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QUESTION NO: 1

Which of the following is a key property of fiat currency?

- A. It has been devalued
- B. It has been declared legal tender
- C. It operates in an exchange rate mechanism
- D. It is pegged to the US dollar

ANSWER: B

Explanation:

“It has been declared legal tender” is the key property. Fiat currency has value because a government or monetary authority issues it, recognises it as legal tender and supports its use within the economy, rather than because it can be redeemed for a fixed quantity of a commodity such as gold. Legal-tender status means the currency is formally recognised for settling monetary obligations in the relevant jurisdiction. This status, together with public confidence, the credibility of the issuer and monetary-policy arrangements, enables fiat money to function as a generally accepted medium of exchange, unit of account and store of value.

In modern monetary systems, banknotes and coins are commonly issued under a statutory framework specifying their legal-tender status. The Bank of England explains that UK banknotes are a form of money whose acceptability rests on confidence and the institutional framework surrounding their issuance; it also clarifies the legal meaning of legal tender. The International Monetary Fund similarly describes contemporary monetary systems as operating with national currencies issued by central banks rather than commodity-convertible money. These points establish legal recognition by the state as a central characteristic of fiat currency. See the [Bank of England's explanation of legal tender](#) and the [IMF's overview of money](#).

QUESTION NO: 2

An investor deposits \$1,000 into an account that pays interest at the rate of 3% per year. If the interest is credited to the account at the end of the year and the investor leaves the money in the account for 5 years, how much money will be in the account at the end of the fifth year?

- A. \$1,150.00
- B. \$1,157.63
- C. \$1,159.27
- D. \$1,276.28

ANSWER: C

Explanation:

The correct result is **\$1,159.27**, because interest credited at the end of each year remains in the account and itself earns interest in subsequent years. This is annual compound interest. The future value is calculated as the initial deposit multiplied by one plus the annual interest rate, raised to the number of years: $\$1,000 \times (1 + 0.03)^5$. This gives $\$1,000 \times 1.1592740743 = \$1,159.2740743$. Financial amounts are normally expressed to the nearest cent, so the balance at the end of the fifth year is \$1,159.27. The timing stated in the question is important: crediting interest annually means that the first year's 3% is added to the account at year-end, and each later year's 3% is applied to the increased balance. This reflects the time value of money and the standard compound-growth approach used in investment calculations. For an overview of compound-interest calculations, see the [U.S. Securities and Exchange Commission Investor.gov guide to compound interest](#). A formula-based illustration is also available from [Math is Fun](#).

QUESTION NO: 3

Capital gains tax CGT is charged:

- A. On any asset at the time of its disposal
- B. At a reduced rate for pensions
- C. On the transfer of assets upon death
- D. On gains arising from the sale of an asset

ANSWER: D

Explanation:

“On gains arising from the sale of an asset” is correct because capital gains tax is a tax on the profit or gain made when an individual disposes of a chargeable asset, rather than a tax on the asset’s full sale price or value. In straightforward terms, the gain is generally calculated by comparing the disposal proceeds with the allowable acquisition cost and allowable expenditure connected with acquiring, improving, or disposing of the asset. The resulting figure may then be affected by available losses, the annual exempt amount where applicable, reliefs, and the taxpayer’s circumstances before the CGT liability is determined.

For ICWIM purposes, the key principle is to distinguish the underlying asset from the economic gain generated on its disposal. A sale is a common form of disposal and therefore provides the clearest expression of the charging event in this question. HM Revenue & Customs states that CGT may be payable when an asset is sold or otherwise disposed of and that the tax concerns the gain made. This framing supports the answer precisely. See [GOV.UK: Capital Gains Tax](#) and [GOV.UK: Work out your gain](#).

QUESTION NO: 4

When investors wish to sell units in mutual funds, there is a risk of the fund being gated. Why might this happen?

- A. To ensure any tax deferral benefits are not lost
- B. To ensure that the commission as a proportion of the fund remains small
- C. Because the investor has not held the units past the 'lock-in' period
- D. To allow fund managers to raise enough funds to pay out to those wishing to sell their units

ANSWER: D

Explanation:

To allow fund managers to raise enough funds to pay out to those wishing to sell their units is correct. A redemption gate is a temporary restriction or limit on investors’ ability to redeem fund units, generally used where redemption requests are unusually large or where the fund’s assets cannot readily be sold for cash without damaging remaining investors’ interests. A mutual fund may hold less-liquid investments, such as property, unquoted securities, thinly traded bonds, or assets in stressed markets. Meeting a sudden volume of sales immediately could force the manager to dispose of holdings at depressed prices. A gate gives the manager time to generate the necessary liquidity through orderly sales, while seeking fair treatment between redeeming investors and those who remain in the fund. The precise mechanism can vary: redemptions may be deferred, processed in stages, or limited to a stated proportion of the fund on a dealing day. In the UK, authorised fund managers have powers and duties relating to suspension and the orderly operation of dealing where exceptional circumstances make this necessary. See the FCA Handbook provisions on suspension and restart of dealings in [COLL 7.2](#) and the FCA’s discussion of [liquidity and fund-manager responsibilities](#).

