

FinQuiz.com

CFA Level I 1st Mock Exam

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FinQuiz.com – 1st Mock Exam 2016 (PM Session)

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Questions 1 through 18 relate to Ethical and Professional Standards

1. An analyst's investment recommendation and opinions with regard to selling, purchasing and holding securities, disseminated to customers through oral communication is:
 - A. not allowed according to CFA Institute *Standards of Practice Handbook*.
 - B. only allowed if the information has already been disseminated through other communication channels as well.
 - C. is allowed according to CFA Institute *Standards of Practice Handbook* if the firm has such a dissemination policy for its customers.
2. Which of the following is *least likely* required by the CFA Institute Code of Ethics? Members and candidates must:
 - A. strive to maintain and improve the competence of their clients.
 - B. practice and encourage others to practice in a professional and ethical manner.
 - C. place the integrity of investment profession and interests of clients above their own personal interests.
3. Marc Bowen, executive vice president at Ramon Brokerage, a large broker/dealer firm, is responsible for directing and leading 50 associates, to manage the compliance of regulatory requirements and to mitigate financial risks. Bowen delegated his responsibilities among his associates and instructed them about methods to prevent and detect violations of laws and regulations clearly. Due to his preoccupation with other projects Bowen never had sufficient time to review their work. According to the Code and standards, will Bowen be held responsible if an associate fails to fulfill regulatory requirements?
 - A. No, because he clearly instructed the methods to prevent and detect violations.
 - B. Yes, because he should decline in writing to delegate the responsibilities to his associates.
 - C. Yes, because he fails to make reasonable efforts to ensure that the procedures are monitored and enforced.

4. Which of the following statements is *most likely* correct regarding GIPS standards?
- A. Compliance with the GIPS standards is typically required by legal and regulatory authorities.
 - B. Plan sponsors and consultants can make a claim of compliance if they are actually managing assets.
 - C. An investment management firm complying with a majority of the requirements of GIPS can make reference to the GIPS standards.
5. Amanda is an equity analyst with Dennis Securities and is analyzing the stocks of Pearl Inn Corp. In her research, Amanda observed that:
- Pearl Inn is a company with bright future prospects.
 - Pearl Inn's current stock price is fully valued.
 - Compensation of Pearl Inn's managers is dependent on stock performance; therefore any negative report can further affect managers' performances and can hurt the company's future growth.

Keeping in view all these facts she concluded that a buy recommendation for Pearl Inn Corp.'s stock is appropriate. Amanda

- A. Violated the standard relating to independence and objectivity by issuing a buy recommendation.
 - B. is in full compliance with the standards due to her foresight and long term vision for Pearl Inn.
 - C. violated the standards because she lack reasonable and adequate basis for her recommendation.
6. According to CFA Institute *Standards of Practice Handbook*, recommended procedures for block trade and new issues *least likely* include:
- A. processing and executing bundling orders on FIFO basis for efficiency purposes.
 - B. giving same execution price and charging same commission for all clients participating in block trade.
 - C. prohibiting partial fills when trades are grouped and requiring cancellation of orders to be documented and time stamped.

7. For an investment management firm, the responsibility to maintain records that support investment action generally falls with:
- A. the firm.
 - B. a regulatory authority.
 - C. employees of the firm.
8. Jason Lee is a junior equity analyst at TR-Securities. For the last two weeks during his lunchtime he has been consulting an attorney for bankruptcy filing as a result of his failure to pay debts. He has not discussed his financial situation with any of his colleagues or his employer. Is Lee in violation of any CFA Institute Standards of Professional Conduct?
- A. No, he has not violated any standard.
 - B. Yes, he has violated standard I-D ‘Misconduct’.
 - C. Yes, he has violated standard IV-‘Duties to Employer’.
9. The key features of GIPS standards *most likely* include:
- A. addressing every aspect of performance measurement and covering unique characteristics of each asset class.
 - B. requiring firms to include all actual, discretionary or non-discretionary, fee paying portfolios in at least one composite defined by investment mandate, objective or strategy.
 - C. complying with all requirements of GIPS standards including any updates, guidance statements, interpretations, questions and answers (Q&A) which are available on the GIPS website as well as in the *GIPS Handbook*.
10. Sandra Hall, CFA is an analyst with Indus Securities and covers the oil and gas industry. In a meeting with the CEO of B2S Corp., a firm covered by her, she found that the firm’s major clients are residents of the country Cote D’Ivoire. Hall expects the CFA franc (currency of Cote D’Ivoire) to depreciate by 15%. Based on this information and her analysis, Hall believes that B2S Corp.’s next quarter’s earnings will drop substantially and therefore issues a sell recommendation. Hall:
- A. is in full compliance with the standards.
 - B. violated the standard by acting on material nonpublic information.
 - C. has failed to satisfy the requirement of Standard V-A, ‘Diligence and reasonable basis’.

