



**PAST QUESTIONS AND ANSWERS (December 2006)**

**PAPER 12**

**ASSET MANAGEMENT**

of

The Licensing Examination  
for Securities and Futures Intermediaries

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### Methodology of Developing Questions

*Our Institute is committed to providing questions of the highest quality.*

*Our current examination structure has been benchmarked against those in both developed and emerging markets such as UK, US, Australia, Singapore, Malaysia and China. The syllabuses, study materials, training guides and questions were designed by international consultants specializing in financial education.*

*The Licensing Examination has been approved by the Academic and Accreditation Advisory Committee of the Securities and Futures Commission (SFC) as recognized industry qualification and local regulatory framework paper for meeting the competence requirements of the SFC.*

*External consultants are appointed to develop new questions according to specified criteria approved by our Examinations Committee. The aim of these criteria is to ensure that the candidates have thorough understanding of the manuals by testing them at different cognitive levels such as recall, comprehension, application, analysis and evaluation on predetermined weightings of each topic. The new questions are reviewed by reviewers who are market practitioners, legal and compliance professionals, and academics to ensure that the knowledge tested is covered in the study manuals, and that the standard of the questions is appropriate and consistent throughout.*

*To maintain their quality, the questions undergo frequent reviews and revisions internally which take into account, among others, the average correctness of the questions (i.e., the percentage of candidates in the examination who correctly answer the questions) and candidates' comments, if any, following each examination. In addition to the quality assurance being imposed on the questions, external assessors who are market practitioners, legal and compliance professionals, and academics, are engaged to conduct regular reviews. There are also periodic comprehensive reviews by external consultants on the manuals and questions.*

*The study manuals and their subsequent updates are the only source of materials for the setting of the questions, so that candidates need to study only those manuals and updates to prepare for the examinations.*

*It is estimated that the study manuals will require 6 to 11 hours of study time per topic, depending on which paper it is. Candidates may need to spend more or less time, depending on their work experience and background. They are advised to use the Learning Outcomes for each topic as a key to the way they study the materials in each topic, and unless explicitly stated, they could be tested on any aspect of the syllabus.*

**Please attempt ALL 40 questions in this question book.  
All questions carry EQUAL MARKS.**

<1>.

Which of the following statements is **CORRECT** about the yield curve?

- A The yield curve shows the behaviour of interest rate forecasts.
- B When short-term rates are lower than long-term rates, there is a downward-sloping yield curve.
- C A downward-sloping yield curve shows that investors demand an additional risk premium for lending money over the long term.
- D A downward-sloping yield curve indicates that the market expects a future rise in interest rates.

<2>.

What type of analysis uses ratio analysis to evaluate equities?

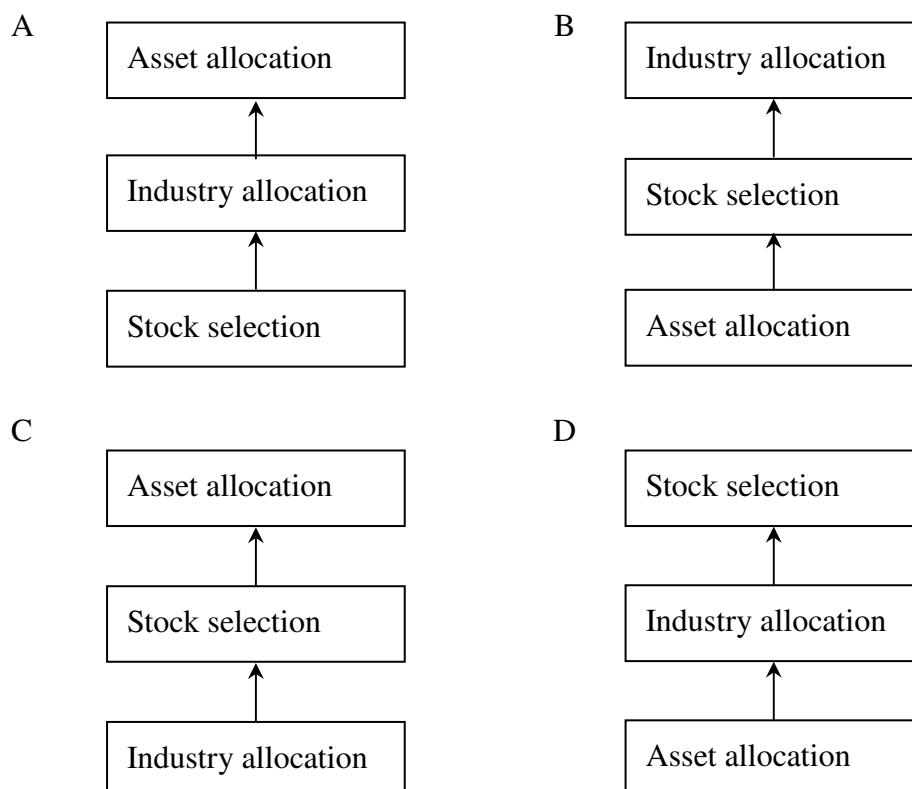
- A Technical analysis.
- B Qualitative analysis.
- C Fundamental analysis.
- D Top-down analysis.

