total debt, end of year | 512.8 |

The cash flow debt coverage ratio for the year is *closest* to:

1. 20.6%.
2. 23.7%.
3. 27.4%

51. Which inventory method best matches the actual historical cost of the inventory sold with their physical flow if a company is using a perpetual inventory system?

A. FIFO.

B. LIFO.

C. Specific identification.

52. On 1 January, a company, which prepares its financial statements according to IFRS, arranged financing for the construction of a new plant. The company:

• borrowed NZ$5,000,000 at an interest rate of 8%,

• issued NZ$5,000,000 of preferred shares with a cumulative dividend rate of 6%, and

• during the first year of construction the company was able to temporarily invest NZ$2,000,000 of the loan proceeds for the first six months and earned 7% on that amount.

The amount of financing costs to be capitalized (NZ$) to the cost of the plant in the first year is closest to:

A. 330,000.

B. 400,000.

C. 630,000.

53. Which of the following statements most accurately describes a valuation allowance for deferred taxes? A valuation allowance is required under:

A. IFRS on revaluation of capital assets.

B. U.S. GAAP if there is doubt about whether a deferred tax asset will be recovered.

C. both IFRS and U.S. GAAP on tax differences arising from the translation of foreign operations.

54. A company had the following events related to $5 million of 10-year bonds with a coupon rate of 8% payable semi-annually on 30 June and 31 December:

• Issued on 1 January 2005, when the market rate of interest was 6%.

• Bought back in an open market transaction on 1 January 2011, when the market rate of interest was 8%.

Which of the following statements best describes the effect of the bond repurchase on the financial statements for 2011? If the company uses the indirect method of calculating the cash from operations, there will be a:

A. $346,511 gain on the income statement.

B. $743,873 gain on the income statement.

C. $350,984 decrease in the cash from operations.

55. On a cash flow statement prepared using the indirect method, which of the following would most likely increase the cash from investing activities?

A. Sale of a long-term receivable.

B. Sale of held-for-trading securities.

C. Securitization of accounts receivable.

56. If a company chooses to capitalize an expenditure related to capital assets instead of expensing it, ignoring taxes, the company will most likely report:

A. a lower cash flow per share in that period.

B. a higher earnings per share in future periods.

C. the same free cash flow to the firm in that period.

57. An accounting document that records transactions in the order in which they occur is *best* described as a:

A. trial balance.

B. general ledger.

C. general journal.

58. Which of the following statements is *most accurate* with respect to financial reporting requirements?

A. Regulatory authorities are typically private sector, self-regulated organizations.

B. Standard-setting bodies have authority because they are recognized by regulatory agencies.

C. The requirement to prepare financial reports in accordance with specified accounting standards is the responsibility of standard-setting bodies.

59. Income statements for two companies (A and B) and the common-sized income statement for the industry are provided below:

|  |  |  |  |
| --- | --- | --- | --- |
| **All $ figures in '000s** | **Company A** | **Company B** | **Industry** |
| Sales | $10,500 | $8,250 | 100.0% |
| Cost of goods sold | 6,353 | 5,239 | 62.8% |
| Selling, general, and administrative expenses | 2,625 | 2,021 | 24.8% |
| Interest expense | 840 | 536 | 7.0% |
| Pretax earnings | 683 | 454 | 5.4% |
| Taxes | 205 | 145 | 1.7% |
| Net earnings | $    478 | $  309 | 3.7% |

The *best* conclusion an analyst can make is:

A. Company B's interest rate is lower than the industry average.

B. both companies' tax rates are higher than the industry average.

C. Company A earns a higher gross margin than both Company B and the industry.

60. Which of the following statements about balance sheets is *most accurate*? Under:

A. U.S. GAAP, intangibles must be valued at historical cost.

B. IFRS, a commercial real estate company should use a liquidity based presentation.

C. IFRS, a classified balance sheet must present current assets before non-current assets.

61. A company recorded the following events in 2010:

|  |  |
| --- | --- |
|  | $'000s |
| Purchase of securities for trading purposes | 240 |
| Proceeds from the sale of trading securities | 300 |
| Proceeds from issuance of bonds | 500 |
| Purchase of 30% of the shares of an affiliated company | 275 |

