**June. 2013 CFA Level 1 Mock Examination**

**Morning Session**

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

1. Alan Quanta, CFA, provides credit rating analysis of high-yield bonds using external credit ratings as a foundation. At the end of the last quarter, Quanta's firm, North Investment Bank, held a large position in the bonds of Veyron Corporation, a real estate company with all of its land holdings in a country recently downgraded by several credit rating agencies. The downgrades made Veyron bonds extremely difficult to sell because the bond price has dropped every day since the downgrades. Quanta has been asked by his supervisor to contact institutional clients of the firm to convince them that Veyron bonds are still an attractive purchase, especially at these lower prices. Quanta does not consider the Veyron bonds a buy at this price level. According to the CFA Institute Code of Ethics and Standards of Professional Conduct, the *most appropriate* action for Quanta is to

A. obey his supervisor's request.

B. ignore his supervisor's request.

C. promote the bonds with appropriate disclosures.

2. Lewis McChord, CFA, a research analyst, covers the auto industry at an investment bank. McChord recently read a report on an auto manufacturing company written by Pierce Brown. Brown's report provided extensive coverage of the company's newly launched products indicating that sales volume, not yet publicly available, would raise future profits. Intrigued by the report, McChord called a senior executive at the company whom she has known personally for years. The officer gave her specific details on new vehicle sales, indicating that profits would double in the current quarter. McChord added this data to Brown's report and then circulated it within her firm as her own report. McChord *least likely* violated which of the following CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Misrepresentation

B. Preservation of Confidentiality

C. Material Nonpublic Information

3. Jacques Lagarde, CFA, is a sell-side analyst at Springhill Financial, a small investment bank. Springhill is the lead manager for the equity offering of Chorale Music, a guitar maker. Lagarde is not part of the IPO team for this offering. While finalizing a research report on Chorale, Lagarde discovers information that makes him believe the company concealed losses in its leasing division last quarter that would significantly reduce its earnings. Based upon this information, Lagarde adds the following statement to his report: "The factual data I have gathered indicate Chorale experienced losses in the last quarter rather than profits." Lagarde suspects Springhill's investment bankers are aware of the unreported losses. The prospectus for Chorale's equity offering has already been approved by regulators and distributed to potential investors. According to the CFA Institute Code of Ethics and Standards of Professional Conduct, Lagarde should *least likely*:

A. seek legal counsel.

B. report the issue to his supervisor.

C. keep loss data in his research report.

4. PNW Bank publishes *Investment Monthly* magazine, which highlights a specific stock in each issue. Publication of the magazine invariably causes the highlighted stocks to rise significantly in value. Rachel Coursing, CFA, manager of PNW's marketing department, often trades in the securities mentioned in the *Investment Monthly* articles prior to publication of the magazine. Coursing has access to the recommendations prior to the magazine's publication because the magazine is created in her department and edited by her. PNW's Code of Ethics restricts trading by all of the bank's analysts and portfolio managers and requires their trades to be pre-cleared by the Compliance Department. Coursing *least likely* violated which of the following CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Priority of Transactions

B. Diligence and Reasonable Basis

C. Material Nonpublic Information

5. Abe Seneca, CFA, supervises a team of analysts who create index funds for institutional investors. When Seneca provides sales demonstrations to potential clients simulating the fund's performance, the scenarios he prepares show outcomes based on assumptions reflecting upside bias and positive risk assessments. Gail Tremblay, CFA, an analyst in Seneca's group, observes that the actual performance of these index funds is less than indicated in the scenario outcomes shown in the sales meetings. Seneca least likely violated which of the following CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Loyalty

B. Performance Presentation

C. Responsibilities of Supervisors

6. Manuel Tacqueria, CFA, is a sole proprietor investment adviser managing accounts for a diversified group of clients. Tacqueria obtains his investment research through a subscription service with Alpha Services, a large financial services organization. Tacqueria notes the research reports are sound because they are extremely detailed and comprehensive. As a result, Tacqueria feels comfortable relying solely upon this research when making recommendations to clients. Tacqueria should *most likely* do which of the following to conform to the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Utilize additional sources of research.

B. Add his own research to the existing reports.

C. Conduct additional due diligence on Alpha Services.

7. Priscilla Moab, CFA, is the director of marketing at Red Lantern Investments. Red's investment approach uses technical and fundamental analysis as well as portfolio construction to minimize risk. Moab plans to market an online investment newsletter to retail clients. Moab decides to let prospective clients have access to Red's buy and sell recommendation list by posting this information on a social media site. The posting also provides information on Red's basic investment process and logic. To avoid violating the CFA Institute Code of Ethics and Standards of Professional Conduct, Moab should *most likely*:

A. describe the investment approach in detail.

B. update investment process changes annually.

C. indicate that additional information and analysis are available.

8. At the conclusion of the afternoon section of the Level I CFA examination, the exam proctor instructs all candidates to stop writing and put their pencils down immediately. Krishna Chowdary thinks he sees other candidates in front of him continue to fill in their answer sheets. Chowdary has two questions left to complete so he randomly fills in one of the ovals on his answer sheet before putting his pencil down on the table. Did Chowdary's actions *most likely* violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Yes.