<3>.

The time weighted return is a method of measuring performance. Which of the following statements **BEST** describes time weighted return?

- A Time weighted return on investment considers the impact of capital inflows and outflows of an investment.
- B The rate of return that discounts a portfolio's terminal value and interim cash flows back to its initial value.
- C The discount rate that equates the present value of future cash flows with the market value.
- D The probability weighted return of cash flows in a portfolio.

&lt;4&gt;.

Which of the following diagrams **BEST** describes bottom-up investing?

&lt;5&gt;.

Investments in smaller company stock compared to investments in larger company stock are generally:

- A more volatile because they are less liquid, have less stock issued and have less diversified sources of income.
- B more volatile because they are less liquid, have less stock issued and have more diversified sources of income.
- C less volatile because they are less liquid, have less stock issued and have less diversified sources of income.
- D less volatile because they are less liquid, have less stock issued and have more diversified sources of income.

&lt;6&gt;.

In the managed funds market, large institutional investors are positioned:

- A in the retail market.
- B in the wholesale market.
- C somewhere between the retail and wholesale markets.
- D in the same group as private client investors.

<7>.

A broker tells you that he has continuously outperformed the market by trading on publicly available information in the Hong Kong market. According to the Efficient Market Hypothesis, what would this imply?

- A The market is weak form efficient.
- B The market is semi-strong form efficient.
- C The market is strong form efficient.
- D The market is not efficient.

<8>.

You are interested in investing in an equity fund. Which step of the investment management process will require you to understand the investment management style?

- A Defining the investment objectives and constraints.
- B Setting the investment strategy.
- C Implementing and managing the portfolio.
- D Monitoring and reviewing.

<9>.

You are a financial advisor with prospective clients in their fifties with two incomes and few or no liabilities. Your clients have typical lifestyles. Which lifestyle stage **BEST** represents their present situation?

- A Single employed.
- B Family nest.
- C Shrinking family.
- D Retirement.

<10>.

Which of the following statements about diversification is **INCORRECT**?

- A Diversification is spreading your assets across different asset classes, sectors, countries or issuers of securities.
- B Diversification is about purchasing shares with different correlations.
- C Diversification is about “putting all your eggs in one basket”.
- D Diversification is a benefit of investing in managed funds.

<11>.

A broker tells you he has outperformed the market by trading on insider information in the Hong Kong market. As a broker yourself, you should respond to this situation by which of the following?

- A Not asking for information as any arbitrage opportunities would now have passed.
- B Not asking for information and reporting it to the regulator as it is an illegal activity in Hong Kong.
- C Asking for information so that you can trade based on that information.
- D Asking for information so that a client can trade based on that information.

<12>.

Compared to top-down investing, bottom-up investing:

- A focuses on macro economic issues.
- B focuses on fundamentals of shares.
- C is active.
- D is passive.

