

Question 1 of 11

TOPIC: EQUITY

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Edwin Lister, an analyst at Connelly Investments, is analyzing Tuck Meal Foods. The company is headquartered in Minnesota, USA, and specializes in food ingredients such as spices, nuts, cocoa, and coffee.

Lister studies the impact of inflation on Tuck Meal's 2022 sales volume. He designs three alternative scenarios each of which predicts how the company will react to inflationary pressure. Exhibit 1 shows Tuck Meal's financial results for the most recent financial year (2021) while Exhibit 2 shows the estimates of input prices, volume growth and pricing under the three scenarios.

Exhibit 1

Sales	\$550,420
Cost of goods sold	\$388,940
Gross profit	\$161,480
Gross profit margin	29.34%

Exhibit 2

	Scenario A	Scenario B	Scenario C
<i>Price increases for revenues</i>	0.0%	5.0%	10.0%
<i>Volume growth</i>	12.0%	8.0%	- 17.0%
<i>Total revenue growth</i>	12.0%	13.4%	- 8.7%
<i>Input prices increase</i>	10.0%	10.0%	10.0%

Lister would also like to estimate the impact on gross profit margin if Tuck Meal is unable to pass on the 10% inflation in input costs to its customers. For his analysis, Lister relies on the data in Exhibit 2 and assumes the same financial results hold for 2022.

Lister concludes his analysis by comparing Tuck Meal's operating performance and financial position to its competitors. He decides to rely on return on invested capital (ROIC) and forecasts that the measure will demonstrate a rising trend in the present inflation scenario based on past observations of how this measure reacted to inflation.

Part 1 of 4

If Scenario C materializes and assuming all cost of goods sold are variable, the change in gross profit margin from that reported in 2021 is *closest* to:

- A. - 50%
- B. - 23%
- C. 0%.

Part 2 of 4

Considering the data in Exhibit 2, which of the following scenarios *most likely* assumes that the demand for Tuck Meal's products is relatively price inelastic? Scenario:

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

Part 3 of 4

Using the data in Exhibit 1, if Tuck Meal is unable to pass on the inflation to its customers, the resulting gross profit margin is equal to:

- A. 22.27%.
- B. 29.34%.
- C. 35.76%.

Part 4 of 4

Which of the following reasons *most likely* supports Lister's preference for the ROIC measure?

- A. The degree of competitive advantage secured by Tuck Meal can be assessed.
- B. Tuck Meal's degree of financial leverage can be compared to its competitors.
- C. The underlying profitability of companies following different tax regimes can be compared.

Question 2 of 11

TOPIC: ECONOMICS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Greenwich Ryerson (GR) is a U.S. based provider of information technology services. Three months ago, GR entered into a three-month forward currency contract to hedge a long exposure to the South African Rand (ZAR) by selling ZAR 50 million forward against the USD at an all-in forward price of USD/ZAR 8.7892. GR would now like to roll its position using a currency forward swap. GR's currency advisor has summarized spot and forward quotes for the USD/ZAR currency pair (Exhibit).

Exhibit
Spot and Forward Quotes (Bid-Offer)

Maturity	Spot or Forward Points
Spot (USD/ZAR)	8.7890/8.7895
One month	-7.5/-6.5
Three months	-18.9/-15.8
Six months	-27.3/-22.2

Part 1 of 4

The current all-in offer rate for the purchase of ZAR against the USD in six months' time is *closest* to:

- A. 8.7863.
- B. 8.7870.
- C. 8.7873.

Part 2 of 4

Which of the following statements is *most likely* correct regarding the bid-offer spread for forward contracts?

- A. Forward and spot bid-offer spreads are influenced by similar factors.
- B. Quoted forward points need to be scaled according to the maturity of the contract.
- C. In a forward currency swap, an average of the bid and offer forward points will be added to the mid-market spot rate.

Part 3 of 4

Which factor will *most likely* affect forward bid-offer spreads but not spot bid-offer spreads?

- A. Counterparty credit risk.
- B. The underlying currency pair.
- C. Relationship between the client and dealer.

Part 4 of 4

The cash flow realized by GR on the settlement date is *closest* to an:

- A. inflow of USD 194.17.
- B. inflow of USD 2,500.00.
- C. outflow of USD 2,500.00.