On the 2010 statement of cash flows, the company's cash flow from investing activities (in '000s) is *closest* to:

A. –$275.

B. –$215.

C. $285.

62. Selected information for a company is provided below.

|  |  |
| --- | --- |
|  | **$ millions** |
| Sales | 4,800 |
| Cost of goods sold | 2,880 |
| Purchases | 2,940 |
| Average receivables | 625 |
| Average inventory | 710 |
| Average payables | 145 |

The company's cash conversion cycle (in days) is *closest* to:

A. 84.

B. 120.

C. 138.

63. Select information from a company that uses FIFO inventory method is provided below.

|  |  |  |  |
| --- | --- | --- | --- |
| **Event** | **Units** | **$/Unit** | **Total ($)** |
| Opening inventory | 1,000 | 7.50 | 7,500 |
| Purchases | 250 | 7.60 | 1,900 |
| Sales | 550 | 12.00 | 6,600 |
| Purchases | 300 | 7.70 | 2,310 |
| Sales | 600 | 12.00 | 7,200 |
| Ending Inventory | 400 |  |  |

If the company uses the perpetual inventory system versus the periodic inventory system, the gross margin would *most likely* be:

A. lower.

B. higher.

C. the same.

64. A company, which prepares its financial statements according to IFRS, owns several investment properties on which it earns rental income. It values the properties using the fair value model based on prevailing rental markets. A summary of the properties' valuations is as follows:

|  |  |
| --- | --- |
| • Original cost (acquired in 2009) • Fair value valuation as at 31 December 2009 • Fair value valuation as at 31 December 2010 • Fair value valuation as at 31 December 2011 | €50 million €50.5 million €54.5 million €48.0 million |

Which of the following *best* describes the impact of the revaluation on the 2011 financial statements?

A. €6.5 million charge to net income.

B. €6.5 million charge to revaluation surplus.

C. €4.5 million charge to revaluation surplus and €2.0 million charge to net income.

65. A company purchased equipment in 2009 for £25,000; the year-end values for accounting purposes and tax purposes are as follows:

|  |  |  |
| --- | --- | --- |
|  | **2010** | **2009** |
| Carrying amount for accounting purposes | £20,000 | £22,500 |
| Tax base for tax purposes | £16,000 | £20,000 |
| Tax rate | 25% | 30% |

Which of the following statements *best* describes the effect of the change in the tax rate on the company's 2010 financial statements? The deferred tax liability:

A. increased by £250.

B. decreased by £200.

C. decreased by £800.

66. An analyst can *most accurately* identify a LIFO liquidation by observing a(n):

A. increase in gross margin.

B. decrease in the LIFO reserve.

C. change in inventory out of line with change in sales.

67. Selected information about a company is as follows:

|  |  |  |
| --- | --- | --- |
| **($ '000)** | **2010 31 December** | **2011 Projection** |
| Sales | 2,200 | 2,500 |
| Variable operating costs (% of sales) | 28% | 30% |
| Fixed operating costs | 1,400 | 1,400 |
| Tax rate | 25% | 25% |
| Dividends paid | 55 | 60 |
| Interest bearing debt at 5% | 500 | 500 |

The forecasted net income (in '000s) for 2011 is *closest* to:

A. $169.

B. $202.

C. $244.

68. An analyst has gathered the following information about a company's capital assets:

|  |  |  |
| --- | --- | --- |
| **Year ending** | **2011** | **2010** |
| **Property plant and equipment** | €2,500 | €2,500 |
| **Accumulated depreciation** | 375 | 250 |
| **Net book value** | 2,125 | 2,250 |

As at the end of 2011, the expected remaining life of the assets, in years, is *closest* to:

A. 6.

B. 17.

C. 20.

**Study Session 11 – Corporate Finance (69-78) Q=10**

69. Two mutually exclusive projects have the following cash flows (€) and internal rates of return (IRR):

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Project** | **IRR:** | **Year 0** | **Year 1** | **Year 2** | **Year 3** | **Year 4** |
| **Project A** | 27.97% | –2,450 | 345 | 849 | 635 | 3,645 |
| **Project B** | 28.3% | –2,450 | 345 | 849 | 1,051 | 3,175 |