QUESTION NO: 5

Government spending, that is financed through borrowing, within an expansionary fiscal policy can have the effect of:

- A. Crowding out private-sector spending

- B. Lowering interest rates
- C. Reducing the money supply
- D. Increasing banks' reserves

ANSWER: A

Explanation:

Crowding out private-sector spending is the appropriate effect to identify. When a government funds expansionary expenditure by borrowing, it enters the market for loanable funds alongside households and businesses. If the economy's available saving and productive capacity are relatively constrained, additional government demand for borrowing can place upward pressure on interest rates and/or absorb funds that might otherwise have financed private investment. Businesses may then defer or scale back investment projects because their cost of finance has risen, while interest-sensitive household expenditure may also be dampened. This mechanism is known as the crowding-out effect.

The extent of crowding out is not fixed: it depends on economic conditions. It is more likely to be material when the economy is near full capacity and monetary policy does not accommodate the fiscal expansion. Conversely, when there is substantial spare capacity or monetary policy keeps financing conditions loose, the initial increase in aggregate demand may have a larger effect and crowding out may be limited. Nevertheless, borrowing-financed fiscal expansion can produce crowding out, making it the correct answer. The IMF discusses how fiscal policy, public debt and financing conditions interact in its [Fiscal Monitor](#); the Bank of England explains the role of interest rates in borrowing and spending decisions in its [Bank Rate](#) guidance.

QUESTION NO: 6

Offshore foundations are often used as a suitable alternative to which similar type of arrangement?

- A. Limited liability partnerships
- B. Credit unions
- C. Trusts
- D. SICAVs

ANSWER: C

Explanation:

Trusts is correct. An offshore foundation is commonly used for wealth-holding, succession planning, asset protection and philanthropic purposes that might otherwise be addressed through a trust. Like a trust, it can separate assets from an individual founder and provide a framework for assets to be managed and applied for specified beneficiaries or purposes under constitutional documents and governance rules. However, a foundation generally has its own separate legal personality, unlike a traditional common-law trust, where trustees hold legal title to trust property for beneficiaries. This feature can make foundations particularly useful in jurisdictions or family circumstances where the trust concept is less familiar, less readily recognised, or where a corporate-style governance structure is preferred. The founder can define the foundation's objects, appoint or influence governing bodies subject to the applicable law and documents, and establish rules for distributions or other benefits. In international wealth planning, the choice between a trust and a foundation requires consideration of the relevant jurisdictions' tax treatment, forced-heirship rules, disclosure obligations, creditor rules, and recognition of legal arrangements. CISI's wealth-management material treats foundations as an important alternative vehicle for functions traditionally performed by trusts. See the [CISI International Certificate in Wealth & Investment Management](#) overview and the [OECD beneficial-ownership guidance](#) for the wider transparency context relevant to legal arrangements and legal persons.

QUESTION NO: 7

Why would a government's expansionary fiscal policy lead to a larger budget deficit?

- A. Less money is collected in taxes
- B. Interest rates fall faster than usual
- C. Private sector spending drops rapidly
- D. Government spending is funded through borrowing

ANSWER: D

Explanation:

Government spending is funded through borrowing is the best answer because expansionary fiscal policy deliberately increases aggregate demand through higher public expenditure, tax reductions, or both. Where this policy increases expenditure beyond the government's available tax and other receipts, the resulting financing gap must be met by borrowing. That borrowing is normally raised by issuing government securities, such as Treasury bills or government bonds. The budget deficit is therefore larger because government outlays exceed its revenue for the period, requiring a greater amount of debt financing.

