Core Unit 4

Financing and Investing for Retirement Provision

Mock Examination

Recommended Time: 1 hour

1. **Alpha and Beta are two terms commonly used to judge active investment manager performance. Explain the meaning of these terms and state what levels of alpha and beta a trustee would typically prefer.**

**5 marks**

Relevant section of the manual is Part 6 Chapter 1.1.

Format: description

Answer should cover. For each approach:

* Trustee typically prefers high Alpha and low Beta
* Alpha: Measure of investment performance compared to a benchmark

Manager seeks to provide alpha through good stock selection to outperform the passive manager

* Beta: Measure of volatility compared with the market

Portfolio with a low Beta has less asset volatility than one with a high Beta

1. **Describe how investment professionals assess whether a company’s share price is reasonable and outline the most common methods of valuing the shares.**

**10 marks**

Relevant section of the manual is Part 2 Chapter 1.4.

Format: descriptive

Answer should cover short description of:

* The company information against which they evaluate the share price
* Return on investment capital
* Price to earnings ratio
* Dividend yield
* Price to book ratio

1. **What is the key difference between a Lifestyle Fund and a Target Date Fund?**

**5 marks**

Relevant section of the manual is Part 4 Chapter 1.3.

Format: short paragraph

Answer should cover:

* Both funds aim to de-risk over time
* Lifestyling – investment in growth assets gradually switched to defensive funds from 5-10 years before retirement
* Target date – investment remains in the same target date fund until retirement, but asset allocation is automatically adjusted over time rather than varied through different combinations of growth and defensive funds

1. **Outline the main objectives of the Pensions Regulator and the powers it has to act where it believes an employer is deliberately attempting to avoid its pension obligations.**

**10 marks**

Relevant section of the manual is Part 5 Chapter 1.3.

Format: list (objectives) and bullets with short explanation (powers)

Answer should cover:

* Governing legislation
* The 5 objectives set out in the legislation
* Powers – explain contribution notices, financial support directions and restoration orders

1. **Explain what a swap is and briefly describe 5 types of swap.**

**10 marks**

Relevant section of the manual is Part 2 Chapter 4.1 and Part 3 Chapter 2.4.

Format: paragraphs or bullets a short explanation for each

Answer should cover:

* Features of a swap
* Types:
  + Interest rate swap
  + Inflation swap
  + Index swap
  + Currency swaps
  + Credit default swaps

1. **Write short notes on how risk can be reduced by improving the employer covenant.**

**5 marks**

Relevant section of the manual is Part 3 Chapter 1.1.

Format: note form/bulleted

Answer should cover:

* Charge on assets
* Parent company guarantee
* Escrow account

1. **A major reason for funding pension schemes in advance is to provide security for members.**

**Explain how this security is achieved.**

**5 marks**

Relevant section of the manual is Part 1 Chapter 1.1.2.

Format: descriptive

Answer should cover:

* Meeting cost of benefits promised
* Why a trust is important
* How the size of the fund affects the level of security