

2019 Level I Mock Exam (B) PM

The afternoon session of the 2019 Level I Chartered Financial Analyst® Mock Examination has 120 questions. To best simulate the exam day experience, candidates are advised to allocate an average of one and a half minutes per question for a total of 180 minutes (3 hours) for this session of the exam.

Questions	Topic	Minutes
1–19	Ethical and Professional Standards	28.5
20–31	Quantitative Methods	18
32–43	Economics	18
44–61	Financial Reporting and Analysis	27
62–73	Corporate Finance	18
74–80	Portfolio Management	10.5
81–93	Equity	19.5
94–106	Fixed Income	19.5
107–113	Derivatives	10.5
114–120	Alternative Investments	10.5
Total:		180

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2019 LEVEL I MOCK EXAM (B) PM

- 1 Which of the following is *most likely* found in the CFA Institute Standards of Professional Conduct, Standard I–Professionalism? Members and candidates must:
 - A not engage in any professional conduct involving dishonesty, fraud, or deceit or commit any act that reflects adversely on their professional reputation, integrity, or competence.
 - B place the integrity of the investment profession and the interest of clients above their own interest.
 - C maintain and improve their professional competence and strive to maintain and improve the competence of other investment professionals.
- 2 Beth Kozniak, a CFA candidate, is an independent licensed real estate broker and a well-known property investor. She is currently brokering the sale of a commercial property on behalf of a client in financial distress. If the client's building is not sold within 30 days, he will lose the building to the bank. A year earlier, another client of Kozniak's had expressed interest in purchasing this same property. However, she is unable to contact this client, and she has not discovered any other potential buyers. Given her distressed client's limited time frame, Kozniak purchases the property herself and foregoes any sales commission. Six months later, she sells the property for a nice profit to the client who had earlier expressed interest in the property. Does Kozniak *most likely* violate the CFA Institute Standards of Professional Conduct?
 - A No
 - B Yes, she did not disclose her potential conflicts of interest to either client.
 - C Yes, she profited on the real estate to the detriment of her financially stressed client.
- 3 Colin Caldwell, CFA, is the chief investment officer of Northwest Mutual Fund, whose investment objective is to invest in fixed income emerging market securities. Caldwell allocates the fund's assets primarily to bonds of commodity producers in emerging markets and invests in a combination of several different investments to ensure an acceptable level of risk. The allocation is clearly disclosed in all fund communications. High volatility in the commodities markets at the start of the year makes Caldwell pessimistic about returns, so he shifts the fund into emerging market and US government securities, positions he maintains at the end of the year. This change is noted in the next annual report to fund shareholders. Caldwell's investment change least likely violated the CFA Institute Code of Ethics and Standards of Professional Conduct concerning:
 - A diversification.
 - B communication with clients.
 - C investments outside his mandate.
- 4 Christina Ng, a Level I CFA candidate, defaulted on a bank loan she obtained to pay for her Master's degree tuition when her wedding cost more than expected. A micro finance loan company lent her money to pay off the tuition loan in full including penalties and interest. The micro finance loan company even extended further credit to pay for her parent's outstanding medical bills. Unfortunately, her parent's health problems escalated to the point where Ng had to take extensive time away from work to deal with the issues. She was subsequently fired

and consequently defaulted on the second loan. As she was no longer employed, Ng decided to file for personal bankruptcy. Do the loan defaults leading up to Ng's bankruptcy *most likely* violate Standard I(D)–Misconduct?

- A No.
 - B Yes, with regard to the first loan default.
 - C Yes, with regard to the second loan default.
- 5 Raymond Ortiz, CFA, provides investment advice to high-net-worth investors. Ortiz has just completed an analysis of Continental Wheat, a manufacturer of wheat-based food products. He rated the company a long-term hold for investors seeking growth and income. Ortiz's analysis included a review of the company's management team, financial data, pro forma financial positions, dividends and dividend policy, and a comparison of Continental with its competitors. Although he does not tell anyone, five years ago, Ortiz worked for and managed the commodities derivatives trading unit of Continental. As part of his compensation at Continental, he received stock, which he still owns. Based upon his research, Ortiz recommends Continental to clients who have a moderate risk tolerance. Two weeks later Continental announces its quarterly earnings are 30% less than a year ago. Consequently, shares of Continental drop by 50%. Ortiz most likely violated the CFA Institute Code of Ethics and Standards of Professional Conduct related to his stock:
- A research.
 - B ownership.
 - C recommendation.
- 6 Belen Zapata, CFA, is the owner of Kawah Investments. Kawah promises investors returns of up to 12% per year and claims to achieve this by investing in non-investment-grade bonds and other fixed-income instruments. Over the next 12 months, bond market yields reach unprecedented lows, and Zapata finds it impossible to achieve the returns she expected. No investments are ever made by Kawah, and clients are completely paid back all of their original investment. Zapata most likely violated the CFA Institute Standards of Professional Conduct because of the:
- A return of capital.
 - B promised returns.
 - C investment mandate.
- 7 Bryan Barrett, CFA, runs an investment advisory service providing advice on gold and other commodities to several large retail banks. Barrett advertises his services in widely read publications to broaden his business to include retail clients. Because the client base for the institutions that Barrett serves is large, he is comfortable stating in the ads that thousands of his clients have benefited from his advice. Does Barrett's advertisement *most likely* violate any CFA Institute Standards of Professional Conduct?
- A No.
 - B Yes, related to Misrepresentation.
 - C Yes, related to Communication with Clients.
- 8 Solomon Sulzberg, CFA, is a research analyst at Blue Water Management. Sulzberg's recommendations typically go through a number of internal reviews before they are published. In developing his recommendations, Sulzberg uses a model developed by a quantitative analyst within the firm. Sulzberg made some minor changes to the model but retained the primary framework. In his reports, Sulzberg attributes the model to both the quantitative analyst and

