

### Question #1 of 27

Question ID: 1716270

Shauna Gebay manages the investments of a large family office and several individually managed accounts, and is considering changing their asset mixes to include a considerable portion in alternative investments. However, she believes that alternative investments are not appropriate for the family office, and only liquid, public alternative investments are appropriate for individually managed accounts. She is correct with respect to:

- A) individually managed accounts only.
- B) neither the family office nor individually managed accounts.
- C) both the family office and individually managed accounts.
- D) the family office only.

#### Explanation

Because family offices have long time horizons and often no immediate liquidity needs, it is appropriate to include alternative investments in their asset mix. Because individually managed accounts receive some tax benefits, the range of investments is generally limited to more liquid, public alternative investments only.

(LO 1.1.1)

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### Question #2 of 27

Question ID: 1716273

Which of the following factors is the least likely consideration in determining asset allocation percentages?

- A) Absolute allocation size.
- B) Relative allocation size.
- C) Time horizon.
- D) Liquidity.

#### Explanation





Determining asset allocation percentages, including caps and floors, primarily considers absolute asset allocation size, relative asset allocation size, and liquidity. (LO 1.1.2)

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### Question #3 of 27

Question ID: 1716264

Andrea Kim is a pension fund consultant who provides expert advice to a wide range of pension funds. For which of these pension funds is she least likely to recommend privately placed alternative investments?

- A) Private defined contribution fund. 
- B) Private defined benefit fund. 
- C) Individually managed account. 
- D) National pension fund. 

#### Explanation

Privately placed alternative investments are not usually available to individually managed accounts.

Although private defined contribution funds have a smaller range of available investments compared to national funds and defined benefit funds, they may invest in alternative investments and would not likely include any restrictions on privately placed alternative investments.

National pension funds and private defined benefit funds are generally large and have long-term horizons; therefore, the range of investments used is wide and would not likely include any restrictions on privately placed alternative investments.

(LO 1.1.1)

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### Question #4 of 27

Question ID: 1716283

Voting proxies that are related to commingled vehicles such as mutual funds are typically the responsibility of:

- A) clients. 
- B) the discretionary adviser. 
- C) the investment manager. 
- D) the custodian. 

#### Explanation





Proxy voting for fund-level issues involving mutual funds or other commingled vehicles is the responsibility of the organization or discretionary adviser. (LO 1.1.4)

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### Question #5 of 27

Question ID: 1716268

Which of the following statements regarding family offices is most accurate?

- A) Family offices are established to serve a single family. 
- B) Family offices have similar overall goals. 
- C) Wealth management is the most common goal of family offices. 
- D) The main source of capital for a family office is legacy wealth. 

#### Explanation

For single-family offices, wealth management is the most common goal.





The goals of family offices can vary quite significantly. In some instances, a family office serves a single person or family. However, it can also be set up to serve multiple families—a multifamily office. Two common sources of capital for family offices are capital spun off from an operating company and legacy wealth that has been inherited from family members of prior generations. (LO 1.1.1)

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### Question #6 of 27

Question ID: 1716262

Which of the following statements about individually managed accounts is the least accurate?

- A) They are subject to regulations that limit the available set of investments. 
- B) Available assets typically include private alternative investments. 
- C) Employees are in full control of the asset allocation. 
- D) Individually managed accounts benefit from tax advantages. 

#### Explanation

Individually managed accounts benefit from tax advantages, which limits the range of available investments and typically excludes privately placed alternative investments. Employees control how the funds are invested. (LO 1.1.1)

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### Question #7 of 27

Question ID: 1716282

A primary function of an outsourced chief investment officer (OCIO) is to:

- A) provide security safekeeping. 
- B) proactively recommend investment strategies. 

C) be responsible for hiring and firing of managers. 

D) make recommendations on areas delegated by the board. 

### Explanation

The OCIO is similar in function to the investment adviser but with greater fiduciary responsibilities, including shifting asset allocations and making decisions on hiring/firing of managers.