Question 3 of 11

TOPIC: DERIVATIVES

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Skylar Jones is a currency derivatives specialist at Lakehouse Consultants, an investment advisory firm. Jones is providing consultancy services to Smart Developers, a property development firm based in Australia, and to the plan sponsor of the Ivanhoe pension fund.

Smart Developers is seeking to expand its operations to the UK and will require £30 million for this project. However, the development firm can obtain financing at a lower rate locally. Smart's chief finance officer contacts Jones who advises the firm to enter into a 1-year pay fixed currency swap denominated in £30 million with a quarterly settlement frequency. The current exchange rate is £0.62/A\$ and the 3-month risk-free rates are 0.5% and 0.7% in Australia and the UK, respectively.

Part 1 of 4

At swap initiation, Smart Developers will receive an amount from the counterparty which equals:

- A. £30.00 million.
- B. A\$18.60 million.
- C. A\$48.39 million.

Part 2 of 4

The amount of interest received by Smart Developers at each settlement period is equal to:

- A. £52,500.
- B. A\$60,483.
- C. A\$24,194.

Part 3 of 4

In contrast to an interest rate swap, a currency swap is characterized by:

- A. a single swap rate.
- B. zero notional principal values at initiation.
- C. greater counterparty risk exposure towards swap expiration.

Part 4 of 4

How are payments handled in a currency swap?

- A. Payments are netted and made in a single currency.
- B. Payments on each leg of the swap are in different currency units and are not netted.
- C. Only the party with the positive balance makes a payment at the end of the swap term.

Question 4 of 11

TOPIC: FINANCIAL STATEMENT ANALYSIS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Vertex Innovations, Inc. (VII) is a leading player in the renewable energy sector. With over 25,000 employees currently employed with the company, pension obligations have steadily increased year after year. To meet their pension expectations, VII provides its employees with the option to choose between a defined contribution plan and a defined benefit plan. Employees have the option to choose the investment plan that suits them best.

Individual accounts are created for each plan participant under the defined contribution plan, with both the employer and the employee contributing quarterly. Under the defined benefit plan, only the employer is required to make contributions to the scheme. The net present obligation of a defined benefit plan is calculated using the projected unit credit method.

The firm is revamping its executive compensation package and intends to implement a new share-based compensation plan that will incentivize top-performing managers and technical staff by giving them a stake in the company's success. The board, headed by Chairman Laura Williams, and supported by CFO Raj Mehta, is preparing to present the new "2025 Sustainable Growth Incentive Plan" to the shareholders. The plan puts a significant emphasis on share-based compensation to align executives' efforts with the company's long-term goals and shareholder value.

As they prepare for the upcoming shareholder meeting, they ponder how the proposed plan might influence executive behavior and whether the incentives are structured to promote the sustainable growth of Vertex Innovations, considering the complexities involved in striking the right balance between risk and reward inherent in such schemes.

Part 1 of 4

How does VII *most likely* fund its obligations for its defined benefit plan?

- A. By contributing to a pension trust.
- B. Through periodic employee contributions only.
- C. The company does not fund DB plan obligations.

Part 2 of 4

What is the nature of an employee's future benefit under a DC plan at VII?

- A. The amount of the future benefit is defined and guaranteed by the company.
- B. The future benefit depends on contributions and the investment performance of plan assets.
- C. The future benefit is based on a formula involving length of service and final year's compensation.

Part 3 of 4

Which factor contributes to the complexity of share-based compensation?

- A. Fluctuating stock market conditions
- B. Guaranteed cash payouts to employees
- C. Reduced influence over company decision-making by employees

Part 4 of 4

Which of the following is an advantage of share-based compensation over cash compensation?

- A. Reduced liquidity concerns for employees
- B. Guaranteed short-term financial gain for employees
- C. Enhanced alignment of employee interests with shareholders

Question 5 of 11

TOPIC: ALTERNATIVE INVESTMENTS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Smart Home Limited (SH) is a company based in United States which specializes in manufacturing smart household equipment. The assembling of finished product is outsourced to an assembling unit (AU) in China. Smart home limited is currently negotiating the purchase of assembling unit with its management and the deal is likely to be a friendly takeover. However, the regulations of merger and acquisition in China pose some risks for the deal. Special regulations have to be followed if the acquirer is a foreign investor and a number of other forms have to be filled. In case of a public company, the merger and acquisition (M&A) related activities require approval from regulatory bodies. The acquirer is required to present 3 years audited financial statements and also a securities valuation report.