B. No, because other candidates continued writing.

C. No, because he randomly answered one question.

9. A large manufacturing company is seeking help finding a fund manager for its pension plan. After a comprehensive but unsuccessful search, Brett Arun, CFA, is hired to solicit proposals from various fund managers. Arun is paid a lump sum fee for his services. The search concludes with the hiring of Ramport Investments as the pension plan's manager. A year after Ramport is hired, the pension administrator sends Arun a letter telling him how satisfied the pension trustees are with the services provided by the fund manager. Subsequently, without the plan sponsor's knowledge, Arun receives a payment from Ramport for successfully introducing it to the pension plan under an agreement entered into when the search was initiated. Regarding the payment received, did Arun *most likely* violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. No.

B. Yes, because he did not disclose the payments to all parties.

C. Yes, because he should have refused payment from the fund manager.

10.Maria Martinez is a research analyst and a Level II CFA candidate. Recently, friends of Martinez organized a party for her 30th birthday. At the party, Martinez received an inexpensive gift from a friend who is the CEO of a publicly listed company Martinez recommends to clients. Martinez also received gifts from some of the firm's *best* clients. Aware of her employer's policy requiring her to report all gifts received within one week of receipt, Martinez declares the gifts she received from the firm's clients two days after the party. Does Martinez *most likely* violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Yes.

B. No, because her CEO friend's gift was inexpensive.

C. No, because the gifts do not impact her research independence and objectivity.

11. Upon receiving notification that he passed his Level III CFA exam, Paulo Garcia updates his educational background on his social media site by adding "completed the CFA course." Does Garcia most likely violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. No.

B. Yes, because it could imply he has obtained the charter.

C. Yes, because he doesn't describe the certification process.

12. Roberto Sanchez, CFA, and Andreas Lopez, CFA, worked as financial analysts for OneWorld Analytics for years. While at OneWorld, Lopez created a highly complex financial valuation model with Sanchez making small contributions to its development. Recently, Lopez left OneWorld to start his own company using a simplified model he developed prior to joining OneWorld. Over a six-month period, he improves this software, duplicating features he used at OneWorld. His upgraded program produces predictions similar to the results of the OneWorld program. At OneWorld, Sanchez continues to use the complex model he and Lopez developed and attains superior results. Whose behavior *most likely* conforms to the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Lopez but not Sanchez

B. Sanchez but not Lopez

C. Both Lopez and Sanchez

13. Ricardo Torres, CFA, is a well-respected telecommunications analyst for Pegasus Advisors. He is known for his thorough analysis, including interviews with suppliers, customers, and competitors. Torres has a strong following, and his research reports can often materially move the market. As a result, Pegasus limits the distribution of his reports to Pegasus clients. After losing market share to Pegasus for over two years, Marco Rodrigo, a CFA candidate, reports Torres to the local securities regulator on suspicion of using insider information to make share recommendations. What CFA Institute Standard has Rodrigo *most likely* violated?

A. Misconduct

B. Market Manipulation

C. Material Nonpublic Information

14. Alexandra Smirnov, CFA, is a pension consultant to the Springwell Pension Fund. After reviewing Springwell's three-year performance presentation showing the fund's underperformance relative to its investment objectives and agreed benchmarks, Smirnov recommends the fund hire new asset managers. Smirnov proposes the fund hire Newday Managers on the basis of recent meetings she has had with the firm. Lengthy discussions at these meetings included Newday's investment strategy, its suitability to manage pension funds, its ability to adhere to its stated strategy, the firm's historical investment performance, and its adoption of the CFA Institute Code of Ethics and Standards of Professional Conduct. Smirnov turned down Newday's offer of an introduction fee when recommending its services but did not inform Springwell trustees of this offer. Which of the following CFA Institute Standards does Smirnov *most likely* violate?

A. Referral Fees

B. Loyalty, Prudence, and Care

C. Diligence and Reasonable Basis

15. Dimitri Kuznetsov, CFA, is a portfolio manager and holds shares of Barnikoff Limited and Matric Ventures in all client portfolios. Both companies have upcoming annual general meetings scheduled for the same day. The management of Barnikoff proposes to change its financial year-end from September to December, while Matric Ventures proposes to enter into a high-risk venture. The proxy voting policy clause in all client investment management agreements managed by Kuznetsov states, "When voting proxies provides a cost benefit to the client, the manager must vote a proxy." Regarding the proxy votes for Matric and Barnikoff, Kuznetsov would *least likely* violate CFA Institute Standard III (A) Loyalty, Prudence, and Care if he votes:

A. with management.

B. only the Matric proxy.

C. only the Barnikoff proxy.

16. Merchant Capital Partners, a regional investment bank, acts as a market maker for Vital Link Health Services and other small firms listed on an over-the-counter exchange. For those shares Merchant acts as market maker, it trades for its own book, as well as engaging in risk arbitrage trading. Merchant allows staff members to trade in shares once clients and the company have traded. Merchant recently obtained material nonpublic information regarding Vital's planned reverse takeover of a publicly listed competitor. In order to be in compliance with the CFA Institute Code of Ethics and Standards of Professional Conduct, which type of trading in Vital shares should Merchant *least likely* suspend?

A. Personal

B. Risk arbitrage

C. Passive proprietary

17. Gregor Pavlov, CFA, is a fund manager working for the general partner of a new private equity fund. Pavlov includes in the fund marketing material his performance history from his previous employer. He received permission from his former employer to take his historical return figures and the supporting research reports he used to make the related investment decisions. Did Pavlov *most likely* violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. No.

