Overview for Questions #1-3 of 84

Question ID: 1748951

TOPIC: ASSET ALLOCATION

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Valerie Gordon is a medical scientist at a large pharmaceutical company. Aged 48, Gordon has saved toward her intended retirement at age 65 in a tax-deferred retirement account that is currently valued at USD 1 million. Exhibit 1 shows her current asset allocation.

Exhibit 1: Current Asset Allocation—Gordon

Asset Class	Weighting
Non-investment-grade bonds	20%
Investment-grade bonds	20%
Equity total return (capital gain) strategy	30%
Equity dividend income strategy	30%

Gordon recently inherited an additional USD 1 million from her aunt, which she plans to invest in a new taxable portfolio. Gordon meets with three potential wealth managers (Manager X, Manager Y, Manager Z) and advises them that she wants to invest in the same set of asset classes as her retirement account. The wealth managers also note the following:

- Gordon wants to maintain her current risk tolerance.
- The equity dividend income strategy focuses on high-dividend-paying stocks.
- The equity total return strategy focuses on growth companies that do not pay dividends.
- Gordon has an annual salary of $150,000 and pays a 40% tax rate.

Exhibit 2 shows each manager's recommended asset allocations.

Exhibit 2: Recommended Asset Allocations

Asset Class	Manager X	Manager Y	Manager Z

Non-investment-grade bonds	15%	0%	0%
Investment-grade bonds	25%	40%	30%
Equity total return (capital gain) strategy	30%	30%	70%
Equity dividend income strategy	30%	30%	0%
Totals	**100%**	**100%**	**100%**

The potential wealth managers each discuss the concept of tactical asset allocation with Gordon. She considers three statements made by the potential managers:

Statement 1:	Tactical asset allocation includes security selection.
Statement 2:	Tactical asset allocation attempts to take advantage of perceived short-term opportunities in the market.
Statement 3:	Tactical asset allocation seeks to maintain the investor's long-term targeted risk profile.

Based on an overall portfolio value of USD 2 million that is split between her tax-deferred retirement account and her taxable account, she wants to know the optimum allocation of assets to each account. She states that she has no constraints on transferring assets between accounts.

Question #1 of 84

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Determine the *most* suitable asset allocation for Gordon, given the recommendations in Exhibit 2 (Manager X, Manager Y, or Manager Z). **Justify** your recommended allocation with *two* reasons.

Question #2 of 84

Question ID: 1748953

Recommend the optimum allocation of assets to each of Gordon's accounts. **Justify** your recommendation with *two* reasons.

Question #3 of 84

Question ID: 1748954

Identify which of the statements made by the potential managers is correct (Statement 1, Statement 2, or Statement 3). **Justify** your choice with *one* reason.

For the other two statements that you believe are incorrect, **justify** your decision with *one* reason for each statement.

Place your responses in separate paragraphs.

Overview for Questions #4-7 of 84

Question ID: 1749044

TOPIC: ETHICAL AND PROFESSIONAL STANDARDS

TOTAL POINT VALUE OF THIS QUESTION SET IS 12 POINTS

Minh Vo, CFA, is an associate at Norman Marshall and Associates (NMA), an investment management firm. Currently, Vo manages the investment account of Jia Oho, a widower who lives off her portfolio and has a low risk tolerance. Oho's account has been with the firm for over 10 years. Last month, Vo added a stock with a beta of 1.65 to Oho's portfolio. Also, Vo has sold call options on these shares as part of a covered call strategy for Oho's portfolio.

Vo sends out quarterly performance reports comparing his client's portfolio performance to the performance of a broad-based market index. Vo notices that his performance would look more attractive if he used a target date index fund for comparison. He also notices that the risk profile of his client portfolios is more closely tracked by target date funds than by the broad-based market index. Starting with the first quarter of the current year, Vo updates his client communications, replacing the broad-based market index with target date funds for comparison.

Vo recently prepared a research report with a buy rating on Nakatomi Enterprises, a publicly traded firm that produces microchips for supercomputers. NMA's investment banking department has completed transactions for Nakatomi in the past six months and is currently working with the company to evaluate a secondary offering. NMA has a policy in place that separates the activities of its investment banking and research departments.

In the report, Vo disclosed that Nakatomi has an investment banking relationship with NMA, and that his wife holds Nakatomi shares. However, he did not comment on the risk profile and suitability of investing in Nakatomi shares.

While NMA has not formally adopted the CFA Institute Code and Standards, the firm strives to ensure that employees behave ethically and comply with all laws and regulations. To ensure regulatory compliance, NMA has a policy that all portfolio managers are responsible to ensure that their supervised employees follow all applicable laws, rules, and regulations.

Question #4 of 84

Question ID: 1748966

With respect to Oho's portfolio, has Vo violated the Standards?

A) Yes, both by buying the stock and selling the call options.
B) Yes, by selling the call options, but not by buying the stock.
C) No, because the overall portfolio risk needs to be evaluated to judge suitability.

Question #5 of 84

Question ID: 1748967

Regarding Vo's decision to change his client's quarterly performance reports, he has *most likely*:

A) not violated the Standards because he has a reasonable basis for the change.
B) violated the Standards because changes to an established performance benchmark are not permitted.
C) not violated the Standards if he discloses the change in performance presentation to his clients.