Smart Home Limited will go for share for share acquisition with every 1 share of Smart home for 2 shares of assembling unit. The share prices were \$55 and \$15 for acquirer and target firm, respectively. The hedge fund manager bought 20,000 shares of AU and short sell 10,000 shares of SH. With the announcement of takeover, the target's share price rose by \$4 and acquirer's share price declined by \$2.

Part 1 of 4

Which of the following statements is *least likely* a risk of cross border acquisition?

- A. Anti-trust scrutiny
- B. Wider merger spreads
- C. Government approvals

Part 2 of 4

The spread earned by the manager, if the deal becomes successful will be equivalent to?

- A. 50,000
- B. 150,000
- C. 250,000

Part 3 of 4

If the deal becomes unsuccessful, the loss will be equivalent to?

- A. 50,000
- B. 100,000
- C. 150,000

Part 4 of 4

The deal's return profile is similar to:

- A. riskless bond + long put option
- B. riskless bond + short call option
- C. riskless bond + short put option

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TOPIC: PORTFOLIO MANAGEMENT

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Dave Gilbert is a portfolio manager and economic analyst at Western Alliance, a wealth management firm operating in Regine, a country with an emerging market. In an effort to diversify his clients' holdings, Gilbert has decided to allocate fixed-income securities to their portfolios. He decides to consider risky corporate bonds as potential asset classes and identifies four bond issues each with a different maturity (Exhibit 1).

Prior to allocation, Gilbert decomposes the value of each issue into two components, the risk neutral present value and discount for risk. The latter represents the covariance between the intertemporal rate of substitution and the future price of the investment one year from today.

Exhibit: Potential Bond Issues for Client Portfolios

Bond Issue	Risk Neutral Present Value*	Discount for Risk*
A	0.8943	0.045
B	0.9021	0.061
C	0.7654	- 0.034
D	0.8993	0.000

*Per \$1 of Par Value

After collecting the data in the exhibit, Gilbert aims to address the following questions:

Question 1: Which bond issue carries a positive risk premium?

Question 2: Which bond issue can be classified as a one-period default-free bond?

Question 3: Which bond issue will be least suitable for those investors who expect their labor income to shrink in the future due to poor economic conditions?

Erin Poninski, an intern at Western Alliance, is assisting Gilbert in evaluating potential securities. Poninski asked Gilbert the following question about default-free interest rates and economic growth.

“Is real risk-free rate is positively related to real GDP growth and the volatility of real GDP growth?”

Part 1 of 4

The *most* appropriate response to Question 1 is bond issue:

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

Part 2 of 4

The *most* appropriate response to Question 2 is bond issue:

- A. A.
- B. C.
- C. D.

Part 3 of 4

The *most appropriate* response to Question 3 is bond issue:

- A. B.
- B. C.
- C. D.

Part 4 of 4

The *most appropriate* response to the Poninski's query is that real risk-free rate is:

- A. positively related to real GDP growth and the volatility of real GDP growth.
- B. negatively related to real GDP growth and the volatility of real GDP growth.
- C. positively related to real GDP growth and negatively related to the volatility of real GDP growth.

Question 7 of 11

TOPIC: CORPORATE ISSUERS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Capulet is a research firm specializing in equity investments and is headquartered in New York. Equity markets covered by analysts at Capulet include emerging, non-U.S. developed, and U.S. markets.

Rupert Vazquez, CFA is one of Capulet's senior research analysts covering emerging markets. For his present research assignment, Vazquez is attempting to determine the equity risk premium for securities traded in Homali, an emerging economy situated in Northern Africa. The Homalian equity market is newly established and does not have a proper functioning trading platform. Any foreign investors seeking Homalian investments will additionally face significant political risk, which provides the potential to earn high returns. Vazquez has decided to derive a local equity risk premium using historical estimates. He justifies his decisions using three arguments.

Argument 1	Historical estimates can be readily used to derive risk premium estimates for the purposes of my analysis.
Argument 2	The method is based on objective data.
Argument 3	Given the harsh and uncertain political climate, historical estimates will allow for scenario analysis to be conducted, using different parameter estimates, to help produce a range of premium estimates.