B. Yes, regarding Loyalty.

C. Yes, regarding Record Retention.

18. Anna Saar, CFA, is the head of compliance for Tranne Advisory Services, a regional financial services group including asset management, investment banking, and stock brokerage entities. Reviewing a draft client investment management agreement for the asset management unit, she is concerned the relationships between the firm's various business units are not properly disclosed. To prevent violating CFA Institute Standard VI (A) Disclosure of Conflicts, which of the following should *least likely* be addressed in the investment management agreement?

A. The group subsidizes staff loans for share purchases.

B. Management fees are frequently loss leaders for brokerage.

C. Asset managers are likely to support corporate finance deals.

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

19. Monte Carlo simulation is best described as:

A. an approach to back testing data.

B. a restrictive form of scenario analysis.

C. providing a distribution of possible solutions to complex functions.

20. Use of a nonparametric test is most appropriate when the:

A. data are given in ranks.

B. distribution is symmetric.

C. population variance is unknown.

21. An analyst applies four valuation screens to a set of potential investments. Assume the screens are independent of one another.

|  |  |
| --- | --- |
| Valuation Screen | Probability of  Passing |
| 1 | 0.65 |
| 2 | 0.45 |
| 3 | 0.40 |
| 4 | 0.30 |

If there are 1,200 potential investments, the number expected to simultaneously pass all four screens is closest to:

A. 42.

B. 97.

C. 360.

22. Consider the following information:

|  |  |
| --- | --- |
| Point estimate of the population mean | 12.5 |
| t-statistic (tα/2) used in calculating the 90% confidence interval | 1.67 |
| Sample size | 64 |
| Sample standard deviation | 5 |

The 90% confidence interval is closest to:

A. 11.46 to 13.54.

B. 11.98 to 13.02.

C. 12.36 to 12.63.

23. A variable is normally distributed with a mean of 2.00 and a variance of 16.00. Calculate the probability of observing a value of 7.40 or less. That is, calculate P(Xi ≦ 7.40) given that X is distributed as N(2, 16). 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

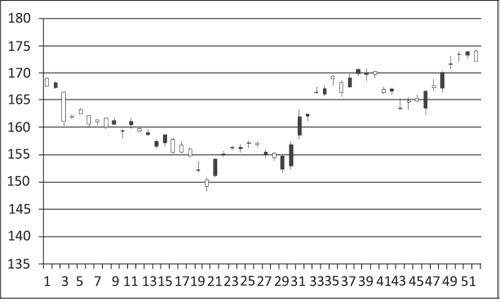
|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| x or z | 0 | 0.01 | 0.02 | 0.03 | 0.04 | 0.05 | 0.06 | 0.07 | 0.08 | 0.09 |
| 0.10 | 0.5398 | 0.5438 | 0.5478 | 0.5517 | 0.5557 | 0.5596 | 0.5636 | 0.5675 | 0.5714 | 0.5753 |
| 0.20 | 0.5793 | 0.5832 | 0.5871 | 0.5910 | 0.5948 | 0.5987 | 0.6026 | 0.6064 | 0.6103 | 0.6141 |
| 0.30 | 0.6179 | 0.6217 | 0.6255 | 0.6293 | 0.6331 | 0.6368 | 0.6406 | 0.6443 | 0.6480 | 0.6517 |
| 0.40 | 0.6554 | 0.6591 | 0.6628 | 0.6664 | 0.6700 | 0.6736 | 0.6772 | 0.6808 | 0.6844 | 0.6879 |
| … |  |  |  |  |  |  |  |  |  |  |
| 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 |
| … |  |  |  |  |  |  |  |  |  |  |
| 1.80 | 0.9641 | 0.9649 | 0.9656 | 0.9664 | 0.9671 | 0.9678 | 0.9686 | 0.9693 | 0.9699 | 0.9706 |
| 1.90 | 0.9713 | 0.9719 | 0.9726 | 0.9732 | 0.9738 | 0.9744 | 0.9750 | 0.9756 | 0.9761 | 0.9767 |
| 2.00 | 0.9772 | 0.9778 | 0.9783 | 0.9788 | 0.9793 | 0.9798 | 0.9803 | 0.9808 | 0.9812 | 0.9817 |
| 2.10 | 0.9821 | 0.9826 | 0.9830 | 0.9834 | 0.9838 | 0.9842 | 0.9846 | 0.9850 | 0.9854 | 0.9857 |

The probability of observing a value of 7.40 or less is closest to:

A. 63.31%.

B. 91.15%.

C. 96.78%.

24. The following chart is best described as an example of which type of technical analysis chart?   


A. A line chart

B. A candlestick chart

C. A point and figure chart

25. A portfolio provides the following returns over a five-year period.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Year | 1 | 2 | 3 | 4 | 5 |
| Return | 10% | –25% | 8% | 5% | 7% |

The compound rate of return (%) of the portfolio across the five-year period is closest to:

A. –9.31.

B. 0.02.

C. 1.00.

26. If the probability for an event "Z" is 14% (i.e., P(Z) = 14%), the odds for Z are closest to:

A. 7.1%.

B. 12.3%.

C. 16.3%.

27. Based on historical returns, a portfolio has a Sharpe ratio of 2.0. If the mean return to the portfolio is 20% and the mean return to a risk-free asset is 4%, the standard deviation of return on the portfolio is closest to:

A. 8%.

B. 10%.

C. 12%.

28. The following 10 observations represent a sample drawn from an approximately normal population:

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Observation | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
| Value | –31 | –14 | 3 | –18 | 34 | 20 | –6 | 9 | 7 | –16 |
|  |  |  |  |  |  |  |  |  |  |  |