himself. Before the internal reviews of his reports were completed, Sulzberg buys shares in one of the companies. After the internal review is complete he fails to recommend the purchase of the stock to his clients and erases all of his research related to this company. Sulzberg *least likely* violated the CFA Institute Code of Ethics and Standards of Professional Conduct related to:

- A Record Retention.
 - B Misrepresentation.
 - C Priority of Transactions.
- 9 Ri Lin, CFA, is a Portfolio Manager with Dynasty Investment Management. Lin is performing research on Titan Mining for potential inclusion in his fund. Management at Titan is interested in having a well-known fund manager such as Lin as a shareholder. Titan pays for Lin to fly to a company retreat in Tokyo, where a brief introductory meeting is followed by attending a sporting event and then dinner at one of the city's top restaurants. Lin participates after disclosing the activities to Dynasty's compliance department. Which standard did Lin's actions *most likely* violate?
- A Disclosures of Conflicts
 - B Independence and Objectivity
 - C Diligence and Reasonable Basis
- 10 Atlantic Capital Management has access to a limited number of shares in a popular new issue expected to be oversubscribed. Atlantic's portfolio managers have determined the issue to be a prudent addition within Atlantic's developing growth equity strategy. A number of the firm's investment professionals have family-member accounts that are managed to the developing growth strategy. Which of the following allocation options *most likely* adheres to the Code and Standards? Atlantic should allocate the shares:
- A to family-member accounts only after non-family accounts have been allocated their shares.
 - B on a prorated basis across all developing growth accounts, including the family-member accounts.
 - C on a prorated basis across all developing growth accounts, excluding the family-member accounts.
- 11 Teresa Avila, CFA, is a micro cap investment analyst at a hedge fund. The fund requires Avila to hold any securities she recommends for the fund in her own account as well. Because Avila has such a small account, whenever she trades for her own portfolio she combines the transactions with those of the hedge fund so she is sure to have her account aligned with the fund. Has Avila *most likely* violated any CFA Institute Standards of Professional Conduct?
- A No.
 - B Yes, related to Misconduct.
 - C Yes, related to Priority of Transactions.
- 12 Colin Gifford, CFA, is finalizing a monthly newsletter to his clients, who are primarily individual investors. Many of the clients' accounts hold the common stock of Capricorn Technologies. In the newsletter, Gifford writes, "Based upon the next six month's earnings of \$1.50 per share and a 10% increase in the dividend, the price of Capricorn's stock will be \$22 per share by the end of the year." Regarding his stock analysis, the *least* appropriate action Gifford should take to avoid violating any CFA Institute Standards of Professional Conduct would be to:
- A separate fact from opinion.