Vazquez next collects relevant historical market data to develop a historical risk premium estimate for local investments in Homali (Exhibit 1).

Exhibit 1: Homali Market Data: 2000 - 2022

Proxy equity index	Developed market-value weighted index (comprising of fifteen countries)
Time period for computing the estimate	2000 – 2022 (22 years)
Risk-free return proxy	20 Year U.S. government bonds
Type of risk premium to be calculated	Compounded annual excess returns of local equities over the 20 Year U.S. government bond yield

James Devos, an analyst at Capulet, specializes in equity securities in international markets. Currently, Devos is assessing the country risk premium (CRP) of Nassai Corporation, a company that operates solely in a developing country.

Erica Morris, CFA is Capulet's developed market research analyst, who is evaluating potential equity risk premiums on stocks of a Japanese automobile manufacturer. Morris intends to use the Constant Growth Dividend Discount Model (DDM) estimate the expected premium for the manufacturer. To facilitate this estimation process, Morris has gathered relevant information as shown in Exhibit 2.

Exhibit 2

Japan	
Nikkei 225 total dividends paid*	175.59
Nikkei 225 index current price level	9,556.00
Japanese long-term average earnings growth rate (%)	2.54
10-year Japanese government bond yield (%)	1.34

*Aggregate forecasted dividends for the following year

Which of Vazquez's arguments support the use of historical estimates to formulate risk premium estimates for an investment made in Homali?

- A. 1
- B. 2
- C. 3

Part 2 of 4

Using the information in Exhibit 1, the issues associated with the data collected by Vazquez *least likely* include:

- A. index representativeness.
- B. nonstationarity of returns data.
- C. appropriateness of risk-free return proxy used.

Part 3 of 4

The most suitable approach for Devos to estimate the CRP of Nassai is:

- A. GCAPM
- B. ICAPM
- C. Sovereign yield approach

Part 4 of 4

The equity risk premium calculated by Morris is *closest* to:

- A. 3.03%
- B. 4.37%
- C. 5.68%

Question 8 of 11

TOPIC: FIXED INCOME

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Laura Peterson is the senior fixed income manager at Leopard Limited, a portfolio management firm. She is attempting to explain to her subordinate, Clark Marshall, how the binomial model can be applied to the valuation of fixed-income securities. Peterson has drawn a list of objectives, which she intends to achieve during the discussion.

Objective 1	Value a 5% annual coupon-paying option-free bond using the binomial model.
Objective 2	Determine the impact of changing volatility on forward rates.
Objective 3	Determine what calibrating an interest rate tree implies for arbitrage profits.
Objective 4	Compare the valuation of a bond issue using spot rates to that performed with a binomial interest rate tree.

To achieve the first objective, Peterson constructs a binomial interest rate tree using one-, two-, and three-year spot rates of 3%, 6%, and 8% respectively (Exhibit 1). A 10% volatility assumption is used for the analysis.

After deriving the binomial interest rate tree, Marshall asks his supervisor how the model can be used to value the subject bond. Using the rates in Exhibit 1, Peterson tasks her subordinate with valuing the bond issue (Objective 1). Exhibit 2 summarizes the results of his efforts.

Exhibit 1: Binomial Interest Rate Tree

Year 0	Year 1	Year 2
		Node 3-1
	10.254%	
3.000%		Node 3-2
	8.395%	

Exhibit 2: 5% Annual Coupon-Paying Bond Value Derived Using the Binomial Interest Rate Tree

Year 0	Year 1	Year 2
		PV = 90.882 Coupon = 5
	PV = 87.994 Coupon = 5	
91.962		PV= 93.153 Coupon = 5
	Node 1-2: PV =? Coupon = 5	
		PV = 95.098 Coupon = 5

The value of the bond at Node 1-2 (Exhibit 2) is *closest* to:

- A. 86.84.
 - B. 91.45.
 - C. 96.45.
-

Part 2 of 4

The process of interest rate tree calibration will *most likely* result in the implied opportunities for arbitrage:

- A. increasing.
 - B. decreasing.
 - C. remaining the same.
-

Part 3 of 4

In contrast to the valuation of option-free bonds using spot rates, the binomial interest rate tree will produce values which are:

- A. lower.
 - B. higher.
 - C. the same.
-

Part 4 of 4

The rate at Node 3-1 is equal to:

- A. 11.508%.
- B. 12.718%.
- C. 15.534%.