The sample standard deviation is closest to:

A. 17.56.

B. 18.58.

C. 19.59.

29. Once an investor chooses a particular course of action, the value forgone from alternative actions is best described as:

A. sunk cost.

B. required return.

C. opportunity cost.

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

|  |  |  |
| --- | --- | --- |
| Time = 0 | Time = 1 | Time = 2 |
| S0 = 40 | Su = 44 | Suu = 48.40 |
|  | Sd = 36 | Sud,du = 39.60 |
|  |  | Sdd = 32.40 |

The initial value of the stock is $40. The probability of an up move in any given period is 65%, and the probability of a down move in any given period is 35%. Using the binomial model, the probability that the stock's price will be $39.60 at the end of two periods is closest to:

A. 22.75%.

B. 42.25%.

C. 45.50%.

31. Given a discount rate of 10%, the net present value (NPV) of the following investment cash flows is closest to:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| Time | 0 | 1 | 2 | 3 | 4 | 5 | 6 |
| Cash flow (€) | –1,500 | 300 | 600 | 1,000 | 200 | 500 | 300 |

A. €578.

B. €605.

C. €636.

32. Investors should most likely be attracted to return distributions that are:

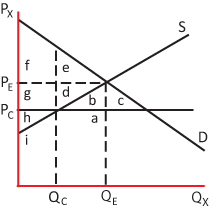
A. normal.

B. positively skewed.

C. negatively skewed.

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

33. The diagram to the right illustrates a market that had been in equilibrium at (PE, QE) prior to the imposition of a price ceiling, PC The deadweight loss that arises because of this market intervention is best described by the area defined by:



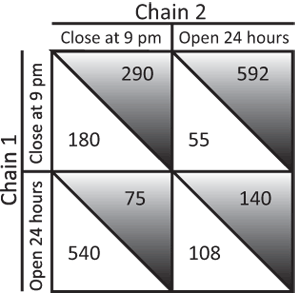
A. d + b.

B. d + e.

C. d + g.

34. The two dominant supermarket chains in the area are attempting to increase their market share by moving to 24-hour service instead of closing at 9 p.m. every night. The strategic outcomes and payoff matrix that arise from their actions are depicted in the diagram to the right (with the shaded sections representing payoffs for Chain 2).

According to a Nash equilibrium, the best strategy is for:



A. both chains to close at 9 p.m.

B. both chains to open for 24 hours.

C. only Chain 2 to open for 24 hours.

35. Which of the following will most likely cause the short-run aggregate supply (SRAS) curve to shift to the right? An increase in:

A. business taxes.

B. nominal wages.

C. the supply of human capital.

36. The most recent economic data release indicates the following:

* Capital spending is expanding rapidly but the growth rate of spending has begun to slow down and
* The rate of hiring has slowed but the unemployment rate continues to fall.

The economy is most likely in which of the following phases?

A. Peak

B. Contraction

C. Late expansion

37. A country's international transactions accounts data for last year are presented below in its domestic currency:

|  |  |
| --- | --- |
| Transaction | Amount |
| Exports of goods and services | 10,000 |
| Imports of goods and services | 14,216 |
| Investment income payments made to foreigners | 2,519 |
| Investment income received from foreigners | 3,409 |
| Net change in assets owned abroad | 1,548 |
| Net change in foreign-owned assets domestically | 4,989 |
| Unilateral current transfers received | 346 |
| Unilateral current transfers paid | 1,107 |
| Statistical discrepancy | 646 |

The current account balance is closest to:

A. –4,345.

B. –4,216.

C. –4,087.

38. The following information is available for 2011:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | New Zealand | | Canada | |
|  | Jan 1 | Dec 31 | Jan 1 | Dec 31 |
| Price index | 1,137 | 1,158 | 117.8 | 119.9 |
| Nominal exchange rate: NZD/CAD | 1.2844 |  | | 1.2589 |

The change in the real exchange rate (in NZD/CAD terms) is closest to:

A. –2.05%.

B. –1.92%.

C. +1.96%.

39. Which of the following is least likely to be a characteristic of a Giffen good?

A. Its income effect is negative.

B. Its demand curve slopes upward.

C. Its substitution effect is negative.

40. A firm's production process requires two factors, labor and capital. The following table illustrates the marginal productivity and cost of each factor at the current level of production.

|  |  |  |
| --- | --- | --- |
| Type of Input | Marginal Product (MP) of Input | Current Price of Input |
| Labor | 120 units | $4 per unit |
| Capital | 120 units | $12 per unit |

If MP is the marginal product, which of the following best describes the firm's optimal decision?