11. Sidney Garza is hired by CRT Securities and is responsible for managing several portfolios with net worth greater than \$25 million. While inspecting the clients' previous financial records, Garza found several suspicious transactions and some questionable practices involving Alan Hart, CFA, CRT's former manager. The applicable laws are strict and require maintaining confidentiality. Under such circumstances Garza should:
- A. reveal confidential information about clients and should inform the CFA Institute professional conduct program (PCP) about Hart's questionable activities.
 - B. not reveal confidential information about clients but should inform the CFA Institute professional conduct program (PCP) about Hart's questionable activities.
 - C. not reveal confidential information about clients and should not inform the CFA Institute professional conduct program (PCP) about Hart's questionable activities.
12. Jacquelyn Kramer is a portfolio manager at a local advisory firm. One of her friends, Wallace Bob, is an independent research analyst and manages his own blog. From time to time Bob refers his subscribers, who need investment advice and want to build portfolios, to Kramer and in return Kramer pays Bob some nominal fees and research reports prepared by her firm. Kramer has never disclosed this arrangement to anyone in her firm. Kramer *most likely* is in violation by failing to disclose the arrangement:
- A. to her employer and the clients.
 - B. to her employer only as clients are not required to pay any additional fees to Bob or Kramer.
 - C. to her clients and not obtaining written consent from her employer prior to making such arrangement.
13. If a firm opts for verification of its claim of compliance with the GIPS standards, the firm:
- A. must hire investment management firm only.
 - B. is required to use an independent third party only.
 - C. can either use an independent third party or can voluntarily perform its own verification.

14. If members and candidates have custody of client's assets they must manage them in accordance with:
- A. some benchmark indices.
 - B. terms of governing documents.
 - C. each asset's risks and return characteristics.
15. In preparing an investment policy statement and suitability analysis, if a client refuses to provide complete information regarding his financial position, the *most suitable* action for a member or candidate is to:
- A. consult the legal and compliance advisors for guidance.
 - B. disclose in writing the impact of withholding information and obtain client approval.
 - C. develop an investment policy statement on the basis of information provided.
16. Kristin Harper, CFA manages individual client portfolios at Lucas Trust Advisory. One of her clients, Nicholas Hanson, is owner of five hotel brands with approximately 800 hotels in Europe. For her vacation, Hanson offered Harper a 25% discount and free meals if she stayed in his hotels. Harper informed her employer about the discount offered by her client over the phone. According to CFA Institute *Standards of Practice Handbook*, if Harper gets that deal she will:
- A. be in compliance with CFA Institute codes and standards.
 - B. violate 'Additional Compensation Arrangements' by failing to disclose free meals and not inform her employer in writing.
 - C. violate 'Independence and Objectivity' as accepting a substantial gift can reasonably be expected to compromise her performance for other clients.

17. Rick Mueller is a junior analyst at Morris & Clifton Advisors (M&CA), a large brokerage and advisory firm with more than 500 analysts. Majority of the analysts at M&CA are either CFA charterholders or are enrolled in different levels of CFA exam program. When the firm asked Mueller, why he wants to become a charterholder, he wrote the following lines, “I have passed Level 2 of the CFA exam. In the field of investment management the CFA designation is globally recognized, it is a rigorous and comprehensive study program, and CFA charterholders achieve better performance results.”

Mueller is *most likely* in violation of the Standards of Professional Conduct with reference to the statement:

- A. “I have passed Level 2 of the CFA exam.”
 - B. “It is a rigorous and comprehensive study program.”
 - C. “CFA charterholders achieve better performance results.”
18. In complying with the GIPS standards, if existing laws and regulations already impose requirements related to the calculation and presentation of investment performance:
- A. firms are required to comply with laws and regulations and disclose the fact in its compliant presentation.
 - B. firms’ compliance with applicable laws and regulations leads to compliance with the GIPS standards.
 - C. firms are strongly encouraged to comply with GIPS standards in addition to applicable regulatory requirements.

Questions 19 through 32 relate to Quantitative Methods

19. An analyst is comparing the performance of a dividend-paying stock for the last seven years. During that time period the central bank has announced a new monetary policy. The results of the analyst are *most likely* subject to:
 - A. survivorship bias.
 - B. time period bias.
 - C. look ahead bias.

20. A pharmaceutical firm has submitted a new drug application(NDA)to FDA. An analyst estimates that the odds for the successful approval of the drug are 1 to 4 and the firm's estimated EPS for the FY2014 is \$15 if FDA accepts NDA and \$7 if FDA rejects NDA.

Firm's expected EPS for FY2014 is *closest* to:

 - A. \$8.6.
 - B. \$9.0.
 - C. \$11.2.

21. A U.S firm will receive four annual payments of £60,000 from its subsidiary in U.K and the firm will invest these payments at the 12% annual interest offered by a U.K bank. If the first payment will be received three years from now, how much will the payments be worth in ten years?
 - A. £451,222.
 - B. £530,563.
 - C. £605,341.