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TOPIC: EQUITY

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Time Corporation has been in the watch making business since 1932. The watchmaker was founded by brothers Earl and Jeremy Montessori. The corporation is now managed by Derek Montessori, who has inherited the business as part of his deceased father's estate.

Ownership of the corporation is limited to immediate and distant family members. The firm prefers to keep the business close knit and each family member is responsible for managing corporate affairs in addition to his/her ownership position. Time Corporation has never applied for a public listing in the past but is considering doing so in the future. The corporation is an established watchmaker in the U.S. with a high level of expertise.

Nicole Jones is the CEO of a large manufacturing firm with operations worldwide. The firm is considering the purchase of a private entity, Vibrant Manufacturers Inc (VMI) that has recently been put up for sale by its owners. VMI targets a niche market where it has just begun producing and distributing its product. Since the firm's product is unique, Jones believes that it has the potential to operate as a large successful firm sometime in the future. However, the entry of new competitors and changes in the industry's structure may erode value and cause profit margins to diminish.

Part 1 of 4

Given the present circumstances of Time Corporation, which of the following factors will *most likely* categorize the watchmaker as a private equity corporation?

- A. Agency issues
- B. Reduced marketability of equity interests
- C. Pressure to achieve above-average returns for shareholders

Part 2 of 4

Based solely on its stage of development and maturity, which of the following valuation approaches is *most* suitable for valuing Time Corporation?

- A. Income approach
- B. Market approach
- C. Asset-based approach

Part 3 of 4

Which approach to private company valuation would be *most* appropriate to value Vibrant Manufacturers Inc. (VMI)?

- A. Income approach.
- B. Market approach.
- C. Asset-based approach.

Part 4 of 4

Which of the following approaches *most likely* values an asset as the present discounted value of the income expected from it?

- A. Income approach.
- B. Market approach.
- C. Asset-based approach.

Question 10 of 11

TOPIC: ETHICAL AND PROFESSIONAL STANDARDS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Alpha and Beta Associates (A&B) is a small U.S. based investment management firm that provides asset management services to private wealth clients. Ryan Becker is the chief investment officer (CIO) at A&B who oversees a team of portfolio managers and research analysts at the firm. Becker has just assigned two clients to Adam Levin, a portfolio manager.

When Levin reviewed the clients' IPS, he determined that Client A was in the later stage of his life and wanted to minimize risk and increase cash flow certainty. Client B, on the other hand, was young, had no dependents, and had a job in a stable industry. After a comprehensive analysis of the clients, and a meeting with each of them, Levin made the following statements to the clients with regards to appropriate investment opportunities:

Client A: "Since your risk tolerance is low you should shift a portion of your investments from equity to bank-sponsored fixed certificates of deposit. This will ensure that your principal is 'guaranteed' up to the insured limit."

Client B: "Even though you can tolerate significant risk, I would still advise you to invest at least a portion of your investment in agency CMOs, like 'interest- only strips'. These derivatives are 'guaranteed' by the U.S. government and hence, limit your risk."

Levin is evaluating the future of the technology sector and is trying to pick stocks that would promise above-average returns. For this, he followed business news and read publications in financial and technology journals. Levin recently read an article published in 'The Capital Markets'. The article was written by Walter Laws, a financial journalist and a technology industry analyst. The article stated that technology stocks were going to outperform the market over the next quarter, and that this trend was expected to continue in the near future. Levin decided to use this information in his own paper, so he contacted Laws' firm to get a copy of the original article. He then included the complete study in his paper and cited only Walter Laws.

After writing his paper, Levin met with Becker to discuss the future of the utilities sector. Levin knew that Becker is a senior analyst and has gained considerable trust and respect in his field. During a discussion with Levin, Becker stated that due to changes in the market and industry structure, he believes the major utilities giants will see a drastic drop in earnings in the coming quarter. Becker continued by stating that he was going to change his 'buy' recommendation to 'sell' and was going to express his opinion in an interview on a global news channel the next day. After his talk with Becker, Levin decided to ask his brother, who worked in the utilities industry for ten years, to advise him on buying or selling utilities stocks. He stated that Levin should follow the 'sell' recommendation, since he believed that the industry was going to see a downfall. Levin quickly sold 10,000 utilities shares that he held in his own portfolio.