In practice, the precise deficit effect depends on the scale of the additional spending, the tax measures adopted, and any subsequent change in tax receipts as activity responds. Nevertheless, borrowing is the direct financing mechanism for the shortfall created when expansionary fiscal measures leave public spending above public revenue. This distinction is important in investment analysis: a larger fiscal deficit can increase government debt issuance and affect bond-market supply, yields, and debt-servicing costs. The UK Office for Budget Responsibility explains the relationship between public-sector borrowing and the gap between government spending and receipts in its [public finances guidance](#). See also the UK government's [Public sector finances](#) statistics for the reporting of borrowing and fiscal balances.

QUESTION NO: 8

The effect of gearing within an investment trust company is that it:

- A. Reduces the trust's premium or discount
- B. Raises initial charges
- C. Lowers operating expenses
- D. Magnifies profits and losses

ANSWER: D

Explanation:

Gearing within an investment trust company magnifies profits and losses. An investment trust is a closed-ended company and may borrow money, or use other forms of leverage, to invest more than the shareholders' capital alone. This means its portfolio has greater market exposure than it would have on an ungeared basis. When the investments held rise in value, returns accrue on this larger pool of invested assets, potentially increasing the return attributable to shareholders after borrowing costs. Conversely, when portfolio values fall, the loss applies to the enlarged investment exposure and can lead to a proportionately greater decline in net asset value per share. Gearing therefore increases both the potential return and the investment risk, making shareholder outcomes more volatile. The extent of this effect depends on the amount and cost of borrowing, the performance of the underlying assets, and whether the trust uses fixed or flexible borrowing arrangements. Investors should consider a trust's gearing level as part of assessing its risk profile and suitability. The Association of Investment Companies explains that gearing can enhance returns in rising markets but also increases losses in falling markets. See [the AIC's explanation of gearing](#) and the FCA's [guidance on investment funds](#).

QUESTION NO: 9

A bullet bond portfolio can have an advantage over a barbell bond portfolio because:

- A. It is always riding the yield curve

- B. It only invests in short-dated bonds
- C. The gross redemption yield is always higher
- D. A bullet portfolio does not require regular rebalancing

ANSWER: D

Explanation:

A **bullet portfolio does not require regular rebalancing** is the correct answer. A bullet strategy concentrates bond holdings around a defined maturity date or narrow maturity range. This creates a relatively focused maturity profile, allowing the portfolio manager to align the bonds with a known future cash-flow need, liability date, or planned investment horizon. As time passes, the portfolio's holdings generally move towards that intended maturity together, rather than requiring the manager to maintain allocations at two widely separated ends of the maturity spectrum.

This can offer a practical operational advantage: the strategy is comparatively straightforward to monitor and can involve less ongoing trading solely to preserve its intended shape. The investor can plan around the maturity proceeds and, where the portfolio is held to maturity, receive redemption proceeds near the targeted date. This focused approach may therefore reduce turnover and associated dealing costs relative to a strategy whose desired maturity exposures must be actively maintained over time.

Bullet and barbell structures are recognised approaches to managing interest-rate exposure and maturity positioning in fixed-income portfolios. Further background is available from [Investopedia's overview of bullet bonds](#) and [its explanation of the barbell strategy](#).

QUESTION NO: 10

Which of the following issues is at the heart of fiduciary relationships with clients?

- A. Commission
- B. Risk
- C. Service
- D. Suitability

ANSWER: D

Explanation:

Suitability is at the heart of a fiduciary relationship because the client places trust and confidence in the adviser or investment manager to exercise professional judgement for the client's benefit. In practice, this means a recommendation or discretionary investment decision must be grounded in a proper understanding of the client's objectives, investment horizon, financial circumstances, capacity for loss, knowledge and experience, and attitude to risk. Suitability is therefore not a one-off administrative exercise: it is the practical expression of the duty to place the client's interests at the centre of advice and investment decisions. A suitable recommendation must be capable of meeting the client's needs and must remain appropriate in the context of the mandate and available information. This principle also supports clear records, appropriate reviews, and communication that enables the client to understand the proposed course of action. The FCA's suitability requirements require firms to take reasonable steps to ensure that personal recommendations are suitable for clients, reinforcing why suitability is a core client-protection and fiduciary concept. See the [FCA Handbook, COBS 9A: Suitability](#) and the [FCA's investment-management guidance](#).

QUESTION NO: 11

What is the expected outcome of an assessment of a client's health protection priorities?

