CFA-LEVEL-1 Q&As

CFA Level I Chartered Financial Analyst

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QUESTION 1

Which inventory costing method is most useful in estimating the amount of inventory lost or destroyed by theft, fire, or other hazards?

A. FIFO

B. None of these answers

C. average cost method

D. gross profit method

E. LIFO

Correct Answer: D

The historical relationship between cost of goods sold and sales is applied to sales of the current period as a way of estimating COGS during the current period. COGS is then subtracted from the cost of goods available for sale to get the estimated cost of the ending inventory.

QUESTION 2

A firm has issued a perpetuity with a total face value of 100 million dollars and a coupon rate of 5.8%. If the risk free rate equals 5.8% and investors require a rate of return of 10.6% from the perpetuity, what\\'s the amount the firm raised through the issue?

A. $55.28 million

B. none of these answers

C. $100 million

D. $54.72 million

Correct Answer: D

The price of a perpetuity that pays C per year, at a discount rate of R, equals C/R. Hence, the price of the perpetuity issue = $(100*5.8%/10.6%) million = $54.72 million.

QUESTION 3

In the full cost method, oil firms:

A. none of these answers.

B. are required to expense all oil-drilling costs resulting in dry holes.

C. must expense drilling costs which result in productive oil wells.

D. can capitalize all oil-drilling costs.

Correct Answer: D

In extractive industries, firms are allowed to use either the full-cost method, in which all search and development costs can be capitalized, or the successful-efforts method, where all such costs are expensed unless they result in revenue-generating assets, in which case, they are capitalized.

QUESTION 4

Business risk is concerned with the operations of the firm. Which of the following is not associated with (or not a part of) business risk?

A. The ability to change prices as costs change.

B. Changes in required returns due to financing decisions.

C. The extent to which operating costs are fixed.

D. Demand variability.

E. Sales price variability.

Correct Answer: B

Business risk depends on:

(1)

unit sales variability,

(2)

sales price variability,

(3)

input price variability,

(4)

ability to adjust output prices for changes in input prices and,

(5)

the extent to which costs are fixed (operating leverage).

QUESTION 5

________ financing is one of the early stages of financing in venture capital.

A. Mezzanine

B. Asset-backed

C. Turnaround

D. Bridge

E. none of these answers.

F. Seed

Correct Answer: F

There are three early stages of financing:

1.

Seed financing. This is capital (typically less than $50,000) that is provided at the "idea" stage, which goes for product development and market research.

2.

Start-up financing. This capital is used in product development and initial marketing for firms in business under one year and has not sold their product commercially.

3.

First-stage financing. This is capital provided to initiate commercial manufacturing and sales.

QUESTION 6

The implications of stock market efficiency for fundamental analysis indicates that using the top-down approach to analyze a firm will yield:

A. superior returns using past and current information.

B. superior returns compared to a randomly selected buy-and-hold portfolio of stocks.

C. returns that are not superior if the analysis only looks at past and current information.

D. superior returns using only past information.

Correct Answer: C

The evidence is that fundamental analysis does not lead to superior returns using the top-down approach if the analyst uses only past and current information. The analyst\\'s job has to be directed towards doing a superior job of estimating the variables that cause long-run trends in realized returns.

QUESTION 7

Load open-end funds charge

A. sales fees of about 7.5 to 8% of NAV.

B. sales and redemption fees of about 1 to 2% of NAV.

C. sales and redemption fees of about 7.5 to 8% of NAV.

D. sales fees of about 10 to 15% of NAV.

E. sales fees of about 1 to 2% of NAV.

Correct Answer: A

Load funds charge a sales fee for share sales that is typically 7.5 to 8% of the NAV. Share prices are quoted with a NAV and an offering price. Load funds generally do not charge a redemption fee, but some no-load funds do charge a small one of about half a percent of NAV.

QUESTION 8

________ attempt to match the composition of the market.

A. Balanced funds

B. Growth funds

C. Composite funds

D. Market index funds

Correct Answer: D

They are funds that attempt to match a benchmark index of the market.

QUESTION 9

Which of the following is a key benefit of using the degree of leverage concept in financial analysis?

A. It shows how a given change in leverage will affect sales.

B. None of these statements are correct.

C. It establishes the optimal capital structure for the firm.

D. It allows decision-makers a relatively clear assessment of the consequences of alternative actions.

E. All of these statements are correct.

Correct Answer: D

The degree of leverage concept is useful primarily for the insights it provides regarding the joint effects of operating and financial leverage on EPS. DOL concepts provide alternatives to decision-makers, giving a better idea of the ramifications of alternative actions.

