# 2026 CFA® Exam Prep

# IFT Mock Exams

# Level III

## Mock Exam 2: Session 1

**PORTFOLIO MANAGEMENT PATHWAY**

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Errata information can be found at https://goo.gl/UVXdAv

# Exam 2 Session 1

| Question Set | Topic | Minutes |
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| 9 | Asset Allocation | 12 |
| 10 | Derivatives & Risk Management | 12 |
| 11 | Ethical & Professional Standards | 12 |
| | **Total** | **132** |

Start time: 9:00 AM

End time: 11:12 AM

**QUESTION 1**
**TOPIC: PORTFOLIO MANAGEMENT PATHWAY - EQUITY**
**THE TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS**

Hal Sechan is the chief risk officer of Lupus Capital Group, an RIA based in Ohio, USA. Lupus Capital offers a menu of investing options in both fixed income and actively managed equity funds to its wide range of customers. Sechan is evaluating the portfolio management approaches of two new managers. Exhibit 1 gives the selected data for Manager A & Manager B.

**Exhibit 1**

| | |
|---|---|
| Manager A | Manager A has a structured investment process. She uses company fundamentals, including company demographics, financial statements, and other market data, relying on data vendors. The manager uses a forecasting model and creates optimization models to minimize risk and maximize the expected returns of the securities. Based on the minimizing risk/maximizing return profile, the portfolio is invested in medium-cap stocks from a mix of sectors to reach appropriate risk diversification. The portfolio has a TE constraint of $\leq 4\%$. Each position is $\leq 3\%$, irrespective of its benchmark weight. |
| Manager B | Manager B follows a fundamental approach based on macroeconomic view whereby she uses sophisticated models to make explicit three-year forecasts of the growth of sectors to determine their attractiveness based on valuation. The portfolio construction process balances security concentration and sector exposure as the manager seeks to maximize the return at an acceptable level of risk. A committee of portfolio managers meets once a month to discuss the timing of sector exposure. The final allocation is driven by the manager's judgment about the risk and return trade-offs. With the help of the feedback mechanism from her team of analysts, she maintains a wide coverage of companies within each sector. Portfolio volatility of each sector is $\sigma_S \leq 0.35$ of total portfolio volatility $\sigma_P$. |

Sechan next talks to two fund managers to discuss their exposure to rewarded risks, timing of exposure, and position sizing. To assess whether the managers are successful at combining these three sources of return in a portfolio, he collects the following information.

**Exhibit 2**

| | **Information coefficient** | **Breadth** | **Transfer coefficient** | **Active risk** |
|---|---|---|---|---|
| Fund Manager I | 0.15 | 180 | 0.35 | 6% |
| Fund Manager II | 0.30 | 80 | 0.50 | 8% |

**1.1 Determine** the most *likely* implementation (fundamental, discretionary) approach, security selection (bottom-up, top-down) approach, concentration, objective function (explicit, implicit), and constraints (absolute, relative) of each manager. **Justify** each answer with one reason from the information given.

- Implementation
- Security Selection Approach
- Concentration
- Objective Function
- Constraints

**1.2**. **Determine** the higher performing manager based on expected active portfolio (fund) return E(R). **Justify** your response. (The response requires calculations.)