<13>.

When researching fund managers, which of the following statements is **CORRECT**?

- A You would generally expect the qualitative findings to be reflected in the quantitative results.
- B You would generally expect the qualitative findings to conflict with the quantitative results.
- C You should look at the qualitative findings separately to the quantitative results.
- D You should test qualitative and quantitative results with sensitivity analysis.

<14>.

What is the **MAIN** role of fund research houses in the funds management industry?

- A To rate individual securities.
- B To report competitor's product development.
- C To aid investors in selecting or monitoring a fund manager.
- D To distribute managed funds via the direct channel.

**Information for Questions no. 15 to 17.**

You are an advisor reviewing fund managers' performance over the last year. Your records indicate that government bonds have returned 6% over the period. You have also obtained the following information:

	<i>Return</i>	<i>Standard deviation</i>	<i>Beta</i>
Market portfolio	0.152	0.26	
Fund manager W	0.170	0.18	0.9
Fund manager X	0.160	0.17	0.8
Fund manager Y	0.140	0.17	1.3
Fund manager Z	0.158	0.28	0.9

<15>.

The beta for the market portfolio is:

- A 0.7
- B 0.8
- C 1.0
- D 1.1

<16>.

Which fund manager has performed **BEST** according to its Sharpe ratio?

- A Fund manager W.
- B Fund manager X.
- C Fund manager Y.
- D Fund manager Z.

<17>.

Given the information above, which statement is **CORRECT** when comparing the fund managers' Jensen's alpha?

- A Fund manager W has performed better than fund manager X and fund manager Y has performed better than fund manager Z.
- B Fund manager W has performed better than fund manager X and fund manager Z has performed better than fund manager Y.
- C Fund manager Y has performed better than fund manager W and fund manager Z has performed better than X.
- D Fund manager Y has performed better than fund manager W and fund manager X has performed better than Z.



<18>.

Which of the following types of efficiency describe investment markets?

- I Operationally efficient.
  - II Informationally efficient.
  - III Allocationally efficient.
  - IV Strategically efficient.
- 
- A I, II and III only
  - B I, II and IV only
  - C I, III and IV only
  - D II, III and IV only

<19>.

What is the asset allocation of a typical capital preservation fund?

- A 10% equities, 85% fixed income and 5% cash.
- B 40% equities, 50% fixed income and 10% cash.
- C 50% equities, 50% fixed income.
- D 70% equities, 20% fixed income and 10% cash.

<20>.

Which of the following statements are **CORRECT**?

- I All managed funds offered to Hong Kong investors under the Mandatory Provident Fund Scheme (MPF) must be onshore funds.
  - II All managed funds in Hong Kong must meet certain Securities and Futures Commission (SFC) standards.
  - III Most of Hong Kong's authorised unit trusts are domiciled outside Hong Kong.
  - IV Most of Hong Kong's authorised unit trusts are domiciled in Hong Kong.
- 
- A I and III only
  - B I and IV only
  - C II and III only
  - D II and IV only

<21>.

Security A has the following probability distribution of returns:

<i>Scenario</i>	<i>Probability</i>	<i>Return</i>
1	0.1	15%
2	0.8	25%
3	0.1	35%

What is the variance for Security A?

- A 0.002
- B 0.020
- C 0.200
- D 0.300

<22>.

Which of the following statements about constituent funds in the Mandatory Provident Fund (MPF) Scheme is **INCORRECT**?

- A They are options offered within a master trust.
- B The employer selects which constituent fund the employee invests in.
- C One of the funds must be a capital preservation fund.
- D They can invest directly in an Approved Pooled Investment Fund.

<23>.

Compared to retail investors, private clients:

- A invest smaller amounts, have a larger investment minimum and are charged a lower fee.
- B invest larger amounts, have a larger investment minimum and are charged a higher fee.
- C invest smaller amounts, have a smaller investment minimum and are charged a higher fee.
- D invest larger amounts, have a larger investment minimum and are charged a lower fee.

<24>.

