47 INTRODUCTION TO ALTERNATIVE INVESTMENTS

1. Historical data on returns of real estate are most likely to exhibit:
   (A) smoothing.
   (B) downward-biased measures of risk-adjusted returns.
   (C) overstated correlations with other asset classes.

2. The notice period for a hedge fund is best described as the period following:
   (A) an investment in the fund, during which the investor is not permitted to redeem shares.
   (B) a request for redemption of shares, within which the fund must fulfill the request.
   (C) the opening of the fund to investors, before the fund is closed to new investors.

3. Alternative investments most likely have which of the following characteristics compared to traditional investments?
   (A) Unique legal structures and tax treatments.
   (B) Lower leverage and higher liquidity.
   (C) Higher levels of regulation and transparency.

4. A private equity provision that requires managers to return any periodic incentive fees resulting in investors receiving less than 80% of profits is a:
   (A) high water mark.
   (B) drawdown.
   (C) clawback.

5. The typical trade used by a merger arbitrage fund is:
   (A) short position in acquirer, long position in firm being acquired.
   (B) long position in acquirer, short position in firm being acquired.
   (C) short positions in both the acquirer and the firm being acquired

6. If a commodity futures market is in backwardation:
   (A) the commodity has a high convenience yield.
   (B) a long futures position will have a negative roll yield.
   (C) the futures price is of the commodity is higher than the spot price.

7. Compared to traditional investments, alternative investments are most likely to be more:
   (A) transparent.
   (B) leveraged.
   (C) liquid.

8. Kettering Incorporated is a successful manufacturer of technology hardware. Kettering is seeking capital to finance additional growth that will position the company for an initial public offering. This stage of financing is most accurately described as:
   (A) mezzanine-stage financing.
   (B) angel investing.
   (C) early-stage financing.

9. To exit an investment in a portfolio company through a trade sale, a private equity firm sells:
   (A) the portfolio company to one of the portfolio company's competitors.
   (B) the portfolio company to another private equity firm.
   (C) shares of a portfolio company to the public.

10. Relatively infrequent valuations of private equity portfolio companies most likely cause:
   (A) average fund returns to be biased upward.
   (B) standard deviations of fund returns to be biased upward.
   (C) correlations of fund returns with equity returns to be biased downward.

11. Supplying capital to companies that are just moving into operation, but do not as yet have a product or service available to sell, is a description that best relates to which of the following stages of venture capital investing?
   (A) Angel investing stage.
   (B) Early stage.
   (C) Mezzanine stage.

12. A hedge fund strategy that takes positions in shares of firms undergoing restructuring or acquisition is said to be pursuing:
   (A) a macro strategy.
   (B) an event driven strategy.
   (C) an equity hedge strategy.

13. Return and risk data on alternative investments may be affected by backfill bias if:
   (A) a firm's historical returns are included when it is added to an index.
   (B) data only include currently existing firms.
   (C) the incorrect distribution is used to model volatility.

14. If a commodity's convenience yield is close to zero, the futures market for that commodity is most likely:
    (A) in contango.
    (B) in backwardation.
    (C) at fair value.

15. Victrix is a hedge fund that has a 3-and-15 fee structure. Compared to hedge funds with 2-and-20 fee structures, Victrix charges higher:
    (A) management fees.
    (B) incentive fees.
    (C) redemption fees.

16. For a given set of underlying real estate properties, the type of real estate index that is most likely to have the lowest standard deviation is a(n):
    (A) repeat sales index.
    (B) appraisal index.
    (C) REIT trading price index.

17. Which of the following best describes a benefit from investing in commodities? Commodities:
    (A) can serve as a hedge against inflation.
    (B) benefit from markets oscillating between contango and backwardation.
    (C) have a strong positive correlation with stock and bond prices.

18. The period of time within which a hedge fund must fulfill a redemption request is the:
    (A) lockup period.
    (B) notice period.
    (C) withdrawal period.