QUESTION 10

The deferred income tax account

A. can be reported as an asset

B. is reported as a liability if it has a credit balance

C. is where the difference between income tax expense and income tax payable is reconciled

D. all of these answers are correct

Correct Answer: D

The difference between income tax expense (based on accounting income) and the actual income taxes payable (based on taxable income) is reconciled in an account called deferred income taxes. It can be reported as an asset or a liability, depending on its balance and the circumstances.

QUESTION 11

You are evaluating 5 portfolio managers (A, B, C, D, and E) whose Sharpe ratios are 0.25, 0.41, 0.92, 0.78, and 0.51, respectively. Which manager would most risk-averse investors prefer?

A. C.

B. A.

C. E.

D. None of these answers is correct.

Correct Answer: A

The Sharpe measure of risk-adjusted performance is equal to (rbar_p - rbar_f)/sigma_p, where rbar_p is the mean portfolio return, rbar_f is the mean risk-free return, and sigma_p is the standard deviation of portfolio return. Thus, the manager with the highest Sharpe ratio is generating the largest return in excess of the risk free rate, per unit of risk assumed. This is manager C, with a Sharpe ratio of 0.92.

QUESTION 12

While working abroad, United States citizen Alex Beggs purchases a foreign bond with an annual coupon of 7.0 percent for 93.0. He holds the bond for one year and then sells it for 95.5 before he leaves. During the year, the dollar appreciated 2.5% relative to the foreign currency.

Which of the following is closest to Begg\\'s Total Dollar Return?

A. 7.460%.

B. 12.970%.

C. 10.215%.

D. 0.121%.

Correct Answer: A

TheTotal Dollar Returnis calculated as follows:

Step 1: Calculate the value change in the foreign currency:

The dollarappreciated0.025, so the foreign currencydepreciatedby 0.025, or 2.5%.

Step 2: Use the Total Dollar return formula to calculate the return:

R$= { [1+($coupon + VEND- VBEG)/ VBEG] * (1 + g) } - 1,

WhereR$=Total dollar return,VEND= Bond value at end of period,VBEG=Bond value at end of period,

andg= % change in thedollarvalue of the foreign currency.

Here,R$= { [1+(7.0 + 95.5 ?93.0)/93.0] * (1 - 0.025) } - 1

= { [1.102151] * (0.975) } - 1

= 0.07460, or7.460%

QUESTION 13

A bottling company offers three kinds of delivery services-instant, same day and within five days. The profit per delivery varies according to the kind of delivery. The profit for an instant delivery is less than the other kinds because the driver has to go directly to a grocery store with a small load and return to the bottling plan. To find out what effect each type of delivery has on the profit picture, the company has made the following tabulation based on deliveries for the previous quarter.

Type of Number of Deliveries Profit per Delivery Delivery During the Quarter Instant 100 $70 Same day 60 $100 Within five days 40 $160

What is the weighted mean profit per delivery?

A. $97

B. $72

C. $142

D. None of these answers

E. $100

Correct Answer: A

(100*70)+(60*100)+(40*160) = 1940. Mean is 1940/200 = 97

QUESTION 14

You are analyzing a firm that has:

If you think next year\\'s earnings will be $4 per share, what value would you place on this stock?

A. $22.24

B. $26.67

C. $33.32

D. $45.45

Correct Answer: C

Explanation:Dividend payout = 1 - earnings retention rate = 1 - .4 = .6 =+ B(-) = .06 + 1.2(.11 - .06) = .12 g = (retention rate)(ROE) = (.4)(.12) = .048 P/E = (div payout rate)/(k - g) = .6/(.12 - .048) = 8.33 Price = (E)(P/E) = (4)(8.33) = 33.32

QUESTION 15

Intraperiod income tax allocation arises because

A. certain revenues and expenses appear in the financial statements but are excluded from taxable income.

B. items included in the determination of taxable income may be presented in different sections of the financial statements.

C. income taxes must be allocated between current and future periods.

D. certain revenues and expenses appear in the financial statements either before or after they are included in taxable income.

E. none of these answers.

Correct Answer: B

To provide a fair presentation of the results of operations, accounting rules require that income tax expense for the period be allocated among income from continuing operations, discontinued operations, extraordinary items, and items charged or credited to shareholders\\' equity.