22. Which of the following premiums is *not* incorporated in the nominal risk-free interest rate?
 - A. liquidity premium.
 - B. inflation premium.
 - C. default-free premium.

23. When a person wants to assign every member of a group of size n to one of n slots, he will *most likely* use:
- n factorial.
 - multinomial formula.
 - combination formula.
24. What is the probability that a portfolio's return will exceed 35%, if its mean return is 25% and the standard deviation of return is 37%, assuming normal distribution?

Table 5		$P(Z \leq x) = N(x)$ for $x \geq 0$ or $P(Z \leq z) = N(z)$ for $z \geq 0$								
x or z	0	0.01	0.02	0.03	0.04	0.05	0.06	0.07	0.08	0.09
0.00	0.5000	0.5040	0.5080	0.5120	0.5160	0.5199	0.5239	0.5279	0.5319	0.5359
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
0.50	0.6915	0.6950	0.6985	0.7019	0.7054	0.7088	0.7123	0.7157	0.7190	0.7224

- 27.03%
 - 39.36%
 - 60.64%
25. An investment of \$96,700 will pay \$100,000 in 145 days. The money market yield of the investment is *closest* to:
- 8.19%.
 - 8.47%.
 - 8.52%.
26. Which of the following *best* describes the advantages of Monte Carlo simulation? Monte Carlo simulation:
- is grounded in actual data like historical simulation.
 - can be used to perform “what if” analysis unlike historical simulation.
 - provides better insight into cause-and-effect relationships compared to analytical methods.

27. How would a technician seek to generate profit in a reverse head and shoulder pattern if the price at the bottom of the head was \$156 and neckline price was roughly \$187?
- A. By taking a long position in the stock and by setting the price target at \$218.
 - B. By taking a short position in the stock and by setting the price target at \$125.
 - C. By short selling the stock and anticipating a profit of \$31 excluding transaction cost.
28. Technical analysis is *least likely* based on the factor that:
- A. future price movements are predictable.
 - B. prices are determined by economic factors.
 - C. changes in supply and demand cause changes in prices.
29. Table below gives statistics relating to three portfolios for the year 2013.

Portfolio	Mean Annual Return (%)	Standard Deviation of Return (%)	Skewness	Excess Kurtosis
A	14.31	23.67	+0.02	+0.01
B	12.65	14.52	-0.01	-0.03
C	10.06	9.66	-0.02	+0.02

*Risk-free rate for 2013 = 6%

Based on the information provided above, the portfolio with superior risk-adjusted performance is:

- A. Portfolio A.
 - B. Portfolio B.
 - C. Portfolio C.
30. Harmonic mean is a special type of weighted mean in which each observation's weight is inversely proportional to:
- A. its magnitude.
 - B. a fixed amount.
 - C. n (total observations).

31. An analyst is assessing the performance of a portfolio manager. The mean return of his portfolio (gross of fees) is 27%, the standard deviation is 35%, and the mean return of the benchmark index is 18%. The portfolio's tracking error is *closest* to:
- A. 9.0%.
 - B. 25.7%.
 - C. 44.4%.
32. Which of the following statements is *least likely* correct regarding the p-value approach to hypothesis testing?
- A. According to the p-value decision rule, reject H_0 when p-value is $\geq \alpha$.
 - B. p-value is the smallest level of significance at which the null hypothesis can be rejected.
 - C. p-value is also known as marginal significance level and this approach is considered more efficient relative to the rejection points approach.

Questions 33 through 44 relate to Economics

33. According to exhibit 1 (given below) up to how many units of labor, will the firm achieve increasing marginal returns?

Exhibit 1

Labor	Total Product	Average Product	Marginal Product
0	0	-	-
10	1,000	1,000	1,000
20	2,700	1,300	1,700
30	4,800	1,400	2,100
40	6,000	1,325	1,200
50	6,300	1,200	300

- A. 30
B. 40
C. 50
34. A change in technology will *most likely* cause a:
- A. shift in the supply curve.
B. movement along the supply curve.
C. shift in the supply and demand curve.
35. Which of the following *most likely* represents the ‘top dog’ approach used by the leader in a ‘Stackelberg model’?
- A. The leader firm overproduces to force the follower firms to scale back their production.
B. The leader firm takes the first mover advantage by choosing its output before the follower firms.
C. The leader firm determines its profit maximizing output by assuming no change in the follower firms’ output.

36. When the demand for money balances increases without any change in interest rates and the money demand becomes infinitely elastic, the impact is *most likely* known as:
- A. liquidity trap.
 - B. demand shock.
 - C. quantitative easing.
37. For a product that is considered to be a necessity, its price and total expenditure:
- A. move in same direction.
 - B. move in opposite direction.
 - C. are not associated with each other.
38. A decrease in which of the following factors causes the AD curve to shift rightward?
- A. Taxes
 - B. Money supply
 - C. Bank reserves
39. A German company is expected to receive \$25 million from a U.S based client in 92 days. The company gathered the following information from a dealer in order to assist in hedging the foreign exchange risk.