A. Simultaneously increase the use of both factors until the MP is maximized.

B. Initially increase the use of capital until its MP/unit cost equals the MP/unit cost of labor.

C. Initially increase the use of labor until its MP/unit cost equals the MP/unit cost of capital.

41. The nominal and real GDP for a country are provided below:

|  |  |  |
| --- | --- | --- |
|  | 2010 | 2011 |
| GDP at market prices (€ millions) | 3,679,098 | 3,818,145 |
| Real GDP (2001 € millions) | 3,163,330 | 3,342,570 |

For 2011, the inflation rate (%) in the country is closest to:

A. –1.8.

B. 3.8.

C. 5.7.

42. The price index that best resolves the substitution bias is the:

A. Fisher index.

B. Paasche index.

C. Laspeyres index.

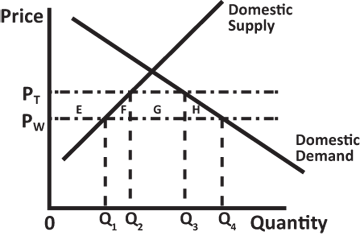
43. A developing country that maintains a fixed value for its currency relative to the U.S. dollar is experiencing a decline in its economic activity, and its inflation rate falls below the level in the United States. As a result of the developing country's actions to maintain the fixed exchange rate target, its:

A. money supply will contract.

B. short-term interest rates will fall.

C. foreign exchange reserves will decrease.

44. The diagram below shows the domestic demand and supply curves for a country that imports a commodity, where PW is the commodity's world price and PT is its domestic price after the imposition of a tariff.



The gain in government revenues arising from the imposition of the tariff is best described by area(s):

A. J.

B. L.

C. K + M.

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

45. The following data are available on a company:

|  |  |
| --- | --- |
| Metric | Company |
| Stock price per share | $60.75 |
| Comprehensive income per share | $4.15 |
| Other comprehensive income (millions) | $87.60 |
| Common shares outstanding (millions) | 46.506 |

On a net income basis, the company's P/E ratio is closest to:

A. 10.1.

B. 14.6.

C. 26.8.

46. The following data are available on a company:

|  |  |
| --- | --- |
| Metric ($ thousands) | Company |
| Interest expense & payments | 1,000 |
| Income tax expense | 1,100 |
| Net income | 3,400 |
| Lease payments | 500 |

The company's fixed charge coverage ratio is closest to:

A. 2.27.

B. 4.00.

C. 5.50.

47. Under the IFRS Conceptual Framework for Financial Reporting, which of the following is least likely considered a fundamental qualitative characteristic that makes financial information useful?

A. Relevance

B. Comparability

C. Faithful representation

48. Under IFRS, which of the following is most commonly classified as a noncurrent liability?

A. Warranties

B. Notes payable

C. Deferred tax liability

49. he following financial data are available for a company:

|  |  |  |
| --- | --- | --- |
| Metric | 2011 (€ thousands) | 2010 (€ thousands) |
| Cost of goods sold | 600 | 400 |
| Inventory | 500 | 600 |
| Accounts payable | 200 | 400 |
| Accounts receivable | 400 | 900 |

Cash paid to suppliers (€ thousands) in 2011 is closest to:

A. 300.

B. 700.

C. 900.

50. The following financial statement data are available for a company:

|  |  |
| --- | --- |
| Metric | (£ thousands) |
| Net income | 500 |
| Depreciation | 150 |
| Cash flow from operations | 600 |
| Free cash flow to the firm | 300 |
| Beginning total assets | 4,000 |
| Ending total assets | 6,000 |
| Book value | 3,000 |

The company's cash return on assets ratio is closest to:

A. 10%.

B. 12%.

C. 13%.

51. For which of the following inventory valuation methods is the gross profit margin least likely to be the same under both a perpetual inventory system and a periodic inventory system?

A. FIFO

B. LIFO

C. Specific identification

52. Under U.S. GAAP, which of the following is least likely a disclosure concerning inventory?

A. The amount of inventories recognized as an expense during the period

B. The carrying amounts of inventories carried at fair value less costs to sell

C. The circumstances or events that led to the reversal of any write-down of inventories

53. Due to significant changes in the marketplace, the demand for a company's product has fallen and is not expected to recover to previous levels. The following information is related to the patent under which the product is produced:

|  |  |
| --- | --- |
| Item Description | $ (thousands) |
| Carrying value amount | 36,000 |
| Undiscounted expected future cash flows | 38,000 |
| Present value of expected future cash flows | 32,000 |
| Fair value if sold | 34,000 |
| Costs to sell | 4,000 |

Which of the following statements is most accurate? The patent is impaired under:

A. IFRS only.

B. U.S. GAAP only.

C. both IFRS and U.S. GAAP.

54. The following information is available about a company for its 2011 fiscal year:

|  |  |
| --- | --- |
| Accounting profit (earnings before taxes) | $250,000 |
| Taxable income | $215,000 |
| Tax rate | 30% |
| Income taxes paid in 2011 | $61,200 |
| Deferred tax liability, 1 January 2011 | $82,400 |
| Deferred tax liability, 31 December 2011 | $90,650 |

The income tax expense reported on the 2011 statement of earnings is closest to:

A. $64,500.

B. $72,750.

C. $83,250.

55. A company that provides cruise ship vacations uses term loans to finance the acquisition of new cruise ships. Which of the following is most likely a negative covenant for the loans? The company must:

A. ensure that the ships are insured.

B. seek lender approval to pay dividends.

C. maintain a minimum level of working capital.

56. Activities or actions that result in inflated sales or underreported expenses will most likely lead to a(an):

A. buildup of assets.

B. buildup of liabilities.

C. increase in cash from operations.

57. The following data are available on a company:



The least likely explanation for the change in the cash conversion cycle is that the firm improved on its:

A. payments to suppliers.

B. inventory management.

C. ability to collect from customers.

58. An e-commerce company sells hotel room nights on its website under agreement from a large number of major hotel chains. The hotel chains grant the company flexibility for the rooms they supply to the company's website and for the prices charged. These major chains bear the responsibility for providing all services once a customer books a room from the website. During 2011, the company received $5 million in payments from the sale of hotel rooms. The cost of these rooms was $4.5 million, which does not include $250,000 in direct selling costs. Under U.S. GAAP, the company's cost of sales is closest to:

A. $250,000.

B. $4,500,000.

C. $4,750,000.

59. The following information is available about a company with potentially dilutive securities in its capital structure:

1. 2011 net income of $32 million.