Security safekeeping is provided by the custodian. Recommending investment strategies is the primary function of the investment adviser. The investment/finance committee makes recommendations on areas delegated by the board. (LO 1.1.4)

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### Question #8 of 27

Question ID: 1716272

When establishing the strategic asset allocation, the expected return on asset classes is calculated as:

A) short-term real riskless rate + expected inflation + risk premium. 

B) real GDP growth rate + expected inflation + asset correlation. 

C) short-term real riskless rate + asset correlation. 

D) real GDP growth rate + risk premium. 

### Explanation

The expected return on asset classes is calculated as: short-term real riskless rate + expected inflation + risk premium.

The short-term real riskless rate is less than the real growth rate. Asset correlations are one of several important factors when calculating the risk premium (other factors include volatilities and risk exposures). (LO 1.1.2)

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### Question #9 of 27

Question ID: 1716277

Mary Parks is an individual investor who works for a credit rating agency analyzing financial institutions, primarily banks. Because of her access to confidential and sensitive information, she is prohibited from investing in bank stocks. In addition, Parks is unable to invest in several private equity (PE) securities given their very high due diligence costs. These two constraints would most appropriately be classified as:

Prohibition Against Bank Stock Investing

High Due Diligence Costs of PE

- |                        |                     |   |
|------------------------|---------------------|---|
| A) Internal constraint | Internal constraint |   |
| B) External constraint | Internal constraint |  |
| C) Internal constraint | External constraint |  |
| D) External constraint | External constraint |  |

### Explanation





Both of these constraints would be classified as external constraints, because they are driven by factors that Parks does not control directly. (LO 1.1.3)

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### Question #10 of 27

Question ID: 1716266

Which of the following statements about sovereign wealth funds (SWFs) is most accurate?

- A) SWFs can be financed by available foreign currency reserves. 
- B) Because of investment restrictions facing national governments, SWFs typically invest the majority of their assets in domestic securities. 
- C) SWFs are set up to provide future income to a country's current citizens. 
- D) SWFs typically have short or medium time horizons given their focus on liquid securities to generate ongoing income for a country's citizens. 

### Explanation



SWFs typically invest a significant portion of their assets in foreign securities and can be financed by available foreign currency reserves. SWFs are set up to provide funds for a country's future (not current) generations. SWFs have long time horizons that allow them to focus on capital gains and asset growth, while providing income to current generations is not a consideration. (LO 1.1.1)



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### Question #11 of 27

Question ID: 1716271

Which of the following statements about asset class allocations is least accurate?

- A) Very large allocations may hinder finding other suitable investment opportunities. 
- B) More established private equity programs tend to generate more liquidity. 

- C) Achieving above-average performance requires a large allocation to a particular asset class. 
- D) Allocations to a specific asset class that are too small will leave the investor underdiversified. 

### Explanation





Allocations to a specific asset class that are too small may leave the investor overdiversified and not generating sufficient returns (conversely, large allocations will create underdiversification and overexposure to specific risks). The rest of the statements are accurate. (LO 1.1.2)

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### Question #12 of 27

Question ID: 1716261

Which of the following types of pension funds is most likely to have the narrowest range of investment opportunities?

- A) National pension funds. 
- B) Private defined contribution plans. 
- C) Private defined benefit plans. 
- D) Individually managed accounts. 

### Explanation

Because individually managed accounts are the smallest and have the shortest time horizon (e.g., one employee as opposed to multiple employees) of the four types of pension plans, the range of investment opportunities for individually managed accounts is the narrowest. (LO 1.1.1)

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### Question #13 of 27

Question ID: 1716285

During a discussion with colleagues, an analyst makes these statements regarding the investment management process:

- I. The investment committee is responsible for approving the investment policy statement (IPS) and the target asset allocation strategy.
- II. The IPS should not only describe the asset owner, but also include a reference to the relevant fiduciary standards.

The analyst is correct with respect to:

- A) II only.
- B) I and II.
- C) I only.
- D) neither I nor II.

**Explanation**

The analyst's first statement is incorrect. It is the board (e.g., board of trustees), and not the investment committee, that is responsible for approving the IPS and the target asset allocation strategy. The analyst's second statement is correct: the IPS should include a description of the asset owner, the purpose and scope of the IPS, and should reference any relevant fiduciary standards.