Spot exchange rate $\$/\epsilon = 1.38$

One month forward points = -15

Three month forward points = -109

The firm could hedge the foreign exchange risk by:

- A. buying €18.12 million (selling \$25 million) at a forward rate of 1.3691.
- B. buying €34.50 million (selling \$25 million) at a forward rate of 1.3676.
- C. selling €18.12 million (buying \$25 million) at a forward rate of 1.3924.

40. Which of the following statements *most likely* represents the property of indifference curves?
- A. Indifference curves are always downward sloping.
 - B. Indifference curves intersect with each other at one single point only.
 - C. Consumers remain indifferent between higher and lower indifference curves.
41. During the economic peak of a business cycle inflation *most likely*:
- A. accelerates further.
 - B. picks up moderately.
 - C. decelerates with a lag.
42. A dealer quotes following rates:
- | | |
|--------------------------------------|---------|
| Spot exchange rate ($S_{USD/CAD}$) | = 0.89 |
| Annual risk-free rate (USD) | = 5.25% |
| Annual risk-free rate (CAD) | = 3.25% |
- Suppose the domestic currency is CAD and dealer quote of the 12-month forward rate is ($F_{USD/CAD}$) 0.9172. As compared to the annual return on a domestic only investment, the annual return on the hedged foreign investment is:
- A. 1.09% lower.
 - B. 1.12% lower.
 - C. 2.12% higher.
43. Which of the following statements is *least likely* correct regarding different profit measures?
- A. Accounting profits are always greater than or equal to economic profits.
 - B. It is not necessary for a firm earning positive economic profit to have covered its opportunity cost of resources.
 - C. For a publicly traded company, economic profit can be calculated by subtracting the required return on equity capital from the accounting profit.

44. Which of the following is the *most* appropriate reason for hyperinflation?
- A. Excess supply of goods during or after war times.
 - B. Increase in government spending without any increase in taxes.
 - C. Failure of central bank to increase money supply to support government spending.

Questions 45 through 68 relate to Financial reporting and Analysis

45. When a third party pays the suppliers of a company on its behalf, the firm's:
- A. investing cash inflows increase.
 - B. financing cash inflows decrease.
 - C. operating cash outflows increase.
46. When valuation allowance increases:
- A. net income remains unchanged.
 - B. deferred income tax expense increases.
 - C. reported deferred tax asset remains unchanged.
47. For a firm operating under U.S. GAAP, the future lease payments are *most likely* disclosed:
- A. for the first year and then in aggregate for the next 2-5 years.
 - B. on a year-by-year basis for the first two years and in aggregate for all subsequent years.
 - C. on a year-by-year basis for the first five years and then aggregated for all subsequent years.
48. Under both IFRS and U.S. GAAP, companies are required to disclose:
- A. circumstances that resulted in inventory reversals.
 - B. accounting policies applied to inventory measurements.
 - C. amount of inventory recovery due to previous write down.
49. A company's year-end net income is \$5,255,200 and common shares outstanding are 325,000. The company paid \$2,250,000 dividends on its 150,000 shares of convertible preferred and each share is convertible into 1.75 shares of its common stock. The company also paid after-tax interest of \$71,250 on its \$950,000 convertible bonds convertible into 52,000 shares. The company's diluted and basic EPS are *closest* to:
- A. \$8.32 and \$9.02 respectively.
 - B. \$8.33 and \$9.25 respectively.
 - C. \$11.84 and \$9.02 respectively.

50. Under U.S. GAAP companies are:
- A. permitted to use only the revaluation model to report identifiable intangible assets.
 - B. not allowed to capitalize the costs associated with internally created intangible assets.
 - C. allowed to report identifiable intangible assets either using cost model or revaluation model.
51. Management's commentary *must*:
- A. provide an overview of specific business lines.
 - B. highlight uncertainties that may affect the liquidity position of the company.
 - C. provide information regarding the accounting methods and policies used by management in developing financial statements.
52. A firm purchases machinery on January 1st 2012 for \$52,000. The machine's fair value is determined to be \$53,500 at the end of 2012 and \$42,700 at the end of 2013. If the firm uses the revaluation model, under IFRS, the firm will *least likely* report a:
- A. loss of \$9,300 in its income statement at the end of year 2.
 - B. revaluation surplus of \$1,500 in the equity section at the end of year 1.
 - C. revaluation loss of \$10,800 in other comprehensive income at the end of year 2.
53. In periods of falling prices and assuming no liquidation, LIFO reports the lowest:
- A. income taxes.
 - B. ending inventory.
 - C. cost of goods sold.

54. An analyst observed that the demand of Lynch Inc., a manufacturing firm has decreased, the company has relatively newer assets and the company is not making full use of its available credit lines. Based on these facts, which of the following ratios of Lynch Inc. would *most likely* be higher as compared to industry averages?