Which of the following are the **MAIN REASONS** for an investor to invest in managed funds?

- I To obtain a better return.
  - II To diversify risks.
  - III Lack of time to look after their own investments.
  - IV More freedom on stock selection.
- A I, II and III only
  - B I, II and IV only
  - C I, III and IV only
  - D II, III and IV only

<25>.

You are an investment analyst evaluating HarbourView shares. You are given the following information:

	HarbourView shares
Dividend per share	HKD0.30
Current share price	HKD5.25
Number of ordinary shares	50 million
After tax profit	HKD4,450,000

What is the price earnings ratio (PER) for HarbourView shares?

- A 47 times.
- B 59 times.
- C 64 times.
- D 69 times.

<26>.

Which investment management style would an equities fund manager who utilises a value approach to stock selection follow?

- A Utilitarian.
- B Strategic.
- C Fundamental.
- D Quantitative.

<27>.

Compared to growth investing, value oriented equities fund managers generally prefer stock with:

- A a higher price earnings ratio and a lower dividend yield.
- B a lower price earnings ratio and a lower dividend yield.
- C a higher price earnings ratio and a higher dividend yield.
- D a lower price earnings ratio and a higher dividend yield.

<28>.

During the Asian financial crisis, which of the following asset classes was the **MOST** volatile in Hong Kong?

- A Fixed-interest securities.
- B Cash.
- C Property.
- D Equities.

<29>.

The Capital Asset Pricing Model (CAPM) considers which type of risk in pricing the expected returns and risk of securities?

- A Systemic risk.
- B Unsystemic risk.
- C Diversifiable risk.
- D Non-market risk.

<30>.

Which of the following statements is **INCORRECT** about the Random Walk Hypothesis?

- A It assumes successive returns are statistically independent.
- B It assumes there is no correlation between the returns in one period and the next.
- C It assumes the distribution of returns in all periods is identical.
- D It assumes historical share prices can be used to predict future price movements.

<31>.

When using the information ratio to compare the performance of two fund managers, all else being equal, which of the following would you select?

- A The fund manager with a positive information ratio.
- B The fund manager with a negative information ratio.
- C The fund manager with the lowest information ratio.
- D The fund manager with the highest information ratio.

<32>.

An investor has invested 75% of his assets in a money market fund. Generally, what is the investment horizon of such an investment?

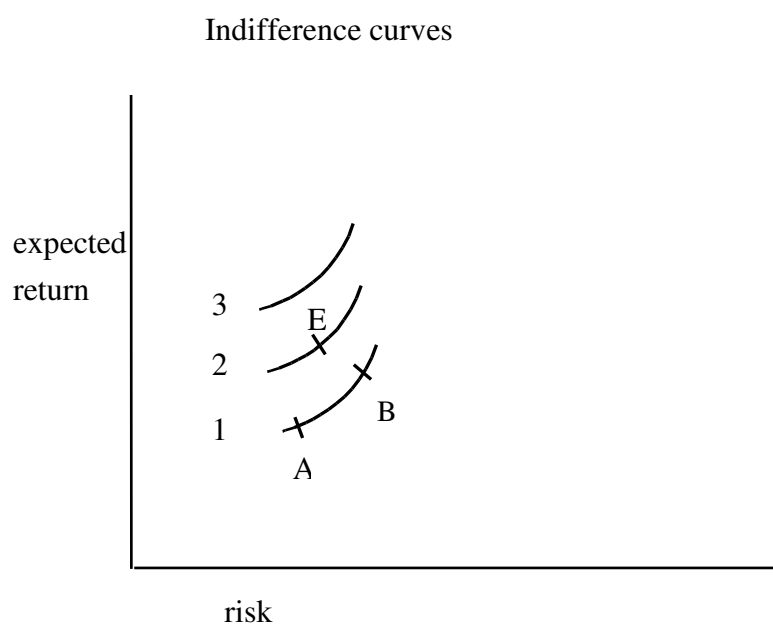
- A 0 – 1 year.
- B 3 – 5 years.
- C 5 – 7 years.
- D 7 – 10 years.