- B include earnings estimates.
 - C identify limitations of the analysis.
- 13 Dilshan Kumar, CFA, is a world-renowned mining analyst based in London. Recently he received an invitation from Cerberus Mining, a London Stock Exchange listed company with headquarters in Johannesburg, South Africa. Cerberus asked Kumar to join a group of prominent analysts from around the world on a tour of their mines in South Africa, some of which are in remote locations, not easily accessible. The invitation also includes an arranged wildlife safari to Krueger National Park for the analysts. Kumar accepts the invitation planning to visit other mining companies he covers in Namibia and Botswana after the safari. To prevent violating any CFA Institute Standards of Professional Conduct, it is *most* appropriate for Kumar to only accept which type of paid travel arrangements from Cerberus?
- A Ground transportation to Krueger National Park.
 - B Economy class round trip ticket from London to Johannesburg.
 - C Flights on a private airplane to the remote mining sites in South Africa.
- 14 Oliver Rae, CFA, is an individual investment adviser specializing in commercial real estate. Rae recently packaged a real estate limited partnership (RELP), which he sold in a private placement to his existing advisory clients. The partnership has purchased four properties in which Rae held a 5% minority interest. According to the CFA Institute Code of Ethics and Standards of Professional Conduct, Rae should:
- A manage the partnership separately from his advisory business.
 - B disclose conflicts related to the real estate he sold to the partnership.
 - C return all profits earned from his minority interest to the limited partners.
- 15 Can an asset management firm who follows the GIPS standards for select performance composites claim that it is GIPS compliant?
- A No.
 - B Yes, but only if those composites meet GIPS performance reporting requirements.
 - C Yes, but only if it uses the GIPS required return calculation requirements for all composites.
- 16 To comply with the GIPS standards, firms *most likely* must:
- A apply standards on a firm-wide basis.
 - B be verified before they can claim compliance.
 - C be defined as separate legal entities.
- 17 From the point of view of an investor, unethical behavior by investment professionals can *most likely* lead to which of the following?
- A Increased willingness to accept risk
 - B Rise in the demand for investments
 - C Demand for a higher return
- 18 A regulator who requires financial advisers to merely consider the suitability of a product when making recommendations to their clients would *most likely* be setting:
- A both a legal and an ethical standard.
 - B an ethical standard.
 - C a legal standard.
- 19 A profession is *most likely* described as a group of people that:

- A has a common level of basic knowledge about a particular subject.
 B monitors its members based on an agreed-on code of ethics.
 C puts the interests of its members first.
- 20 When flipping three coins simultaneously, the number of outcomes that contain at least two heads is *most likely*:
- A eight.
 B four.
 C three.
- 21 A company has an unsecured line of credit and needs to maintain its EBIT-to-interest coverage ratio greater than 2.0. Its EBIT is estimated to be between \$36 million and \$48 million, with all values equally likely. If the forecasted interest charge for the year is \$20 million, the probability that EBIT/interest will be more than 2.0 is *closest* to:
- A 61.5%.
 B 33.3%.
 C 66.7%.
- 22 An investor purchases 100 shares of stock at \$40 per share. The investor holds the shares for exactly one year and then sells all of them at \$41.50 per share. On the date of sale, the investor receives dividends totaling \$200. The holding period return (HPR) on the investment is *closest* to:
- A 8.75%.
 B 3.75%.
 C 8.43%.
- 23 When testing a hypothesis, the power of a test is *best* described as the:
- A same as the level of significance of the test.
 B probability of rejecting a true null hypothesis.
 C probability of correctly rejecting the null hypothesis.
- 24 If the probability for an event Z is 14% (i.e., $P(Z) = 14\%$), the odds for Z are *closest* to:
- A 0.163.
 B 0.071.
 C 0.123.
- 25 Assuming no short selling, a diversification benefit is *most likely* to occur when the correlations among the securities contained in the portfolio are:
- A greater than +1.
 B equal to +1.
 C less than +1.

- 26 The following information applies to a portfolio composed of Fund A and Fund B:

	Fund A	Fund B
Portfolio weights (%)	70	30
Expected returns (%)	10	16
Standard deviations (%)	7	13
Correlation between the returns of Fund A and Fund B	0.80	

The portfolio's standard deviation of return is *closest* to:

- A 7.38%.
 B 8.80%.
 C 8.35%.
- 27 A mutual fund manager wants to create a fund based on a high-grade corporate bond index. She first distinguishes between utility bonds and industrial bonds; she then, for each segment, defines maturity intervals of less than 5 years, 5 to 10 years, and greater than 10 years. For each segment and maturity level, she classifies the bonds as callable or noncallable. She then randomly selects bonds from each of the subpopulations she has created. For the manager's sample, which of the following *best* describes the sampling approach?
- A Simple random
 B Systematic
 C Stratified random
- 28 A descriptive measure of a population characteristic is *best* described as a:
- A parameter.
 B sample statistic.
 C frequency distribution.
- 29 The daily intraday price performance of a security over a specified period could *best* be analyzed with which type of chart?
- A Line
 B Candlestick
 C Point and figure
- 30 The stated (quoted) annual interest rate on an automobile loan is 10%. The effective annual rate (EAR) of the loan is 10.47%. The frequency of compounding per year for the loan is *closest* to:
- A quarterly.
 B monthly.
 C weekly.
- 31 A consultant starts a project today that will last for three years. Her compensation package includes the following:

Year	End-of-Year Payment
1	\$100,000
2	\$150,000
3	\$200,000

- If she expects to invest these amounts at an annual interest rate of 3%, compounded annually until her retirement 10 years from now, the value at the end of 10 years is *closest* to:
- A \$618,994.
 B \$566,466.
 C \$460,590.
- 32 Which of the following is *most likely* to lead to a recessionary gap?
- A Rising stock prices
 B Declining consumer confidence
 C Easing monetary policy

	Spot Rate	Expected Spot Rate in One Year
USD/EUR	1.3001	1.3456
USD/GBP	1.5805	1.5489

- 33 Based on the table, the appreciation of which of the following currencies is *most likely* to occur?
- A The British pound against the US dollar by 2.00%
 - B The US dollar against the euro by 3.38%
 - C The euro against the US dollar by 3.50%
- 34 An investor examines the following rate quotes for the Brazilian real (BRL) and the Australian dollar (AUD) and shorts BRL500,000.
- Spot rate BRL/AUD: 2.1128
 - BRL 1-year interest rate: 4.1%
 - Forward rate BRL/AUD: 2.1388
 - AUD 1-year interest rate: 3.1%
- The risk-free arbitrage profit that is available is *closest* to:
- A –BRL6,327.
 - B BRL1,344.
 - C BRL6,405.
- 35 Consider two countries, A and B. Country A, a closed country with a relative abundance of labor, holds a comparative advantage in the production of textiles. Country B has a relative abundance of capital. When the textile trade is opened between the two countries, Country A will *most likely* experience a favorable impact on:
- A labor.
 - B both capital and labor.
 - C capital.
- 36 A country implements policies that are expected to increase taxes by €100 million, increase government spending by €50 million, and reduce investments and private sector savings by €25 million each. As a result, the country's current account balance is *most likely* to:
- A decrease by €50 million.
 - B increase by €100 million.
 - C increase by €50 million.
- 37 The tools used by central banks to implement monetary policy *most likely* include:
- A transfer payments.
 - B open market operations.
 - C raising or lowering income taxes.
- 38 An increase in the official policy rate will *most likely* lead to:
- A gradual increases in commercial banks' base rates.
 - B reduced credit availability.
 - C contracting commercial bank liquidity.
- 39 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 Costs (\$)
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 100.
 - B 60.
 - C 20.
- 40 An electricity producer charges lower rates to its high-volume customers and higher rates to its low-volume customers. The degree of price discrimination is *best* described as:
- A second.
 - B first.
 - C third.
- 41 A college student's monthly demand for pizza is given by the equation:

$$Q_{\text{Pizza}}^D = 11 - 0.50 \times P_{\text{Pizza}} + 0.01 \times I - 0.20 \times P_{\text{Cola}}$$

where

Q_{Pizza}^D = the number of pizzas ordered per month

P_{Pizza} = the price of a pizza

I = her monthly food budget

P_{Cola} = the price of cola per bottle

The student's current monthly food budget is \$540, the price of a pizza is \$6, and the price of a bottle of cola is \$2. If the student's monthly food budget were to increase to \$740, the slope of her demand curve for pizza would be *closest* to:

- A -2.0.
 - B -2.3.
 - C -0.5.
- 42 The following data are for a basket of three consumption goods used to measure the rate of inflation:

Goods	Prior Year		Current Year	
	Quantity	Price	Quantity	Price
5 lb. bag sugar	150 bags	\$3.12	180 bags	\$2.92
5 lb. bag flour	800 bags	\$2.18	750 bags	\$3.12
Frozen pizza (each)	250	\$2.90	250	\$3.00

Using the consumption basket for the current year, the Paasche Index is *closest* to:

- A 124.6.
- B 123.7.
- C 125.4.

- 43 Suppose that inflation increases due to higher capacity utilization. Such inflation is *best* described as:
- A demand–pull inflation.
 - B stagflation.
 - C cost–push inflation.
- 44 All else being equal, a decrease in which of the following financial metrics would *most likely* result in a lower return on equity (ROE)?
- A The tax rate
 - B Leverage
 - C Days of sales outstanding
- 45 The following selected financial information is available:

Metric	
Sales	\$421,000
Cost of goods sold (COGS)	315,000
Cash	30,000
Average accounts receivable	40,000
Average inventories	36,000
Average accounts payable	33,000

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

- A 76.4.
 - B 45.2.
 - C 38.2.
- 46 Which of the following descriptions of financial reporting is considered to be of the *highest* quality?
- A Within GAAP but with earnings management
 - B Within GAAP but with biased choices
 - C Outside GAAP but with conservative choices
- 47 Which of the following statements is *least* accurate?
- A IFRS Foundation trustees appoint members of the IASB.
 - B The IASB is monitored by a board that includes the US SEC.
 - C IFRS Foundation trustees oversee the policy decisions of the FASB.
- 48 The *best* description of a classified statement of financial position is one that:
- A is supported by note disclosures relevant to understanding its components.
 - B distinguishes between current and non-current assets and liabilities.
 - C has not been audited.
- 49 A credit analyst considers selected ratios calculated for three companies:

	Company A	Company B	Company C
EBITDA/Average assets	8.4%	6.2%	4.3%
Debt/EBITDA	2.0	2.8	3.5
Inventory turnover	4.2	5.8	6.3

Based on the information given, which company is *most likely* to receive the highest credit rating?