- A. Payables turnover ratio
- B. Fixed asset turnover ratio
- C. Receivables turnover ratio

55. The elements directly related to measurement of financial position *most likely* include:

- A. equity.
- B. income.
- C. capital maintenance adjustments.

56. An analyst gathered the following data from a company's financials:

CFO	\$50 million
WC changes	\$18 million
Dividends	\$7 million
Total debt	\$78 million

He obtained retained cash flow (RCF) by deducting WC changes and dividends from cash flow from operations. Assuming no capital expenditures, the company will be able to pay off its debt from cash retained in the business in approximately:

- A. 4.0 months.
- B. 1.5 years.
- C. 3.0 years.

57. Which of the following is initially recorded as a prepaid asset and then reflected as an expense over time?

- A. Advertising.
- B. Equipment.
- C. Rent expense.

58. Employing aggressive pension plan assumption can *least likely* result in:
- A. misstatement of both earnings and financial leverage.
 - B. lower pension expense and liability due to the assumption of a higher discount rate.
 - C. lower pension expense and liability due to the assumption of a higher expected return on plan assets.
59. Which of the following is typically prepared at the end of an accounting period as a first step in producing financial statements?
- A. T-accounts.
 - B. Trial balance.
 - C. General ledger.
60. Under U.S. GAAP foreign firms that prepare their financial statements in accordance with IFRS are:
- A. obligated to provide reconciliation statements.
 - B. not required to provide reconciliation statements.
 - C. required to provide details of major sections in U.S. GAAP if differences are significant.
61. In periods of falling prices and increasing inventory quantities the operating profit of a firm using the weighted average cost method will be:
- A. higher compared to a firm using the LIFO method.
 - B. lower compared to a firm using the FIFO method.
 - C. indeterminate due to increasing inventory quantities.
62. When a company writes off its uncollectible receivables, the accounting treatment *most likely* includes a decrease in:
- A. cash and an increase in the allowance for doubtful accounts.
 - B. account receivable and the allowance for doubtful accounts.
 - C. the allowance for doubtful accounts and the cash, and no change in the accounts receivables.

63. For an analyst interested in the ratio analysis of a diversified company, it is *more appropriate* to:
- A. use industry specific ratios for different lines of business.
 - B. use the weighted average ratios of the respective industries.
 - C. avoid comparing the company's ratios with industry averages.
64. Compared to an operating lease, a lessee that makes use of a finance lease will *most likely* report higher:
- A. total net income.
 - B. operating income.
 - C. cash flows from financing.
65. An analyst is comparing the financials of two firms given below:

Firm:	Reporting Standard:	Available for sale debt securities Gains/losses:
ABC	IFRS	\$6,000 gain (from exchange rate)
XYZ	U.S GAAP	\$4,500 loss (from exchange rate)

- In order to adjust the income statements, the analyst will *most likely* report:
- A. \$4,500 loss for XYZ.
 - B. \$6,000 gain for ABC.
 - C. \$1,500 gain for ABC.
66. Cruz Corp. reported \$52,480 as salary expense and \$22,000 as other operating expenses for the year ended December 2013. If the beginning and ending salaries payable are \$38,500 and \$22,670 respectively, the cash paid to the employees by Cruz Corp. is *closest* to:
- A. \$36,650.
 - B. \$46,310.
 - C. \$68,310.
67. Which of the following is *least likely* classified as a financing activity under IFRS?
- A. Payment of interest.
 - B. Repayment of debt.
 - C. Purchase of debt securities.

68. An analyst is calculating the depreciation expense for the year ended 31 December 2011. The analyst has gathered the following information:

Cost of machinery (acquired on 1 January 2011)	= £4,450,000.
Estimated residual value	= £225,000.
Remaining useful life	= 11 years.
Production in FY 2011	= 255 units.
Expected production (for remaining years)	= 2,354 units.
Productive capacity (total)	= 2,500 units.

Under units of production method, the depreciation expense reported by the analyst in FY 2011 is *closest* to:

- A. £16,568.
- B. £430,950.
- C. £453,900.

Questions 69 through 76 relate to Corporate Finance

69. Greek Lime Inc. is a small firm currently operating in Ohio and is planning a new project in Illinois. The CEO of the firm gathered the following data to estimate the project's cost of capital:

	Comparable Public Firm	Greek Lime Inc.'s Project
Market value of debt	\$220 m	\$82 m
Market value of equity	\$340 m	\$145 m
Marginal tax rate	36%	34%
Beta	1.7	

The asset beta of Greek Lime Inc. is *closest* to:

- A. 1.20.
 - B. 1.65.
 - C. 2.33.
70. A company will not be able to use higher degrees of financial leverage if its:
- A. ratio of tangible assets to total assets is lower.
 - B. ratio of long term debt to total debt is higher.
 - C. sensitivity of revenues to business cycle is below average.
71. The following data is related to Peyton Brick Inc. for the year ended June 2012.