Assuming a discount rate of 8% annually for both projects, the firm most likely should accept:

A. both projects.

B. Project A only.

C. Project B only.

70. A company's asset beta is 1.2 based on a debt-to-equity ratio of 50%. If the company's tax rate increases, the associated equity beta will most likely:

A. increase.

B. decrease.

C. remain unchanged.

71. A firm's price-to-earnings ratio (P/E) is 12.5. The firm has decided to repurchase shares using external funds that have an after-tax cost of 9%. After the repurchase, the earnings per share (EPS) will most likely:

A. increase.

B. decrease.

C. remain unchanged.

72. Which is most likely considered a "pull" on liquidity?

A. Obsolete inventory.

B. Reduction in a line of credit.

C. Increased difficulty in collecting receivables.

73. Based on best practices in corporate governance procedures, independent board members most likely:

A. meet only in the presence of management.

B. have a "lead" director when the board chair is not independent.

C. hire independent consultants who are pre-approved by management.

74. Given the following information about a firm:

* debt-to-equity ratio of 50%
* tax rate of 40%
* cost of debt of 8%
* cost of equity of 13%,

the firm's weighted average cost of capital (WACC) is *closest* to:

A. 7.5%.

B. 8.9%.

C. 10.3%.

75. The unit contribution margin for a product is $20 and the firm's fixed costs of production up to 300,000 units is $500,000. The degree of operating leverage (DOL) is *most likely* the lowest at which of the following production levels (in units)?

A. 100,000.

B. 200,000.

C. 300,000.

76. Which date in the chronology of a dividend payment is *most likely* determined by a security exchange? The:

A. declaration date.

B. ex-dividend date.

C. holder-of-record date.

77. Which of the following share repurchase methods will *most likely* take the longest amount of time to execute?

A. Dutch auction.

B. fixed price tender offer.

C. open market repurchase.

78. Assuming a 365-day year and the following information for a company:

|  |  |  |
| --- | --- | --- |
|  | **Current Year** | **Previous Year** |
| Sales | $12,000 | $10,000 |
| Cost of goods sold | $6,000 | $5,000 |
| Inventory | $1,200 | $1,000 |
| Accounts payable | $600 | $500 |

The firm's days in payables for the current year is *closest* to:

A. 18.3.

B. 35.3.

C. 36.5.

**Study Session 13, 14 – Equity Investments (79-90) Q=12**

79. Which of the following statements concerning regulatory bodies is least accurate? Regulatory bodies:

A. act to level the playing field for market participants.

B. help define minimum standards of practice for agents.

C. require that regulated firms maintain optimum levels of capital.

80. Which of the following statements is most accurate?

A. Investors prefer to invest in callable common shares rather than putable common shares.

B. The issuing company is obligated to buy callable common shares at a predetermined price.

C. Putable common shares facilitate raising capital because of their appeal to investors over callable common shares.

81. An investor who wants to estimate the enterprise value multiple (EV/EBITDA) of a company has gathered the following data:

|  |  |
| --- | --- |
| Market value of debt | $10 million |
| Market capitalization | $45 million |
| Cash and short-term investments | $2.5 million |
| EBITDA | $15 million |
| Firm's marginal tax rate | 40% |

The company's EV/EBITDA multiple is closest to:

A. 2.5.

B. 3.5.

C. 5.8.

82. An investor gathers the following data to estimate the intrinsic value of a company's stock using the justified forward P/E approach.

|  |  |
| --- | --- |
| Next year's earnings per share | $3.00 |
| Return on equity | 12.5% |
| Dividend payout ratio | 60% |
| Required return on shares | 10% |

The intrinsic value per share is closest to:

A. $36.

B. $48.

C. $72.

83. A company's series B, 8% preferred stock with a par value of $50 pays quarterly dividends. Its current market value is $35. The shares are retractable (at par) with the retraction date set for three years from today. Similarly rated preferred issues have an estimated nominal required rate of return of 12%. Analysts expect a sustainable growth rate of 4% for the company's earnings. The intrinsic value estimate of a share of this preferred issue is closest to:

A. $33.33.

B. $45.02.

C. $52.00.

84. Which of the following multiples is most useful when comparing companies with significant differences in capital structure?