- A Company C

B Company A

C Company B

- 50** One of the notable differences between IFRS and US GAAP when dealing with income tax is *best* illustrated by the fundamental treatment of:

A non-deductible goodwill.

B the revaluation of property, plant, and equipment.

C temporary differences between the carrying amount and tax base of assets and liabilities.

- 51** At the beginning of the year, a company purchased a fixed asset for \$500,000 with no expected residual value. The company depreciates similar assets on a straight-line basis over 10 years, whereas the tax authorities allow declining balance depreciation at the rate of 15% per year. In both cases, the company takes a full year's depreciation in the first year. The tax rate is 40%. Which of the following statements concerning this asset at the end of the year is *most* accurate?

A The tax base is \$500,000.

B The deferred tax asset is \$10,000.

C The temporary difference is \$25,000.

- 52** A firm that prepares its financial statements according to US GAAP and uses a periodic inventory system had the following transactions during the year:

Date	Activity	Tons (thousands)	\$ per Ton
	Beginning inventory	1	600
February	Purchase	5	650
May	Sale	2	700
August	Purchase	3	680
November	Sale	4	750

The cost of sales (in thousands) is *closest* to:

A \$5,890 using weighted average.

B \$4,080 using LIFO.

C \$3,850 using FIFO.

- 53** In a period of rising prices and stable inventory levels, which inventory valuation method will *most likely* result in the highest inventory turnover ratio, all else being equal?

A Last-in, first-out (LIFO)

B Weighted average cost

C First-in, first-out (FIFO)

- 54** Holding all else constant, a company that develops intangible assets internally rather than purchasing them is *most likely* to report:

A lower amounts of assets.

B higher investing cash outflows.

C lower operating cash outflows.

- 55** A company is purchasing a customer list that it expects will provide economic benefits for the next 5 years. The company chooses to use an accelerated amortization method. The choice will *most likely* result in an amortization expense that will be the:

A highest in the fifth year.

- B** highest in the first year.
C same in all five years.
- 56 Which of the following is *most likely* a benefit of debt covenants for the borrower?
- A** Limitations on the company's ability to pay dividends
B Restrictions on how the borrowed money may be invested
C Reduction in the cost of borrowing
- 57 The following information is available from a company's current financial data, prepared according to US GAAP:

	\$ thousands
Defined-Contribution Plan:	
Contributions to defined contribution plan	1,000
Defined-Benefit Plan:	
Contributions to defined benefit plan	1,500
Employees' service cost for the period	1,400
Interest expense accrued on the beginning pension obligation	200
Expected return on plan assets	400
Actuarial gains for the period	100

- The pension expense (in \$ thousands) reported in the current year is *closest* to:
- A** 2,200.
B 2,500.
C 2,400.
- 58 The analytical tool that would be *most* appropriate for an analyst to use to identify the percentage of a company's assets that are liquid is the:
- A** cash ratio.
B common-size balance sheet.
C current ratio.
- 59 Data for a firm are presented in the following table:

As of 31 December	£ thousands
Cash	200
Accounts receivable	350
Inventory	1,250
Accounts payable	300
Taxes payable	200
Installment loan payable, due in three equal annual payments on 30 June.	600

- The current ratio for the firm's industry is 3.2. Based on the current ratio, the firm's liquidity compared with the industry is *best* described as being:
- A** higher.
B equivalent.
C lower.
- 60 A company recorded the following events during 2014:

	\$ thousands
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 2014 statement of cash flows, the company's net cash flow from investing activities (in thousands) is *closest* to:

- A \$285.
 - B -\$275.
 - C -\$215.
- 61 The converged revenue recognition standards (issued by the International Accounting Standards Board and the Financial Accounting Standards Board in May 2014) are *best* described as differing from pre-converged US GAAP in that they:
- A align the recognition of revenue with the customer's fulfillment of payment obligations.
 - B provide extensive additional guidance for specific industries and transactions.
 - C provide a principles-based approach applicable to many types of revenue-generating activities.
- 62 When computing the cash flows for a capital project, which of the following is *least likely* to be included?
- A Financing costs
 - B Opportunity costs
 - C Tax effects
- 63 A project has the following annual cash flows:

Year 0	Year 1	Year 2	Year 3	Year 4
-\$4,662,005	\$22,610,723	-\$41,072,261	\$33,116,550	-\$10,000,000

Which of the following discount rates *most likely* produces the highest net present value (NPV)?