Total units sold	= 52,000
Sale price (per unit)	= \$80
Variable cost (per unit)	= \$32
Fixed operating costs	= \$1.5 m
Interest paid	= \$600,000

The number of units Peyton sold beyond its breakeven quantity Q_{BE} is *closest* to:

- A. 8,250.
- B. 20,750.
- C. 43,750.

72. Which of the following is *least likely* a limitation of the average accounting rate of return?
- A. It is not adjusted for risk.
 - B. It ignores time value of money.
 - C. It requires complex calculations.
73. Which of the following is *most likely* an advantage of dividend reinvestment plans (DRP) to a company?
- A. Obtaining additional shares through DRPs involve no transaction costs.
 - B. DRPs promote long-term investment in the company by increasing shareholders' loyalty.
 - C. DRPs require no extra record keeping in computing gains/losses when shares are sold.
74. An analyst observed the following practices of the executive committee of Lamp Black Inc.

Exhibit 1

1.	Major portion of total compensation award includes bonuses, stock options and grants of restricted shares.
2.	Salary and perquisites awards constitute a small portion of total compensation awards.
3.	Compensation is reported as an expense in the income statement.
4.	Equity based awards vest over a series of years.
5.	Reprising of stock options is allowed.

Using the information in Exhibit 1, how many activities of Lamp Black Inc.'s executive committee are in the best interest of shareowners?

- A. 2
- B. 3
- C. 4

75. MaryMore Inc. is planning to issue bonds to finance a new project. It offers \$1,000 par 5-year, 7% semi-annual coupon payment bond. The bond is currently trading at \$1,150. The firm's current costs of preferred equity and common equity are 4% and 5.5% respectively and marginal tax rate is 34%. The firm's project cost is *closest* to:
- A. 2.43%.
 - B. 3.98%.
 - C. 11.93%.
76. Lora Inc. is planning to repurchase 0.8 million shares through borrowing. The before tax cost of borrowing is 8.07%. The current EPS of the firm is \$1.92 and the share is currently trading in the market for \$34. The firm is in a 30% tax bracket.

After the share repurchase, EPS of the firm will *most likely*:

- A. increase.
- B. decrease.
- C. remain unchanged.

Questions 77 through 88 relate to Equity Investments

77. When a market is semi-strong form inefficient current security prices:
- A. reflect information of company specific events.
 - B. do not reflect information on financial market data.
 - C. incorporate past information about prices and volumes.
78. An investor holds 500 shares of Siena Inc. for one year on margin. Both the interest on loan and dividends on shares are paid at the end of the year. The other details are as follows:

Purchase price	\$45/share
Sale price	\$42/share
Dividend	\$1/share
Commission	\$0.1/share
Leverage ratio	1.5
Call money rate	4%

The investor's return on equity (ignoring commission, interest and dividends) is *closest* to:

- A. – 10.00%.
 - B. -9.00%.
 - C. – 6.67%.
79. A firm that has compromised its current profitability to achieve a major market share is *most likely* using:
- A. offensive pricing.
 - B. defensive pricing.
 - C. predatory pricing.

80. A group of investors purchased 3 million shares of Buddies Inc., a publicly traded corporation, at a price of \$14 per share. The shares are trading in the market for \$20. The firm needs proceeds on an urgent basis for expansion purposes. This is *most likely* an example of a:
- A. PIPE transaction.
 - B. leveraged buyout.
 - C. venture capital investment.
81. An investor owns 2-year duration credit default swap (CDS) of Greenz Inc. He asked an analyst how his investment will perform if market interest rates remain the same but the credit spread of the firm widens.

The *most reasonable* response of the analyst to the investor would be that:

- A. you may benefit from an increase in the company's credit spread.
 - B. your investment value will decrease as the default probability of the firm will increase.
 - C. there will be no any change in your investment value as CDS provides protection against firm's credit spread widening.
82. An analyst gathered the following information for an index with the initial value set to 100.

Period	Price Return	Income Return
1	6.2%	1.5%
2	4.7%	2.5%
3	5.5%	3.0%

The value of the total return index at the beginning of period 3 is *closest* to:

- A. 115.45.
- B. 123.40.
- C. 125.27.

83. According to efficient market hypothesis:
- A. investors may have heterogeneous beliefs regarding asset values.
 - B. analysts assess future probabilities on the bases of recent outcomes.
 - C. abnormal returns are due to some statistical problems with analyzing the stocks.
84. Information about the arrangement of the final settlement of the trade are found under:
- A. validity instructions.
 - B. clearing instructions.
 - C. execution instructions.
85. A portfolio manager wants to sell 5 million shares of GEM Electric Power Inc. He observes that generally at the end of trading day share prices lower as many investors close their positions. The *most* suitable validity instruction for him is:
- A. good on close order.
 - B. good-till-canceled order (GTC).
 - C. immediate or cancel order (IOC).
86. An analyst gathered the following data for an equally weighted index.