Levin is responsible for the management of two equity funds: The Beta Fund and The Equatic Fund. Both funds have 5% of their worth invested in the stock of QUIN Technologies, but their investment guidelines indicate this to be an excessive amount. Because QUIN's stock has low liquidity in the stock market, Levin decided to trade portions of the stock back and forth between the two funds so as to increase liquidity. Due to his trading, Levin managed to bring the amount invested within the guidelines of the two funds.

With respect to his comments to his clients, is Levin *most likely* in violation of the Standard I(C) 'Misrepresentation' of the Standards of Professional Conduct?

- A. No.
- B. Only with respect to Client A.
- C. Only with respect to Client B.

Part 2 of 4

With respect to the inclusion of the article in his paper, is Levin *most likely* in violation of Standard I(C), Misrepresentation?

- A. No.
- B. Yes, because he did not mention 'The Capital Markets' in references.
- C. Yes, because he did not make efforts to determine whether the study was comprehensive and not misrepresented.

Part 3 of 4

With respect to trading utilities shares, did Levin violate Standard II(A), Material Nonpublic Information?

- A. No.
- B. Yes, because he traded on Becker's advice before it became public.
- C. Yes, because he traded on his brother's advice before it became public.

Part 4 of 4

With respect to the Beta and Equatic Funds, has Levin *most likely* violated Standard II(B), Market Manipulation?

- A. Yes.
- B. No, because he was working in the best interest of his clients.
- C. No, because he did not manipulate the market with the intentions of profiting from the trading.

Question 11 of 11

TOPIC: PORTFOLIO MANAGEMENT

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Wesley Ragland is an equity analyst at Fadel Capital, an investment advisory company in the United States. Ragland specializes in evaluating equity strategies and heads the company's quantitative research team. Primal Capital Fund, one of Fadel Capital's clients, has asked Ragland to assist in creating a new investment strategy to provide superior risk-adjusted absolute returns for his clients, and examine the risk and return profiles of the current approach using backtesting methods.

Ragland explains how his business employs backtesting techniques to develop successful investing strategies during a discussion with Loretta Brady, CEO of Primal Capital Fund. Loretta asks the following questions:

Question 1: "Can backtesting approximate the real-life investment process?"

Question 2: "Financial data often contains structural breaks. Which type of backtesting technique is suitable for assessing the strategy's performance in different structural regimes?"

Ragland instructs his assistant Elmer Kelly to prepare the backtesting strategy framework to evaluate the performance of the strategy. The exhibit below is the framework prepared by Kelly.

Exhibit

Goal	Superior risk-adjusted absolute return
Hypothesis	Performance of value investing stocks based on earnings yield factor
Specifications of Key Parameters	<ul style="list-style-type: none">• Investment universe - Russel 3000• Return Definition - All investment returns are in the U.S. dollar.• Rebalancing Frequency - Monthly including transaction costs.• Start and end date - June 2001 to June 2021

Part 1 of 4

Which of the following is the *most appropriate* response to Loretta's Question 1?

- A. No, backtesting cannot approximate the real-life investment process.
- B. Yes, the backtesting approach fully accounts for the dynamic nature of financial markets by including extreme upside and downside risks that have not occurred before.
- C. Yes, backtesting approximates the real-life investment process by using historical data to evaluate whether a strategy would have produced desirable results.

Part 2 of 4

The *most appropriate* response to Loretta's Question 2 is:

- A. Historical scenario analysis
- B. Rolling windows backtesting
- C. Backtesting multifactor models

Part 3 of 4

Based on Exhibit, which of the following will *least likely* be a concern, if Kelly chooses to backtest the investment strategy using daily rebalancing frequency?

- A. Transaction costs will be increased
- B. Price data will likely be biased by bid-ask spreads
- C. The likelihood of the structural breaks occurring in the data will be increased.

Part 4 of 4

All else equal, which of the following will most likely be correct, if Kelly chooses to backtest the investment strategy using the start date of June 2011 rather than June 2001 in Exhibit?

- A. Non-stationary data problems will be increased.
- B. The usefulness of backtest findings may be decreased.
- C. Higher statistical confidence in the results will be achieved.