- A 8%
 - B 15%
 - C 10%
- 64 An analyst gathered the following information about a company that expects to fund its capital budget without issuing any additional shares of common stock:

Source of Capital	Capital Structure Proportion	Marginal After-Tax Cost
Long-term debt	50%	6%
Preferred stock	10%	10%
Common equity	40%	15%

IRR of Two Independent Projects

Warehouse project	8%
Equipment project	12%

If no significant size or timing differences exist among the project(s) and both projects have the same risk as the company's existing projects, which project(s) should be accepted?

- A The warehouse project only
 - B The equipment project only
 - C Both projects
- 65 A company's optimal capital budget *most likely* occurs at the intersection of the:
- A net present value and internal rate of return profiles.
 - B marginal cost of capital and investment opportunity schedule.
 - C marginal cost of capital and net present value profiles.
- 66 A mining company has received government approval for the development of a mining property and has also consulted with members of the local community near the development site throughout the project assessment process. The latter action is *best* described as an example of:
- A principal-agent conflict mitigation.
 - B stakeholder management.
 - C regulatory compliance.
- 67 According to good corporate governance practices, which of the following committees is *most likely* to have members from executive management?
- A Remuneration
 - B Audit
 - C Environmental health and safety
- 68 When computing the weighted average cost of capital (WACC) and assuming a fixed-rate non-callable bond is currently selling above par value, the before-tax cost of debt is *closest* to the:
- A coupon rate.
 - B yield to maturity.
 - C current yield.
- 69 A company's \$100 par value preferred stock with a dividend rate of 9.5% per year is currently priced at \$103.26 per share. The company's earnings are expected to grow at an annual rate of 5% for the foreseeable future. The cost of the company's preferred stock is *closest* to:
- A 9.5%.
 - B 9.2%.
 - C 9.7%.
- 70 A firm is uncertain about both the number of units the market will demand and the price it will receive for them. This type of risk is *best* described as:
- A sales risk.
 - B operating risk.
 - C business risk.

- 71 If the degree of financial leverage (DFL) is 1.00, the operating breakeven point compared with the breakeven point is *most likely*:
- A lower.
 - B the same.
 - C higher.
- 72 For a 90-day US Treasury bill selling at a discount, which of the following methods *most likely* results in the highest yield?
- A Discount-basis yield (DBY)
 - B Money market yield (MMY)
 - C Bond equivalent yield (BEY)
- 73 The effective annualized cost (%) of a banker's acceptance that has an all-inclusive annual rate of 5.25% for a one-month loan of \$2,000,000 is *closest* to:
- A 5.54%.
 - B 5.38%.
 - C 5.27%.
- 74 In the context of strategic asset allocation, adding asset classes with low correlation will *most likely* improve a portfolio's risk–return trade-off as long as the stand-alone risk of the added asset class:
- A does not exceed its diversification effect.
 - B equals its diversification effect.
 - C exceeds its diversification effect.
- 75 Which of the following is *most likely* a part of the feedback step in the portfolio management process?
- A Performance measurement
 - B Developing the investment policy statement
 - C Portfolio construction
- 76 Selected information about shares of two companies is provided in the following table:

Stock	Standard Deviation	Correlation of Returns*	Portfolio Weights
Cable Incorporated	30%	0.65	68%
GPT Company	20%		32%

* Correlation of returns between Cable Incorporated and GPT Company.

The standard deviation of returns of the portfolio formed with these two stocks is *closest* to:

- A 32.85%.
 - B 26.80%.
 - C 25.04%.
- 77 For a portfolio consisting of two assets with a correlation coefficient of +1.0, it is *most likely* that portfolio risk is:
- A equal to the weighted average of the risk of the two assets in the portfolio.
 - B less than the weighted average of the risk of the two assets in the portfolio.