Security	Beginning period		Ending Period	
	Price	Shares	Price	Shares
A	10	100	12	100
B	18	180	17	180
C	25	250	21	250

The index return over the period is *closest* to:

- A. -5.66%.
- B. -1.55%.
- C. -0.55%.

87. The return on equity and expected payout ratio of a firm is 14% and 30% respectively while investor's required return is 15%. Based on the information provided, the price-to-earnings multiple for the firm is *closest* to:
- A. 0.46.
 - B. 2.78.
 - C. 5.77.
88. A share of ELY Inc. is currently trading for \$87. An analyst calculated the estimated intrinsic value of ELY Inc.'s share to be \$102.67 by using the following data:

Most recent dividend $D_0 = \$5.5$

Growth rate $g = 12\%$

Required return = 18%

The contribution of the dividend growth assumption to the intrinsic value estimate is *closest* to:

- A. \$15.67.
- B. \$30.55.
- C. \$72.11.

Questions 89 through 94 relate to Derivatives

89. An analyst made the following statements.

Statement 1: Sellers of options in both exchange traded and OTC markets are not subject to the risk of default of buyers.

Statement 2: In contrast to forwards, futures and swaps, options do have value at the start.

The analyst is *most likely* correct with respect to:

- A. Statement 1 only.
- B. Statement 2 only.
- C. Statement 1 and Statement 2.

90. As compared to over the counter derivatives, exchange traded derivatives are:

- A. more private and less regulated
- B. less customized and less flexible.
- C. subject to a greater risk of default.

91. In an asset back securities (ABSs), which of the following tranches have the lowest expected returns?

- A. Senior tranches.
- B. Junior tranches.
- C. Mezzanine tranches.

92. Which of the following statements is *most likely* correct for a 3×9 FRA?

- A. The contract will expire in 270 days.
- B. The underlying rate will be 180 day LIBOR.
- C. The underlying loan will be settled in 90 days.

93. Which of the following strategies reduces both the overall risk and the expected return compared to simply holding the underlying?

- A. Covered call
- B. Protective put
- C. Collar strategy

94. For European call options the lower bound is either 0 or:

- A. $\left[\frac{S_0 - X}{(1+r)^T} \right]$, whichever is greater.
- B. $\left[\frac{X}{(1+r)^T} \right] - S_0$, whichever is lower.
- C. intrinsic value, whichever is greater.

Questions 95 through 106 relate to Fixed income

95. A 7-year 6% annual coupon payment bond priced at 100 of par value is trading in the market for 103. The modified duration and convexity of the bond is 6.5 and 86 respectively. The approximate return impact on the bond from 150 basis points spread widening is *closest* to:
- A. -8.78%.
 - B. -9.75%.
 - C. -10.72%.
96. An investor is choosing a money market instrument with a higher expected rate of return. Both the instruments have the same credit risks.
- i. 180-day commercial paper at a discount rate of 7.85% for 360-day year.
 - ii. 180-day bank time deposit quoted at an-add on rate of 8.15% for 365-day year.

He will *most likely* choose:

- A. bank time deposit as it offers 10 bps more in annual return than commercial paper.
 - B. commercial paper as it offers 13 bps more in annual return than bank time deposit.
 - C. bank time deposit as it offers 30bps more in annual return than commercial paper.
97. Constant yield price trajectory illustrates:
- A. that there is a constant change in price of a fixed income bond as time passes.
 - B. how the bond prices remain constant as time passes when market discount rates remain the same.
 - C. the pull to par effect on bond price trading at a premium or discount to par value.

98. When a national government runs a budget deficit, the primary source of funds for making interest payments and repaying the principal for sovereign bonds are:
- A. excess tax revenues over expenditures.
 - B. borrowing funds from interbank market.
 - C. rolling over existing debt into new debt.
99. Callable but can be called every October 10 one year from now till maturity.

The call provision is *most likely* a (n):

- A. Bermuda call.
 - B. European call.
 - C. American call.
100. Which of the following statements is *most likely* correct regarding credit spreads?
- A. During financial crises, a flight to quality can cause benchmark yields to rise.
 - B. More thinly traded corporate bonds have much narrower difference between the bid and offer prices.
 - C. An unexpected credit downgrade on a corporate bond can result in greater credit as well as liquidity risk.
101. Which of the following source of financing is *least expensive* for a highly rated company?
- A. Bilateral loan
 - B. Syndicated loan
 - C. Bond issued in financial market.
102. An investor purchased a 2-year bond at 1,050 with par value of 1,000 in a country, which lacks an issue premium tax provision in its tax code. He has not paid or deducted any tax on that bond for two years. Now when the bond is redeemed at maturity he can:
- A. declare a capital loss of 50.
 - B. declare a capital gain of 50.
 - C. deduct 25 from his taxable income for year-2 only.

103. The internal rate of return on the cash flows assuming the payments are made on the scheduled dates is referred to as:

- A. true yield.
- B. street convention.
- C. government equivalent yield.