19. Indices for alternative investments are least likely to exhibit:
    (A) backfill bias.
    (B) time-period bias.
    (C) survivorship bias.

20. The formative stage of venture capital investing when capital is furnished for market research and product development is best characterized as the:
    (A) angel investing stage.
    (B) seed stage.
    (C) early stage.

21. A hedge fund has a 2-and-20 fee structure with a soft hurdle rate of 5% and a high water mark. Incentive fees are calculated net of management fees. The fund's gross return is 15% in Year 1, -10% in Year 2, and 30% in Year 3. Incentive fees for Year 3 will be:

    (A) less than 20% of the increase in value in Year 3 after management fees.

    (B) equal to 20% of the increase in value in Year 3 after management fees.

    (C) greater than 20% of the increase in value in Year 3 after management fees.

22. Investments in infrastructure assets that will be constructed in the future are most accurately described as:

    (A) brownfield infrastructure investments.

    (B) greenfield infrastructure investments.

    (C) openfield infrastructure investments.

23. A portfolio manager who adds commodities to a portfolio of traditional investments is most likely seeking to:

    (A) increase expected returns only.

    (B) decrease portfolio variance only.

    (C) both increase expected returns and decrease portfolio variance.

24. Which of the following risk measures is based on downside deviation?

    (A) Sortino ratio.

    (B) Treynor ratio.

    (C) Sharpe ratio.

25. A hedge fund that employs a fundamental growth strategy using equity securities is most likely to seek out shares of companies that are:

    (A) growing revenues and earnings rapidly.

    (B) undervalued only.

    (C) either undervalued or overvalued.

26. The stage at which venture capital financing is used to fund market research and product development is best characterized as the:

    (A) seed stage.

    (B) early stage.

    (C) angel investing stage.

27. Compared to a traditional mutual fund, a hedge fund is more likelyto feature:
    (A) lower leverage.
    (B) higher liquidity.
    (C) higher fees.

28. An example of a relative value hedge fund strategy is:
    (A) merger arbitrage.
    (B) market neutral.
    (C) convertible arbitrage.

29. With respect to venture capital, the term "mezzanine-stage financing" is used to describe the financing:
    (A) to initiate commercial manufacturing.
    (B) to prepare for an initial public offering.
    (C) that supports product development and market research.

30. Lou Gold, CFA, is screening all stocks on an exchange and grouping them by the industry in which they operate. Gold then selects stocks at random from each industry and combines the selected stocks to form an index to represent the performance of all stocks on the exchange. Gold's screening process is best described as:
    (A) stratified sampling.
    (B) simple random sampling.
    (C) systematic random sampling.

31. Social infrastructure assets most likely include:
    (A) broadcasting towers.
    (B) waste treatment plants.
    (C) health care facilities.

32. An additional risk of direct investment in real estate, which is not typically a significant risk in a portfolio of traditional investments, is:
    (A) liquidity risk.
    (B) market risk.
    (C) counterparty risk.

33. In a 2-and-20 hedge fund fee structure, the "2" refers to a hedge fund's
    (A) incentive fee.
    (B) hurdle rate.
    (C) management fee.

34. A portfolio manager who adds hedge funds to a portfolio of traditional securities is most likely seeking to:
    (A) decrease portfolio variance only.
    (B) increase expected returns only.
    (C) both increase expected returns and decrease portfolio variance.

35. An equity hedge fund strategy that focuses primarily on exploiting overvalued securities is best described as a(n):
    (A) fundamental value strategy.
    (B) event driven strategy.
    (C) short bias strategy.

36. A hedge fund that charges an incentive fee on all profits, but only if the fund's rate of return exceeds a stated benchmark, is said to have a:
    (A) high water mark.
    (B) soft hurdle rate.
    (C) hard hurdle rate.

37. A private equity firm that provides equity capital to a publicly traded company to finance the company's restructuring, but does not take the company private, is best described as engaging in:
    (A) private investment in public equity.
    (B) angel investing.
    (C) mezzanine-stage financing.