2. Weighted average number of common shares outstanding of 4.5 million.

3. $15 million of 12% convertible bonds, convertible into 50,000 shares.

4. 200,000 options with an exercise price of $50 per share.

5. Average market price of $80 per share during the fiscal year.

6. Tax rate of 30%.

The company's diluted EPS is closest to:

A. $6.99.

B. $7.19.

C. $7.31.

60. Which of the following statements about the direct method for presenting cash from operating activities is most appropriate? The direct method:

A. shows the impact of accruals.

B. shows the reasons for differences between net income and operating cash flows.

C. provides information on the specific sources of operating cash receipts and payments.

61. Interest payable decreased during a company's fiscal year. Compared with the amount of cash interest payments made, interest expense is most likely:

A. lower.

B. higher.

C. the same.

62. Unused tax losses and credits that a company expects to use in future periods will most likely give rise to:

A. deferred tax assets.

B. valuation allowances.

C. deferred tax liabilities.

63. During the year, a company purchases 1,000 units of inventory at £20.20 per unit. In addition, the following items relate to inventory acquisition and handling during the year.

 The total costs (in £ thousands) that will be included in inventory are closest to:

A. 22,766.

B. 23,091.

C. 24,341.

64. The following information is available concerning a new showroom a company built, with construction starting on 1 January 2010 and the grand opening on 2 January 2012:



The depreciation expense (in € millions) for the showroom in 2012 is closest to:

A. 0.8250.

B. 0.9575.

C. 1.0175

65. A company that prepares its financial statements under IFRS can most likely report which of the following assets using the fair value model?

A. Houses built by the company for sale to customers

B. A building owned by the company and leased out to tenants

C. A building the company owns and uses to house its administrative activities

66. If a company has a deferred tax asset reported on its statement of financial position and the tax authorities reduce the tax rate, which of the following statements is most accurate concerning the effect of the change? The existing deferred tax asset will:

A. not be affected.

B. increase in value.

C. decrease in value.

67. A company prepares its financial statements according to U.S. GAAP and leased a piece of equipment on 1 January 2012. Information relevant to the transaction is as follows:

1. Five annual lease payments of $25,000, with the first payment due 1 January 2012.

2. Interest rate on similar company debt is currently 8%.

3. The fair value of the equipment is $115,000.

4. Useful life of the equipment is seven years.

5. The company depreciates other equipment in the same asset class on a straight-line basis.

The total expense related to the lease on the company's 2012 income statement will be closest to:

A. $22,024.

B. $25,000.

C. $28,185.

68. An increase in which of the following ratios would most likely result in an increase in operating cash flows?

A. Quick ratio

B. Days sales in payables

C. Days sales in receivables

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

69. When a new project reduces the cash flows of an existing project of the same firm, it is best described as a(n):

A. sunk cost.

B. externality.

C. opportunity cost.

70. A company intends to issue new common stock with flotation costs of 3.2% per share. The expected dividend next year is $0.32, and the dividend growth rate is expected to be 10% in perpetuity. Assuming the shares are issued at a price of $14.69, the cost (%) of external equity for the firm is closest to:

A. 12.18.

B. 12.25.

C. 12.48.

71. A company is considering a switch from an all-equity capital structure to a structure with equal amounts of equity and debt without increasing assets. This change will reduce the net income by 30%. If the current return on equity (ROE) is 10%, the ROE (%) under the proposed capital structure will be closest to:

A. 6.

B. 14.

C. 20.

72. According to best practices of corporate governance, which of the following committees will most likely have members from executive management?

A. Audit

B. Nominations

C. Environmental health and safety

73. A project has the following cash flows (£):

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Year 0 | Year 1 | Year 2 | Year 3 | Year 4 |
| –1,525 | 215 | 345 | 475 | 1,215 |

Assuming a discount rate of 11% annually, the discounted payback period (in years) is closest to:

A. 3.4.

B. 3.9.

C. 4.0.

74. A company issues new 20-year, $1,000 bonds with a coupon rate of 6.2% payable semiannually at an issue price of $1,030.34. Assuming a tax rate of 28%, the firm's annual after-tax cost of debt (%) is closest to:

A. 4.28.

B. 4.46.

C. 5.94.

75. A company has decided to switch to using accelerated depreciation from straight-line depreciation. Holding other factors constant, the degree of total leverage will most likely:

A. increase.

B. decrease.

C. not change.

76. Which of the following is most likely a secondary source of liquidity?

A. Trade credit

B. Bank line of credit

C. Inventory liquidation

77. If a 90-day, $10,000 U.S. Treasury security is selling for $9,870, the discount-basis yield (%) is closest to:

A. 5.20.

B. 5.27.

C. 5.34.

78. If a stock is currently selling at $30.00, after a 5% stock dividend, the new share price is closest to:

A. $28.50.

B. $28.57.

C. $30.00.

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

79. A trader who owns shares of a stock currently trading at $100/share places a "GTC, stop 90, limit 85 sell" order (GTC = Good till cancelled). Assuming the specified stop condition is satisfied and the order becomes executed, which of the following statements is the *most accurate*?