104. A bond portfolio consists of following three fixed rate bonds trading in different markets.

	Time-to-maturity	Coupon	Yield-to-maturity
Bond A	6	7%	9
Bond B	4	8%	10
Bond C	5	5%	10

The bond with the *lowest* convexity would be:

- A. bond A.
- B. bond B.
- C. bond C.

105. Which of the following bond structures attracts the more conservative classes of investors?

- A. Puttable bond
- B. Callable bond
- C. Option-free bond

106. At the time of financial crises banks:

- A. reduce funding to other banks as interbank deposits are unsecured.
- B. increase funding to other banks and hoard less liquidity in anticipation of expected payoffs.
- C. increase interbank funding as corporations' use of credit lines decrease.

Questions 107 through 112 relate to Alternative Investments

107. A manager seeking to generate returns from a merger arbitrage will *most likely*:
- A. sell the stocks of target company and buy the stocks of the acquiring company.
 - B. buy sufficient equity with an attempt to have control on the company.
 - C. buy the stocks of target company and take a short position in the acquiring company.
108. Jerry invested \$15 m in EV Fund of funds (EV FOF) that invested 75% with Tsar Hedge Fund (THF). EV FOF and THF have “1 & 10” and “2 & 20” fee structures respectively. Management fees are calculated based on beginning of period capital and both management and incentive fees are computed independently. THF earned 17% annual return before management and incentive fees. The total fees paid by Jerry is *closest* to:
- A. \$435,038.
 - B. \$856,500.
 - C. \$1,134,000.
109. A hedge fund that uses “Reporting NAV” *most likely* represents NAV:
- A. adjusted for liquidity discounts based on quoted market price.
 - B. based on quoted market price and does not incorporate liquidity discounts.
 - C. adjusted for liquidity discounts based on the size of the position held relative to the total amount outstanding.
110. For valuing a large and mature private company, the multiple *most* commonly used under the market or comparable approach is:
- A. Revenue multiple.
 - B. EBITDA multiple.
 - C. Net income multiple.
111. Returns to commodity investing are based on:
- A. income stream.
 - B. change in prices.
 - C. both income stream and change in prices.

112. Which of the following risk measure take into account in its measurement the low correlation of alternative investments with traditional investments?

1. Sharpe ratio
2. Sortino ratio
3. Value at risk
4. Safety-first risk

- A. None.
- B. 1 and 3 only.
- C. 1, 3 and 4 only.

Questions 113 through 120 relate to Portfolio Management

113. With respect to portfolio management process construction of a client's portfolio *most likely* occur in the:

- A. planning step.
- B. execution step.
- C. feed back step.

114. An analyst made the following statements regarding passive and active portfolios.

Statement 1: Passive portfolios are based on the assumption of unbiased market prices.

Statement 2: In an actively managed portfolio undervalued assets are over weighted relative to the market weight in the benchmark index.

The analyst is *most likely* correct with respect to:

- A. Statement 1 only
- B. Statement 2 only.
- C. .both Statement 1 and Statement 2.

115. Wesley is preparing the IPS of Aaban Masri. Masri prohibits Wesley from investing in the shares of:

- GreenX Inc. for certain periods in the year as he is director at GreenX and cannot trade shares before financial results are published.
- Casinos and bonds due to his compliance with Islamic law.

In which section of the IPS, will Wesley *most likely* document Masri's instructions regarding:

GreenX Inc.?

- A. Unique circumstances
- B. Legal and regulatory factors
- C. Legal and regulatory factors

Casinos & bonds?

- Unique circumstances
- Unique circumstances
- Legal and regulatory factors

116. Which of the following *best* describes the outcome of the portfolio approach?
- A. Portfolios generally reduce risk more than they increase returns.
 - B. Portfolio diversification provides better risk-reduction benefits during severe market turmoil.
 - C. The standard deviation of an equally weighted portfolio can be greater than the average of the standard deviation of the individual components.
117. The sensitivity of the derivative price to a small change in the value of the underlying asset is called:
- A. delta.
 - B. vega.
 - C. gamma.
118. Which of the following *least* describes the implications of separation theorem? Under separation theorem:
- A. optimal risky portfolio is same for all investors.
 - B. investors cannot separate their risk aversion from choice of market portfolio.
 - C. optimal portfolio selection is separated into investing and financing decisions and both are independent of each other.
119. Tom Dixon, CFA wrote the following statement in his article:
- “An investor’s expected income and time horizon helps in determining his willingness to take risk and his level of wealth relative to liabilities helps in determining his ability to take risk.”
- Dixon is *most likely* correct with respect to:
- A. his statement.
 - B. factors determining the ability to take risk.
 - C. factors determining the willingness to take risk.

120. Which of the following is not one of the principles on which the strategic asset allocation is based?
- A. Similar assets have similar exposures to certain sets of systematic factors.
 - B. Changes in portfolio value over the long term are primarily determined by portfolio's systematic risk.
 - C. When an asset class or subset of an asset class represents an efficient market, passive management is preferred.