A. EV/EBITDA.

B. Price-to-book ratio.

C. Price-to-cash flow ratio.

85. If a stock's intrinsic value is less than its current market price, the *most appropriate* strategy an active investor can adopt is to:

A. sell the stock short.

B. buy the stock on margin.

C. buy a call option on the stock.

86. An analyst finds that a company she is following has initiated the process of selling unproductive land representing 5% of its total assets and using the proceeds to buy back its common shares. Holding other factors constant, these actions by the company will *most likely* result in a:

A. higher return on equity.

B. higher operating margin.

C. lower sustainable growth.

87. Which of the following is the *most appropriate* reason for using a free-cash-flow-to-equity (FCFE) model to value equity of a company?

A. FCFE is a measure of the firm's dividend-paying capacity.

B. FCFE models provide more accurate valuations than the dividend discount models.

C. A firm's borrowing activities could influence dividend decisions but they would not impact FCFE.

88. The following information is available about a company:

|  |  |
| --- | --- |
| Next year's sales revenue | $180 million |
| Next year's net profit margin | 15% |
| Dividend payout ratio | 60% |
| Dividend growth rate expected during Years 2 and 3 | 25% |
| Dividend growth rate expected after Year 3 | 5% |
| Investors' required rate of return | 12% |
| Number of outstanding shares | 8.1 million |

The current value per share of the company's common stock according to the two-stage dividend discount model is *closest* to:

A. $39.36.

B. $49.20.

C. $51.20.

89. A trader buys 500 shares of a stock on margin at $36 a share using an initial leverage ratio of 1.66. The maintenance margin requirement for the position is 30%. The stock price at which the margin call occurs is *closest* to:

A. $20.57.

B. $25.20.

C. $30.86.

90. Which of the following inferences concerning market efficiency is *most accurate*?

A. Fully exploitable over and under-reactions often occur in efficient markets.

B. Market pricing anomalies and behavioral biases are contrary to the existence of market efficiency.

C. If a market is semi-strong form efficient, neither technicians nor fundamental analysts can expect to consistently earn abnormal returns.

**Study Session 17 – Derivatives (91-96) Q=6**

91. A corporation issues 5-year fixed-rate bonds. Its treasurer expects interest rates to decline for all maturities for at least the next year. She enters into a 1-year agreement with a bank to receive quarterly fixed-rate payments and to make payments based on floating rates benchmarked on 3-month LIBOR. This agreement is best described as a:

A. swap.

B. futures contract.

C. forward contract.

92. A portfolio manager is required to sell 31,250 shares of XYZ Inc. in two months. She is concerned that the price of XYZ will decline during the 2-month period, so she enters into a deliverable equity forward contract to sell 31,250 shares of XYZ in 2 months for EUR 160 per share. When the contract expires, XYZ is trading at EUR 138 per share. The portfolio manager will most likely:

A. pay EUR 687,500 to the dealer.

B. receive EUR 4,312,500 from the dealer.

C. receive EUR 5,000,000 from the dealer.

93. A trader takes a long position in 40 futures contracts on Day 1. The futures have a price limit of $5 and settle at $106. On Day 2, the futures trade at $111 and the bid and offer move to $113 and $115, respectively. The futures remain at these price levels until the market closes. What marked-to-market value does the trader receive in his account for Day 2?

A. $200.

B. $280.

C. $320.

94. An investor is long an in-the-money American call option. Would this option *most likely* ever be exercised early?

A. No.

B. Yes, if its time value is high enough.

C. Yes, if it pays a high enough dividend.

95. A European company issues a 5-year euro-denominated bond with a face value of EUR 50,000,000. The company then enters into a 5-year currency swap with a bank to convert the EUR exposure into US$ exposure. The notional principals of the swap are EUR 50,000,000 and US$70,000,000. The European company pays a fixed rate of 5% and the bank pays a fixed rate of 4.5%. Payments are made semiannually on a basis of 30 days per month and 360 days per year. What is the payment from the bank to the company at the end of year 4?