(LO 1.1.4)

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**Question #14 of 27**

Question ID: 1716263

Which of the following investment vehicles is best categorized under pension funds?

- A) Charitable foundations.
- B) Individually managed accounts.
- C) Sovereign wealth funds.
- D) Family offices.

**Explanation**

The four types of pension funds are national pension funds, private defined benefit (DB) funds, private defined contribution (DC) funds, and individually managed accounts. (LO 1.1.1)

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**Question #15 of 27**

Question ID: 1716260

Which of the following types of pension funds is most likely to have the widest range of investment opportunities?

- A) National pension funds.
- B) Private defined contribution plans.
- C) Private defined benefit plans.
- D) Individually managed accounts.

### Explanation





Because national pension funds are the largest and have the longest time horizon of the four types of pension plans, the range of investment opportunities for national pension funds is the widest. (LO 1.1.1)

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### Question #16 of 27

Question ID: 1716281

The longest time horizon and lowest liquidity needs would best characterize:

- A) an individually managed account. 
- B) an endowment. 
- C) a defined benefit pension plan. 
- D) a family office. 

### Explanation





Endowments are very long-term investors typically seeking to invest in perpetuity, with relatively low liquidity needs. (LO 1.1.4)

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### Question #17 of 27

Question ID: 1716284

Which of the following objectives would be least common for an endowment or foundation?

- A) Maintain purchasing power. 
- B) Achieve a specific performance target above inflation. 
- C) Support spending needs. 
- D) Establish reserves. 

### Explanation





Endowments and foundations are tax-exempt, long-term investors with few investment restrictions. Supporting their ongoing spending needs, capital preservation/maintaining purchasing power, and outperforming inflation are common investment objectives. Establishing reserves is more common with sovereign wealth funds. (LO 1.1.4)

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### Question #18 of 27

Question ID: 1716279

Which of the following factors is least likely an example of a portfolio constraint?

- A) An investor's preference to avoid utility stocks. 
- B) Significant upcoming spending needs in five years. 
- C) Lower tax rate on dividend income than on capital gains. 
- D) Minimum return requirement of 7%. 

#### Explanation





Return requirements are part of an investment policy statement's objectives, not constraints. (LO 1.1.4)

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### Question #19 of 27

Question ID: 1716280

With respect to investment objectives stated in an investment policy statement, a common investment objective of a pension fund is:

- A) to perform in line with inflation. 
- B) to focus on long-term spending needs. 
- C) a return target percentage above the liability discount rate. 
- D) to generate a real rate of return percentage above the appropriate inflation rate. 

#### Explanation

A common investment objective of pension funds is to generate a return target percentage above the liability discount rate.




Focusing on long-term spending and on exceeding the inflation rate is typically a target of endowments and foundations. (LO 1.1.4)

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### Question #20 of 27

Question ID: 1716265

The primary difference between sovereign wealth funds (SWFs) and national pension funds is that:

- A) national pension funds invest for the benefit of future generations. 
- B) SWFs do not aim to provide retirement income to citizens. 
- C) national pension funds are much larger and have longer time horizons. 

D) only SWFs are owned by sovereign governments.



### Explanation

Both SWFs and national pension funds are set up by national (sovereign) governments and are typically similar in size and time horizon. However, national pension funds aim to provide retirement income to a country's citizens and, therefore, invest for the current generation, whereas SWFs aim to invest for the benefit of future generations. (LO 1.1.1)

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### Question #21 of 27

Question ID: 1716269

A family with \$50 million in investable assets would like to set up a family office. Which of these statements is least accurate regarding this structure?

A) The scope of the investments typically excludes alternative investments.



B) It may be funded with old money or entrepreneurship.



C) Time horizons are generally long.



D) Funds can be used to support current living needs.



### Explanation

A family office is a firm that manages the investment assets of one very wealthy individual or family. The scope of investments typically includes (rather than excludes) alternative investments. Time horizons are generally long, funds can be used for myriad purposes (current living needs, funds for future generations, charitable generations), and the sources of funds can be from entrepreneurship or old money.

