

**Question #1 of 10**

Question ID: 1552310

An equity analyst makes the following statements about the role of equities in a multi-asset portfolio.

Statement 1: Equities are likely to achieve better returns than other asset classes when the economy exhibits strong growth.

Statement 2: Long-term returns on equities are mainly driven by stable dividend yields.

Which of the analyst's statements is correct?

**A) Statement 1 only.**



**B) Statement 2 only.**



**C) Both Statement 1 and Statement 2.**

**Explanation**

Equities are likely to outperform other asset classes when the economy is growing strongly.

Long-term returns on equities are mainly driven by capital appreciation.

(Module 13.1, LOS 13.a)

**Question #2 of 10**

Question ID: 1552339

A global equity absolute return fund charges a fee of 20% of the outperformance in excess of a threshold return of 8%, subject to a high-water mark. This fee is *most likely*.

**A) a management fee.**



**B) an incentive fee.**



**C) a platform fee.**

**Explanation**

An incentive or performance fee is earned by the fund manager when the portfolio outperforms a stated return objective. A high-water mark incorporated into the calculation of the incentive fee protects the investor from paying twice for the same return.

(Module 13.2, LOS 13.c)

**Question #3 of 10**

Question ID: 1552337

A fund analyst makes the following statements related to writing options as a source of income for an equity fund.

- Statement 1: Covered call writing generates income for the fund but limits the upside from price appreciation of the underlying shares.
- Statement 2: Writing cash-covered puts generates income for the fund, but the fund may be required to purchase shares at a premium to their market price.

Which of the analyst's statements is correct?

- A) Statement 2 only.**
- B) Statement 1 only.**
- C) Both Statement 1 and Statement 2.**

**Explanation**

Writing options generates income from the options premiums earned.

If the fund writes (sells) a covered call, it loses the potential upside on the underlying share above the strike price of the call option. (In this scenario, the option buyer will choose to exercise the call option.)

When the fund writes a cash-covered put, the fund is obliged to purchase the underlying share from the holder of the put option if the option is exercised. The option buyer will choose to exercise the put option if the share price falls below the strike price of the put.

(Module 13.2, LOS 13.c)

**Question #4 of 10**

Question ID: 1552350

Which of the following statements regarding active management is correct?

- A) It is more likely to benefit portfolios investing in companies in large-cap and/or developed markets.**
- B) It is more likely to have a benchmark that is liquid.**



**C) It is more likely to have greater tax efficiency than passive management.**



### Explanation

Active management usually requires benchmarks with underlying stocks that are liquid to avoid excessive trading costs.

Companies in large-cap and/or developed markets are usually well-covered by analysts so all publicly available information would be imputed in stock prices, thereby most likely limiting the usefulness of active management.

Compared to passive management, active management is more likely to have higher turnover and more short-term capital gains. Higher turnover and short-term capital gains are generally less tax efficient.

(Module 13.2, LOS 13.e)

---

### Question #5 of 10

Question ID: 1552338

An investor states that the direct costs of research are higher for actively managed funds than for passively managed funds, but that direct costs of portfolio management are higher for passively managed funds than for actively managed funds. Are the investor's statements accurate?

**A) Yes.**



**B) The investor is correct about direct costs of research but incorrect about direct costs of portfolio management.**



**C) The investor is correct about direct costs of portfolio management but incorrect about direct costs of research.**



### Explanation

Direct costs of research and portfolio management are higher for actively managed funds than for the direct costs of passively managed funds.

(Module 13.2, LOS 13.c)

---

### Question #6 of 10

Question ID: 1552314

Which of the following statements regarding the role of equities as a hedge against inflation is correct?

- Statement 1: For equities to be used as a hedge against inflation, real returns on equity should be negatively correlated with inflation.
- Statement 2: Equities have been successfully used as a hedge against inflation because the correlation between real returns on equity and inflation is relatively constant over time.

A) Statement 1 only.



B) Neither Statement 1 nor Statement 2.



C) Statement 2 only.



#### Explanation

If real returns on equity and inflation exhibit positive correlation, equities can in theory be used as an inflation hedge.

The general record for equities as an inflation hedge is mixed because the correlation between the real returns on equity and inflation varies over time and by country.

(Module 13.1, LOS 13.a)

---

#### Question #7 of 10

Question ID: 1552346

The Luna fund invests in the shares of large-cap, value-oriented companies across the developed markets. One of the top 10 holdings of the fund is in Allkinds Insurance Company, which itself is a significant investor in the fund. This scenario *most likely*:

A) does not create potential conflict of interest.



B) creates a potential conflict of interest for the Luna fund but not for the Allkinds Insurance Company.



C) creates a potential conflict of interest for the Allkinds Insurance Company but not for the Luna fund.



#### Explanation

The scenario creates a potential conflict of interest for the Luna fund, arising from shareholder engagement. (*Shareholder engagement* refers to the process whereby investors actively interact with companies by, for example, voting on corporate matters at general meetings.) The Luna fund manager may feel unduly pressured to vote in support of the insurance company's management to avoid losing the significant investment in the fund by the insurance company.




(Module 13.2, LOS 13.d)

---

### Question #8 of 10

Question ID: 1587435

Your client is interested in less conventional approaches to capturing income linked to equity holdings. Which idea is one that you should discuss with this client?

- A) A covered call is a good option in an upward-trending market. 
- B) A cash-covered put is a good option in a deeply downward-trending market. 
- C) A dividend capture strategy is a good idea for dividend paying stocks in a range-bound market.** 

#### Explanation

While a covered call does create additional portfolio income, the capital gains loss from capping a stock's upside in an upward-trending market is detrimental to financial success. A cash-covered put could be a good option in a range-bound or a slight downtrend, but in a deep downtrend, the investor could be forced to purchase shares at a strike price that is considerably higher than the current market price at the time of exercise. Dividend capture works best in a scenario when the stock's price rises or at least falls less than the amount of the dividend paid. A dividend paying stock in a range-bound market could potentially satisfy this need.

(Module 13.2, LOS 13.c)

---

### Question #9 of 10

Question ID: 1552326

Which of the following statements regarding the segmentation of the equity investment universe is correct?

Statement 1: An advantage of segmentation by size and style is that it ensures consistent categorization across investors.

Statement 2: A shortcoming of segmentation by geography is that an investment in a foreign market may offer lower-than-expected exposure to that market.

**A) Both Statement 1 and Statement 2.**



**B) Statement 1 only.**



**C) Statement 2 only.**



### Explanation

A major disadvantage of segmenting by size and style is that categories may be defined differently by different investors.

When segmenting by geography, a major disadvantage is that investing in a foreign market may offer lower exposure to that market than the investor expects. For example, a domestic investor from a developed market buys shares in large companies in a foreign market to diversify. However, these companies may have already diversified their business internationally and may even derive much of their income from the investor's country.

(Module 13.1, LOS 13.b)

---

### Question #10 of 10

Question ID: 1552345

A portfolio analyst makes the following statements about the exercise of voting rights in shareholder engagement.

Statement 1: When an investor borrows stock, voting rights are transferred from the stock lender to the investor (stock borrower).

Statement 2: Empty voting enables the stock lender to keep the voting rights of the loaned stock in exchange for receiving a lower fee from the stock borrower.

Which of the analyst's statements is correct?

**A) Statement 1 only.**



**B) Statement 2 only.**



**C) Both Statement 1 and Statement 2.**



**Explanation**

In a stock loan, voting rights are transferred to the stock borrower.

Empty voting occurs when an investor borrows stock for the explicit purpose of exercising the voting rights attached to the stock.

(Module 13.2, LOS 13.d)