A. US$ 1,750,000.

B. EUR 1,125,000.

C. EUR 1,250,000.

96. An investor with $5000 to invest believes that the price of ABC Corp. stock will appreciate by $7 to $95 in two months. Two-month at-the-money puts on one share of ABC stock are trading at $1.76, while two-month at-the-money calls are trading at $1.56. What action will he *most likely* take to profit from his view on ABC stock?

A. Sell 100 ABC puts.

B. Buy 100 ABC calls.

C. Buy 100 ABC shares.

**Study Session 18 – Alternative Investments (97-102) Q=6**

97. U.S. farmers become concerned that the future supply of wheat production would exceed demand. Their hedging activities would most likely drive which market condition?

A. Contango.

B. Full carry.

C. Backwardation.

98. An apartment building currently being marketed has the following financial characteristics:

|  |  |
| --- | --- |
|  | **Annual Figures** |
| Gross potential rental income | $625,000 |
| Estimated vacancy and collection losses | 3.75% |
| Insurance and taxes | $65,000 |
| Utilities | $27,000 |
| Repairs and maintenance | $62,000 |
| Depreciation | $55,000 |
| Interest rate on proposed financing | 6.5% |
| Average market cap rate | 8.5% |

The estimated value for the building being sold using the income approach is closest to:

A. $5,265,400.

B. $5,541,200.

C. $6,400,000.

99. An investor contributes £2,500,000 to a new venture capital project that is expected to earn £7,500,000 at the end of year 5 if it is successful. The probabilities of failure for the project are provided in the table below:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Year:** | **1** | **2** | **3** | **4** | **5** |
| **Failure Probability:** | 0.35 | 0.20 | 0.15 | 0.15 | 0.15 |

If the cost of capital for the JV is 12%, the project's expected NPV is closest to:

A. –£560,674.

B. –£1,140,964.

C. £1,701,638.

100. An investor is evaluating the purchase of a mutual fund that offers three classes of shares. Fees for each class are provided in the table below:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Class A | Class B | Class C |
| Annual fees | 1.00% | 1.25% | 1.25% |
| Front-end load | 2.75% | None | None |
| Back-end load | None | 4% year 1, 1% annually after | 1.50% initial 5 years |

Given a time horizon of three years, which class is *most likely* to result in the lowest fees for the investor?

A. Class A.

B. Class B.

C. Class C.

101. In estimating the value of inactively traded securities of a closely held corporation, which of the following statements is *least likely* correct?

A. A control premium values the equity from a minority shareholder perspective.

B. The cost approach assigns the original acquisition price to the company's assets.

C. Shares should reflect a marketability discount to compensate for a lack of trading in a public market.

102. When using the historical track record of hedge funds to interpret performance, which of the following is *least likely* correct?

A. Databases may have backfilling bias since only hedge fund managers with good track records agree to be included.

B. Self-selection bias is present as index providers decide whether to include a hedge fund in a performance database.

C. Survivorship bias occurs because poorly performing hedge funds no longer appear in hedge fund databases, thus inflating the reported average performance.

**Study Session 15, 16 – Fixed Income (103-114) Q=12**

103. If a bond's issuer is required to retire a specified portion of the issue each year, the bond most likely:

A. is a step-up note.

B. is currently callable.

C. has a sinking fund provision.

104. One reason why the duration of a portfolio of bonds does not properly reflect that portfolio's yield curve risk is that the duration measure:

A. assumes all yields change by the same amount.

B. assumes all the bonds have the same discount rate.

C. ignores differences in coupon rates across the bonds.

105. Investor A's marginal tax rate is 45%, while Investor B's is 30%. Both investors are considering two bonds for inclusion in a taxable portfolio. One bond is tax-exempt with a yield of 4.50%, while the other is taxable with a yield of 6.30%. Which bond will each investor most likely choose?