<33>.

You propose managing a portfolio of fixed income securities by utilising a passive strategy. Which of the following actions would your strategy involve?

- A Buying inflation linked bonds.
- B Buying index linked bonds.
- C Matching the fixed income securities to a stated performance benchmark.
- D Managing the sector-spread to benefit from a positive sloping yield curve.

**Information for Questions no. 34 to 35.**



<34>.

A shift from curve 1 to 2 shows that:

- A investors will have less utility because there is greater return for the same level of risk.
- B investors will have less utility because there is greater return for a different level of risk.
- C investors will have more utility because there is greater return for the same level of risk.
- D investors will have more utility because there is greater return for a different level of risk.

<35>.

Given the indifference curves above, which of the following statements is **CORRECT**?

- A The investor prefers portfolio A because it has a lower level of risk.
- B The investor prefers portfolio B because it has the greatest expected return.
- C The investor prefers portfolio E because it is on the indifference curve 2, which is higher than the indifference curve 1, where both portfolios A and B are situated.
- D The investor does not prefer one portfolio from another as each portfolio lies on an indifferent curve.

<36>.

You are a prospective fund manager to a life insurance company. You propose to manage its assets utilising a liability-driven strategy. Which of the following actions would your strategy involve?

- A Aligning the coupon payments and maturities from your proposed portfolio of fixed income securities with the company's anticipated claim payments.
- B Aligning the dividends and capital appreciation of your proposed portfolio of equities with the company's anticipated claim payments.
- C Managing the sector-spread of your proposed portfolio to capitalise on the margins offered by different governments and other institutions' fixed income securities.
- D Managing the sector-spread of your proposed portfolio to benefit from a positive sloping yield curve.

<37>.

Which of the following statements **BEST** describes investors of retail or wholesale managed funds?

- A Individuals, large corporations and private clients invest in retail managed funds.
- B Individuals, large corporations and private clients invest in wholesale managed funds.
- C Trustees and individuals invest in retail managed funds.
- D Trustees and large corporations invest in wholesale managed funds.

<38>.

What is the shortcoming of using peer group performance comparisons to judge performance of a fund?

- A The fund manager's investment objectives may be more meaningful than its peers.
- B The fund manager's investment objectives may be more cash dominant than its peers.
- C The fund manager's investment objectives may be the same as its peers.
- D The fund manager's investment objectives may be narrower or wider than its peers.

<39>.

You are an advisor reviewing fund managers performance over the last year. Your records indicate that government bonds have returned 5% over the period. You have also obtained the following information:

	Return	Standard deviation	Beta
Market portfolio	0.148	0.52	
Fund manager W	0.148	0.36	0.18
Fund manager X	0.160	0.34	0.16
Fund manager Y	0.114	0.34	2.60
Fund manager Z	0.158	0.56	1.80

Given the information above, which fund manager's performance shows it lies on the Capital Market Line?

- A Fund manager W.
- B Fund manager X.
- C Fund manager Y.
- D Fund manager Z.

<40>.

Which of the following does attribution analysis involve?

- A Carrying out sensitivity analysis to the actual holdings of shares in the portfolio.
- B Comparing the performance of a fund to its stated benchmark or its peer grouping.
- C Examining past annualised returns across 5 and 10 years to determine whether the investment style is true to label.
- D Breaking down fund performance to find which proportion comes from sector and security selection, asset allocation and their interaction.

*~End of the Examination Paper~*

**Answers**

<b>Question No.</b>	<b>Answer</b>	<b>Question No.</b>	<b>Answer</b>
1	A	21	A
2	C	22	B
3	A	23	D
4	A	24	A
5	A	25	B
6	B	26	C
7	A	27	D
8	B	28	D
9	C	29	A
10	C	30	D
11	B	31	D
12	B	32	A
13	A	33	C
14	C	34	C
15	C	35	C
16	A	36	A
17	B	37	D
18	A	38	D
19	A	39	C
20	A	40	D