A. The trader faces a maximum loss of 15.

B. The order will be executed at the exact price, either 90 or 85.

C. The order becomes a market order when the price falls below 85 and remains valid for execution.

80. Which of the following statements is *least accurate* with respect to fixed-income indices?

A. Many of the underlying securities in the index tend to be illiquid.

B. The indices are susceptible to turnover of the underlying securities.

C. Compared with equity indices, it is easier and less expensive to replicate fixed-income indices.

81. Which of the following statements concerning the characteristics of equity securities is *most accurate*?

A. Putable common shares provide benefits to both the issuing company and investors.

B. Convertible preference shares are more volatile and riskier than the underlying common shares.

C. Investors owning a small number of common shares would prefer statutory voting to cumulative voting.

82. Which of the following statements concerning companies in different industry environments is *most accurate*?

A. Companies in mature industries tend to focus on efficiency gains and gain market share through superior products.

B. An industry's experience curve declines with a decrease in the utilization of capital equipment and spreading overhead over a fewer number of units.

C. Companies in fragmented industries would not be highly price competitive because they tend to think individualistically, making coordination difficult.

83. An investor gathers the following data pertaining to a company for the fiscal year 2011.

|  |  |
| --- | --- |
| Net income | $5,000,000 |
| Dividend payout ratio | 40% |
| Common shareholders' equity (1 January 2011) | $45,000,000 |
| Number of outstanding shares | 6,000,000 |
| Price per share (31 December 2011) | $30.00 |

The company's price-to-book ratio as of 31 December 2011 is *closest* to:

A. 3.60.

B. 3.75.

C. 3.83.

84. A company's non-callable, non-convertible preferred stock paying an annual dividend of $3.75 is currently selling at its par value of $50 per share. If the investors' required rate of return increases by 75 bps, the preferred stock's new price is *closest* to:

A. $45.45.

B. $49.50.

C. $55.56.

85. If the following three stocks are held in a portfolio, the portfolio's total return on an equal-weighted basis (%) is closest to:



A. 3.28.

B. 5.94.

C. 6.37.

86. An internal evaluation of the trading behavior of three fund managers of a mutual fund company during the past year has revealed the following:

 From the above, which of the three managers most likely displayed a behavioral bias called "disposition effect"?

A. Manager X

B. Manager Y

C. Manager Z

87. For a U.S. investor, which of the following statements concerning investing in depository receipts (DRs) is least accurate?

A. Investing in DRs could provide arbitrage opportunities and entail currency risk.

B. Sponsored DRs are subject to greater reporting requirements than unsponsored DRs.

C. Investors in unsponsored DRs would have the same voting rights as the direct owners of common shares.

88. An investor who wants to estimate the market capitalization of a company located in India has gathered the following data:

 Assuming an enterprise value multiple of 3.2, the company's market capitalization (in INR millions) is closest to:

A. 28.5.

B. 33.0.

C. 37.5.

89. The following data pertain to a company that can be appropriately valued using the Gordon growth model. The dividend is expected to grow indefinitely at the current sustainable growth rate.

 The stock's intrinsic value is closest to:

A. $34.62.

B. $37.94.

C. $41.90.

90. Which of the following statements concerning different valuation approaches is most accurate?

A. The justified forward P/E approach offers the advantage of incorporating fundamentals and presenting intrinsic-value estimations.

B. It is advantageous to use asset-based valuation approaches rather than forward-looking cash flow models in the case of companies that have significant intangibles.

C. One advantage of the three-stage dividend discount model (DDM) is that it is equally appropriate for young companies entering the growth phase and those entering the maturity phase.

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

91. A financial institution enters into a forward rate agreement (FRA), expiring in 30 days, to lend $15,000,000 at the 90-day LIBOR interest of 2%. If 90-day LIBOR is 3% when the FRA expires in 30 days, the payoff to the financial institution is closest to:

A. –$37,500.

B. –$37,221.

C. $12,469.

92. A U.S.-based company wishes to borrow R$434,525,000 to fund an expansion of its operations in Brazil. Based on an exchange rate of R$1.7381 per US$, the company borrows US$250,000,000 in the United States and enters into a currency swap with a dealer. The interest rates are 6.5% on US dollars and 10.7% on Brazilian real. Payments are made every 180 days. Based on a 360-day year, the periodic 180-day payments made by the U.S. company and the dealer, respectively, are closest to:

|  |  |  |  |
| --- | --- | --- | --- |
|  | U.S. Company |  | Dealer |
| A. | Pays US$5,250,000 |  | — |
| B. | Pays R$23,247,088 |  | Pays US$8,125,000 |
| C. | Receives R$434,525,000 |  | Receives US$250,000,000 |

A.

B.

C.

93. An interest rate cap can best be described as a combination of a series of interest rate:

A. put options.

B. call options.

C. call and put options.

94. For which of the following futures contracts is price dependent on the LIBOR interest rate and cash settlement permitted when the contract expires?