A. Both investors will choose the taxable bond.

B. Both investors will choose the tax-exempt bond.

C. Investor A will choose the tax-exempt bond and investor B will choose the taxable bond.

106. The yield on a U.S. Treasury STRIPS security is also known as the Treasury:

A. spot rate.

B. yield spread.

C. forward rate.

107. A 4-year amortizing security with a par value of $5,000 and a coupon rate of 7% has an expected cash flow of $1,476 per year, assuming no principal prepayments. Assuming a discount rate of 5%, the present value of this security is closest to:

A. $5,234.

B. $5,355.

C. $9,347.

108. Consider a 5-year option-free bond that is priced at a discount to par value. Assuming the discount rate does not change, one year from now the value of the bond will most likely:

A. increase.

B. decrease.

C. stay the same.

109. The value of an 18-year zero-coupon bond with a maturity value of $1,000 discounted at a 12% annual interest rate with semi-annual compounding is *closest* to:

A. $122.74.

B. $130.04.

C. $350.34.

110. A 10% coupon bond with annual payments, maturing in 3 years, is priced at 105. The bond is callable in one year at a call price of 104 or in two years at a call price of 102. The bond's yield to worst *most likely* occurs when the bond is:

A. called in year 1.

B. called in year 2.

C. held until maturity.

111. All else being the same, the difference between the nominal spread and the Z-spread for a non-Treasury security will be larger when the:

A. yield curve is flatter.

B. maturity of the security is longer.

C. security has a bullet maturity rather than an amortizing structure.

112. Assume the following six-month forward rates (presented on an annualized, bond-equivalent basis) were calculated from the yield curve.

|  |  |
| --- | --- |
| **Notation** | **Forward Rate** |
| 1*f*0 | 0.50% |
| 1*f*1 | 0.70% |
| 1*f*2 | 1.00% |
| 1*f*3 | 1.50% |
| 1*f*4 | 2.20% |
| 1*f*5 | 3.00% |
| 1*f*6 | 4.00% |

The 3-year spot rate is *closest* to:

A. 0.74%.

B. 1.48%.

C. 2.06%.

113. One advantage of the full valuation approach to measuring interest rate risk relative to the duration/convexity approach is the full valuation approach is:

A. more accurate.

B. easier to model.

C. less time-consuming.

114. An analyst uses a valuation model to estimate the value of an option-free bond at 92.733 to yield 11%. If the value estimate rises to 94.474 for a 60 basis point decrease in yield and falls to 91.041 for a 60 basis point increase in yield, the effective duration of the bond is *closest* to:

A. 1.85.

B. 3.09.

C. 6.17.

**Study Session 12 – Portfolio Management (115-120) Q=6**

115. Which of the following is least likely a part of the execution step of the portfolio management process?

A. Security analysis.

B. Portfolio construction.

C. Performance measurement.

116. The correlation between the historical returns of Stock A and Stock B is 0.75. If the variance of Stock A is 0.16 and the variance of Stock B is 0.09, the covariance of returns of Stock A and Stock B is closest to:

A. 0.01.

B. 0.09.

C. 0.16.

117. The point of tangency between the Capital Allocation Line (CAL) and the efficient frontier of risky assets most likely identifies the:

A. optimal risky portfolio.

B. optimal investor portfolio.

C. global minimum-variance portfolio.

118. The stock of GBK Corporation has a beta of 0.65. If the risk-free rate of return is 3% and the expected market return is 9%, the expected return for GBK is *closest* to:

A. 3.9%.

B. 6.9%.

C. 10.8%.

119. A return-generating model that provides an estimate of the expected return of a security based on factors such as earnings growth and cash flow generation is *best* described as a:

A. market factor model.

B. fundamental factor model.

C. macroeconomic factor model.

120. A portfolio manager earned a rate of return of 15.5%. The beta of the portfolio is 1.2. If the risk-free rate of return is 2.5% and the market return is 11.8%, Jensen's alpha for the portfolio is *closest* to:

A. 1.84%.

B. 3.70%.

C. 4.34%.