2026
Level 3 Core - Formula Sheet

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Volume 1: Asset Allocation

LM1: Capital Market Expectations, Part 1: Framework and Macro Considerations

(Note: there are no calculate LOS, however, the following formulas may help with 'describe', 'explain', and 'discuss' keywords)

Aggregate trend growth =

- Growth from labour inputs, consisting of:
  - Growth in potential labour force size
  - Growth in actual labour force participation
- Growth from labour productivity, consisting of:
  - Growth from increasing capital inputs
  - Growth in total factor productivity

Aggregate market value of equity:

$$V_t^e = GDP_t \times S_t^k \times PE_t$$

$$E(R^e) = V_t^e + D_t$$

where:
V_t^e = Aggregate market value of equity
GDP_t = the level of nominal GDP
S_t^k = the share of profits in the economy (earnings/GDP)
PE_t = the P/E ratio
D_t = dividends

The Taylor Rule:

$$i^* = r_{neutral} + \pi_e + 0.5\left(\hat{Y}_e - \hat{Y}_{trend}\right) + 0.5(\pi_e - \pi_{target})$$

In terms of the real, inflation-adjusted, target rate:

$$i^* - \pi_e = r_{neutral} + 0.5\left(\hat{Y}_e - \hat{Y}_{trend}\right) + 0.5(\pi_e - \pi_{target})$$

where:
i* = the target nominal policy rate
$r_{neutral}$ = the real policy rate that would be targeted if growth is expected to be at trend and inflation on target
$\hat{Y}_e$ = expected GDP growth rate
$\hat{Y}_{trend}$ = the observed GDP trend growth rate
π_e = the expected inflation rate
π_{target} = the target inflation rate