(LO 1.1.1)

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### Question #22 of 27

Question ID: 1716276

Which of the following constraints is least appropriately classified as an external constraint?

A) Asset concentration limit.



B) Country limit.



C) Tax-exempt status.



D) Pension legislation.



### Explanation

External constraints include tax status (taxable or tax exempt) and rules and regulations, including pension legislation and asset concentration limits. Sector and country limits, along with liquidity and time horizon, are classified as internal constraints. (LO 1.1.3)

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### Question #23 of 27

Question ID: 1716274

A bond trader gathers the following economic and asset class data:

- Real growth rate in the economy: 2.5%
- Inflation: 1.5%
- Bond risk premium: 4%

Based on the trader's expectations, the short-term real riskless rate and bond return, respectively, are which of these?

	<u>Short-Term Real Riskless Rate</u>	<u>Bond Return</u>	
A)	Less than 2%	Less than 8%	
B)	2.5%	8%	
C)	More than 2.5%	More than 8%	
D)	Less than 2.5%	8%	

#### Explanation

The short-term real riskless rate is typically lower than the real growth rate. Because the real growth rate is estimated at 2.5%, the short-term real riskless rate is less than 2.5%. The bond return can then be calculated as follows:

*Asset class expected return = short-term real riskless rate + expected inflation + risk premium*

Asset class (bond) return = (less than 2.5%) + 1.5% + 4% = less than 8%.





(LO 1.1.2)

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### Question #24 of 27

Question ID: 1716275

The managers of the Melies family office use standard risk-return optimization models in establishing the appropriate asset allocations for the family's investment portfolio. The primary shortfall of this approach is that it ignores the difficulty in estimating:

- A) asset correlations and economic fundamentals. 
- B) return standard deviation and risk premiums. 
- C) economic fundamentals and betas. 
- D) risk premiums and asset correlations. 

#### Explanation

Using standard risk-return optimization models to establish asset allocations ignores the difficulty in estimating the appropriate risk premiums and correlations. Difficulties arise due to the lack of readily available data for many alternative investments needed for the inputs to estimate risk premiums and correlations, and given the need to make significant assumptions in the optimization process.

(LO 1.1.2)

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#### Question #25 of 27

Question ID: 1716259

Which of the following forms of investment is least likely to be considered a major class of asset owners?

- A) Foundation. 
- B) Family office. 
- C) Individually managed account. 
- D) Sovereign wealth fund. 

#### Explanation

The four major classes of asset owners are endowments/foundations, pension funds, sovereign wealth funds, and family offices.

An individually (or separately) managed account is a type of pension fund for large individual or institutional investors. It is similar to a private savings plan and is generally not considered large enough to be one of the four major classes of asset owners. (LO 1.1.1)

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#### Question #26 of 27

Question ID: 1716267

Which of the following items is least likely to be a source of capital for sovereign wealth funds?

- A) Natural resources. 
- B) Foreign aid receipts. 
- C) Trade surpluses. 
- D) Debt issuances. 

### Explanation

Funds in a sovereign wealth fund are generated through a country's savings and accumulated budget surpluses and surplus reserves. Issuing debt is a form of borrowing and would not be consistent with savings.





Common sources of capital for sovereign wealth funds include: natural resource revenues, consistent trade surpluses, and foreign aid receipts. (LO 1.1.1)

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### Question #27 of 27

Question ID: 1716278

An investor wishes to invest in commodities because of their potential mean-reverting properties. Within an investment policy statement, which of these descriptions of the type and classification of the investor's constraint is most accurate?

- A) Time horizon constraint, and it is an internal constraint. 
- B) Liquidity constraint, and it is an internal constraint. 
- C) Time horizon constraint, and it is an external constraint. 
- D) Liquidity constraint, and it is an external constraint. 

### Explanation

Commodities are likely to demonstrate mean reversion over the long term; therefore, an investor who has a short time horizon might not have a sufficiently long *time horizon* to accrue the benefits of possible mean reversion. *Internal constraints* are those that are imposed by the investor based on specific needs and situations. Examples include time horizon and liquidity.

(LO 1.1.3)