- C greater than the weighted average of the risk of the two assets in the portfolio.
- 78 Stock X and Stock Y have the same level of total risk. Stock X has twice the systematic risk of Stock Y and half its non-systematic risk. Stock X's expected return will *most likely* be:
- A the same as the expected return of Stock Y.
 B lower than the expected return of Stock Y.
 C higher than the expected return of Stock Y.
- 79 Which of the following is *least likely* an assumption underlying the capital asset pricing model (CAPM)?
- A Investors analyze securities according to their own future cash flow estimates and probability distributions.
 B There are no restrictions on short selling assets.
 C The amount invested in an asset can be as much or as little as the investor wants.
- 80 In a good risk management process, the duties of Chief Risk Officer (CRO) *least likely* include:
- A setting the risk tolerance of the organization.
 B participating in the key strategic decisions of the organization.
 C building the risk framework for the organization.
- 81 Which of the following statements is *least* accurate? A firm's free cash flow to equity (FCFE):
- A is a measure of the firm's dividend-paying capacity.
 B increases with an increase in the firm's net borrowing.
 C is significantly affected by the amount of dividends paid by the firm.
- 82 An investor gathers the following data to estimate the intrinsic value of a company's stock using the justified forward price-to-earnings ratio (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 Given the following information for a company:
- Market value per share \$250
 - Current dividend per share \$5
 - Dividend growth rate 4%
 - Required rate of return 6%
- and using the Gordon growth model to estimate the intrinsic value, a share of the company is *best* described as being:
- A fairly valued.
 B overvalued.
 C undervalued.

- 84 Industry analysis is *least* useful to those who are engaged in:
- A a top-down investment approach.
 - B indexing and passive investing strategies.
 - C portfolio performance attribution.
- 85 Unlike commercial industry classification systems, industry classification systems developed by governments *most likely*:
- A are updated more frequently.
 - B are more transparent.
 - C include private companies.
- 86 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.
- 87 The following table shows some data on a company before and after unexpected news is announced to the public:

	Before the Announcement	After the Announcement
Market value per share	\$30	\$31
Estimated intrinsic value per share	\$30	\$33

Based on the data in the table, the market for this company's shares is *best* described as:

- A relatively inefficient.
 - B semi-strong efficient.
 - C overvalued.
- 88 Which of the following is *most likely* a cross-sectional anomaly in financial markets?
- A Closed-end fund discount
 - B Overreaction effect
 - C Value effect
- 89 An investor opens a margin account with an initial deposit of \$5,000. He then purchases 300 shares of a stock at \$30 each on margin, and his account requires a maintenance margin of 30%. Ignoring commissions and interest, the price at which the investor will receive a margin call is closest to:
- A \$19.05.
 - B \$23.08.
 - C \$23.81
- 90 A trader who owns shares of a stock currently trading at \$100 per share places a "GTC, stop \$90, limit \$85 sell" order (GTC means good till cancelled). Assuming the specified stop condition is satisfied and the order becomes executed, which of the following statements is *most* accurate?
- A The order becomes a market order when the price falls below \$85 and remains valid for execution.

- B The trader faces a maximum realized loss of \$15.
 - C The order will be executed at either \$90 or \$85.
- 91 A trader describes her currency contract exposure as “long the euro against the British pound.” Which of the following situations *best* fits her description? She has a:
- A contract that allowed her to sell British pounds and acquire euros.
 - B forward contract to buy euros in exchange for British pounds at a predetermined exchange rate.
 - C forward contract to buy British pounds, using euros she currently holds.
- 92 Participating preference shares are *least likely* to entitle the shareholders to participate in:
- A additional distribution of the company’s assets upon liquidation.
 - B corporate decisions through voting rights.
 - C additional dividends if the company’s profits exceed a predetermined level.
- 93 According to the industry life-cycle model, companies in a mature industry are *most likely* to experience:
- A high barriers to entry.
 - B fierce competition.
 - C low dividend yields.
- 94 Zet Bank has entered into a contract with Louly Corporation in which Zet agrees to buy a 2.5% US Treasury bond maturing in 10 years and promises to sell it back next month at an agreed-on price. From Zet Bank’s perspective, this contract is *best* described as a:
- A repo.
 - B collateralized loan.
 - C reverse repo.
- 95 Which of the following bonds are *most likely* to be bearer bonds?
- A Foreign bonds
 - B Domestic bonds
 - C Eurobonds
- 96 If an issuer is required to retire a specified portion of the bond’s principal each year, the bond *most likely*:
- A is callable.
 - B is a step-up note.
 - C has a sinking fund provision.
- 97 The Delfain Corporation reported a significant improvement in profitability that was followed by a material upgrade in its credit rating. The market responded by immediately requiring a 100 basis point narrower spread to Gilts on Delfain’s 8-year bond. If the bond’s modified duration is 6.0 and its convexity is 55.0, the return impact of this change is *closest* to:
- A 6.28%.
 - B -5.73%.
 - C 7.10%.
- 98 An investor who owns a mortgage pass-through security is exposed to extension risk, which is the risk that when interest rates:

- A fall, the security will effectively have a shorter maturity than was anticipated at the time of purchase.
 - B rise, the security will effectively have a shorter maturity than was anticipated at the time of purchase.
 - C rise, the security will effectively have a longer maturity than was anticipated at the time of purchase.
- 99 A synthetic collateralized debt obligation is a CDO backed by a portfolio of:
- A leveraged bank loans.
 - B residential or commercial mortgage-backed securities.
 - C credit default swaps.
- 100 If the annual market discount rate is 6%, the value of a three-year bond that has a 7% coupon rate, has a maturity (par) value of \$1,000, and pays interest annually is *closest to*:
- A \$1,026.73.
 - B \$1,049.17.
 - C \$973.76.
- 101 Which of the following is *most likely* a limitation of the yield to maturity measure?
- A It assumes coupon payments can be invested at the yield to maturity.
 - B It does not consider the capital gain or loss the investor will realize by holding the bond to maturity.
 - C It does not reflect the timing of the cash flows.
- 102 A credit analyst is *least likely* to use matrix pricing to estimate the required yield and price of a(n):
- A newly underwritten bond.
 - B actively traded speculative grade bond.
 - C inactively traded investment grade bond.
- 103 An analyst uses a valuation model to estimate the value of an option-free bond at 92.733 to yield 11%. If the value is 94.474 for a 60 bp decrease in yield and 91.041 for a 60 bp increase in yield, the approximate modified duration of the bond is *closest to*:
- A 3.09.
 - B 6.17.
 - C 1.85.
- 104 Which of the following *most likely* exhibits negative convexity?
- A A callable bond
 - B An option-free bond
 - C A puttable bond
- 105 The duration and convexity of an option-free bond priced at \$90.25 are 10.34 and 151.60, respectively. If yields increase by 200 bps, the percentage change of the price is *closest to*:
- A -17.65%.
 - B -23.71%.
 - C -20.68%.
- 106 For an option-free, fixed-rate bond the coupon reinvestment risk would *most likely* dominate market price risk when the investment horizon is:

- A greater than the Macaulay duration of the bond.
 - B lower than the Macaulay duration of the bond.
 - C equal to the Macaulay duration of the bond.
- 107 A perfectly hedged position consisting of a derivative and its underlying asset will *most likely* yield a return that is:
- A equal to the risk-free rate.
 - B smaller than the risk-free rate.
 - C greater than the risk-free rate.
- 108 A high convenience yield is *most likely* associated with holding:
- A bonds.
 - B equities.
 - C commodities.
- 109 A swap that involves the exchange of a fixed payment for a floating payment can be interpreted as a series of forward contracts with different expiration dates. These implied forward contracts will *most likely* have:
- A different prices due to differences in the price of the underlying at expiration.
 - B identical prices.
 - C different prices due to differences in the cost of carry.
- 110 Holding other factors constant, the value of a European put option will *most likely* decrease as the:
- A risk-free interest rate increases.
 - B volatility of the underlying increases.
 - C value of the underlying decreases.
- 111 In contrast to over-the-counter options, futures contracts *most likely*:
- A are not exposed to default risk.
 - B represent a right rather than a commitment.
 - C are private, customized transactions.
- 112 Which of these is *best* classified as a forward commitment?
- A A convertible bond
 - B A call option
 - C A swap agreement
- 113 In efficient financial markets, risk-free arbitrage opportunities:
- A will not exist.
 - B may persist in the long run.
 - C may exist temporarily.
- 114 Compared with traditional investments, over longer periods, alternative investments are *least likely* to have:
- A better diversifying power.
 - B higher expected returns.
 - C more efficiently priced assets.
- 115 Categories of alternative investments would *least likely* be described by which of the following?
- A Fine wine and other tangibles
 - B Schools and other long-lived real assets

- C Cash and other liquid investments
- 116 Based on the historical record, adding alternative investments to a traditional investment portfolio consisting of publicly traded debt and equity will *most likely* decrease the portfolio's:
- A liquidity.
 - B downside risk.
 - C risk-adjusted return.
- 117 Which attribute would a private equity firm *most likely* desire when deciding if a company is particularly attractive as a leveraged buyout target?
- A Sustainable cash flow
 - B Efficient management
 - C Market value exceeds intrinsic value
- 118 The three main sources of return for commodities futures contracts *most likely* are:
- A convenience yield, dividend yield, and spot price return.
 - B collateral yield, roll yield, and spot price return.
 - C collateral yield, convenience yield, and roll yield.
- 119 In commodity futures market pricing, when the convenience yield is higher than the cost of carry, the roll yield is positive for:
- A long futures.
 - B short futures.
 - C both long and short futures.
- 120 A measure that is *most likely* well suited to analyzing the performance of alternative investments that may exhibit negative skewness in returns is the:
- A Sortino ratio.
 - B Sharpe ratio.
 - C safety-first measure.