A. Currency futures

B. Eurodollar futures

C. U.S. T-bond futures

95. A put option with an exercise price of $530 that is expiring in five months is selling for a price of $23. If the price of the underlying stock at expiration is $540, the profit to the seller (or writer) of the put is closest to:

A. –$33.

B. –$13.

C. $23.

96. An investor has purchased a share of stock for $190. A call option on this stock, expiring in seven months and with an exercise price of $200, is priced at $11.40. If the investor enters into a covered call now, the profit on this strategy if the stock price at expiration is $215 is closest to:

A. –$3.60.

B. $21.40.

C. $28.60.

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

97. Compared with traditional investments, over longer periods, alternative investments are least likely to have:

A. higher expected returns.

B. better diversifying power.

C. more efficiently priced assets.

98. A hedge fund strategy that most likely involves simultaneously holding short and long positions in common stock is:

A. volatility.

B. quantitative directional.

C. distressed/restructuring.

99. A hedge fund begins the year with $120 million and earns a 25% return for the year. The fund charges a 1.5% management fee on end-of-year fund value and a 15% incentive fee on the return, net of the management fees, that is in excess of a 6% fixed hurdle rate. A fund investor's return for the year, net of fees, is closest to:

A. 19.66%.

B. 20.56%.

C. 21.25%.

100. Management fees for a private equity fund are most likely based on:

A. fair value of assets under management.

B. drawdowns of committed capital plus any undistributed capital gains.

C. total committed capital less capital returned from investments that are exited.

101. It is most likely easiest for a research analyst to value the holdings of a:

A. hedge fund that follows a short bias strategy.

B. REIT invested only in high-rise office buildings.

C. private equity firm concentrating in management buy-in LBOs.

102. Which of the following risk issues is most likely important for an investment in a private equity fund that focuses on venture capital but not an investment in a REIT that holds undeveloped land?

A. Investment liquidity

B. Mismeasurement of volatility

C. Independence of valuation estimates

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

103. Which of the following would most likely represent the coupon rate for an inverse floater?

A. 5% + 1-year LIBOR

B. 5 x 1-year LIBOR – 6%

C. 18% – 2 x 1-year LIBOR

104. A 20-year bond indenture requires its issuer to retire 5% of the issue each year. This requirement is best referred to as a

A. refunding provision.

B. sinking fund provision.

C. special redemption provision.

105. Which of the following most likely increases the interest rate risk of a floating-rate security?

A. Higher interest rate cap

B. Greater spread over the index

C. Longer time until the next coupon reset

106. A bond is currently selling for 102.31. A valuation model estimates the price will fall to 101.12 if interest rates increase by 20 bps and rise to 103.74 if interest rates decrease by 20 bps. Using these estimates, the duration of the bond is closest to:

A. 6.31.

B. 6.40.

C. 6.48.

107. A central government auctions additional bonds of a previously outstanding bond issue. This is best referred to as the:

A. tap method.

B. single price method.

C. ad hoc auction method

108. Compared with Tranche A, Tranche B of the same CMO structure will most likely have:

A. more prepayment risk.

B. a lower principal balance.

C. a longer repayment period.

109. The argument that investors cannot learn about market expectations for future interest rate changes from the shape of the yield curve is most closely associated with which theory of the term structure of interest rates?

A. Pure expectations

B. Liquidity preference

C. Market segmentation

110. The yield on a five-year U.S. corporate bond is 8.17%, and the yield on a five-year U.S. Treasury bond is 5.64%. An analyst calculates a yield spread measure for the corporate bond equal to 1.45. This measure is most likely the:

A. yield ratio.

B. relative yield spread.

C. absolute yield spread.

111. How much will the value of a three-year $100 par value coupon bond with annual payments, a coupon rate of 9%, and a discount rate of 7% most likely change if market interest rates immediately increase by 1%?

A. –3.47

B. –2.68

C. –2.40

112. Treasury spot rates on a bond-equivalent yield (BEY) basis are provided below.

 Using these spot rates, the value of a 2.5-year Treasury security that makes semiannual payments based on a 2% coupon rate is closest to:

A. 99.06.

B. 101.98.

C. 106.88.

113. A bond's duration is 7.31 and its convexity is –24.85. Using the duration model with convexity adjustment, the bond's percentage change in price if interest rates decrease 2% is closest to:

A. 13.64%.

B. 15.12%.

C. 15.60%.

114. Consider two sovereign bonds issued in different markets. Bond A will most likely have higher interest rate risk than Bond B if Bond A has a higher:

A. yield.

B. coupon rate.

C. expected yield volatility.

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

115. Which of the following is least likely true for a separately managed account (SMA) compared to a mutual fund?

A. Assets are directly owned by the individual.

B. Transactions can be tailored to the specific tax needs of the investor.

C. The minimum investment required to open an SMA is lower than that of a mutual fund.

116. The 15-month holding period return for a security is 12%. Its annualized return is closest to:

A. 9.49%.

B. 9.60%.

C. 10.03%.

117. A portfolio contains equal weights of two securities having the same standard deviation. If the correlation between the returns of the two securities was to decrease, the portfolio risk would most likely:

A. increase.

B. decrease.

C. remain the same.

118. If the expected return on the market portfolio is 6% and the risk-free rate is 2%, the expected return of a security with a beta of 1.25 is closest to:

A. 5.00%.

B. 7.00%.

C. 9.50%.

119. Which of the following is least likely an assumption of the capital asset pricing model (CAPM)?

A. Security prices are not affected by investor trades.

B. An investor can invest as much as he or she desires in any asset.

C. Investors are different only with respect to their unique holding periods.

120. Which of the following is most likely associated with an investor's ability to take risk rather than the investor's willingness to take risk?

A. The investor has a long investment time horizon.

B. Safety of principal is very important to the investor.

C. The investor believes earning excess returns on stocks is a matter of luck.