- A. It will generate a new health policy
- B. It will remove the need to focus on other financial planning areas

- C. It will minimise the risk that policy exclusions will be imposed
- D. It will quantify the extent to which the client should consider action

ANSWER: D

Explanation:

An assessment of a client's health protection priorities should establish and quantify the potential financial consequences of ill health, injury or disability, and identify the scale of any gap between the client's available resources and their needs. This includes considering likely changes to income, essential expenditure, existing employer or state benefits, savings, insurance arrangements, dependants and the period for which support could be required. The resulting analysis gives the client and adviser an evidence-based indication of whether action should be considered and, if so, the likely extent and priority of that action within the wider financial plan. Therefore, "It will quantify the extent to which the client should consider action" is the expected outcome. Health protection planning is needs-led: the assessment helps frame a proportionate recommendation or next step based on the client's individual circumstances, objectives and capacity to address identified risks. The UK MoneyHelper guidance on protection insurance similarly highlights the importance of considering how illness or injury could affect income and the ability to meet bills: [MoneyHelper: types of insurance](#). This approach is also consistent with the CISI's focus on applying financial-planning knowledge to client circumstances: [CISI Wealth Management qualifications](#).

QUESTION NO: 12

A main feature of critical illness cover is that it:

- A. Provides a regular income if the policyholder requires long-term care
- B. Covers the cost of routine medical procedures
- C. Replaces any income lost due to ill health
- D. Pays a lump sum upon diagnosis of a specified medical condition

ANSWER: D

Explanation:

Critical illness cover pays a tax-free lump sum when the insured person is diagnosed with a serious condition specifically covered by the policy, provided the policy's definition of that condition is met and any applicable survival period has passed. The amount is normally selected when the cover begins and is paid as a single cash benefit rather than as reimbursement for particular treatment or as an ongoing income. This allows the recipient to decide how best to use the money during a period of serious illness: for example, repaying or reducing a mortgage, replacing funds needed for household bills, paying for home adaptations, arranging care, or meeting other costs while recovering. Cover is based on the conditions and definitions stated in the contract, commonly including conditions such as cancer, heart attack, and stroke, so a diagnosis alone does not automatically result in a payment unless it satisfies the relevant policy wording. The Association of British Insurers explains that critical illness insurance provides a lump sum if the policyholder is diagnosed with one of the specified conditions: [ABI: Critical illness insurance](#). Further consumer guidance on the product and its purpose is available from [MoneyHelper: Critical illness insurance](#).

QUESTION NO: 13

Which currency is most heavily traded on international markets?

- A. British pound sterling
- B. US dollar
- C. Japanese yen
- D. Euro

ANSWER: B

Explanation:

The US dollar is the most heavily traded currency in international foreign-exchange markets. Foreign exchange is conventionally measured by counting both sides of each currency transaction, and the US dollar is on one side of the overwhelming majority of trades. Its central role reflects the depth and liquidity of US financial markets, its widespread use for cross-border trade and commodity pricing, and its importance in international funding, investment and central-bank reserves. These features mean that market participants commonly use the US dollar to exchange one non-US currency for another, so it acts as the principal vehicle currency in global FX dealing. The Bank for International Settlements' Triennial Central Bank Survey is the leading global source for FX market turnover data. Its 2022 survey found that the US dollar was involved in 88% of all foreign-exchange trades, substantially more than any other currency. This percentage does not represent a share that must total 100%, since every FX transaction involves two currencies and turnover is allocated to each currency appearing in the trade. See the [BIS Triennial Central Bank Survey 2022: FX turnover](#) and the [BIS survey report](#).

QUESTION NO: 14

What is a key feature of offshore trusts that can make them attractive to wealthy UK clients?

- A. They are not publicly registered
- B. The offshore trust is only liable for local taxes
- C. The beneficiaries never have to pay inheritance tax
- D. The offshore trust is usually a less complex product to understand

ANSWER: A

Explanation:

They are not publicly registered is the key feature. An offshore trust may provide a greater degree of privacy than a comparable UK arrangement because, where it has no relevant UK connection or UK tax liability, it may not fall within the UK Trust Registration Service requirements. This can be attractive to wealthy clients who place legitimate value on confidentiality around family wealth, asset ownership, and succession planning. Privacy does not mean secrecy from tax authorities or that reporting obligations can be ignored: trustees and relevant persons must still meet applicable tax, anti-money-laundering, disclosure, and information-exchange requirements. In particular, UK-resident settlors and beneficiaries can remain subject to UK tax rules, and non-UK trusts can require registration where they incur UK tax liabilities, acquire UK land, or enter certain business relationships in the UK. The attraction is therefore the potential for reduced public visibility in appropriate circumstances, rather than an exemption from legal, regulatory, or tax compliance. HMRC outlines the circumstances in which trusts must be registered in its [Trust Registration Service guidance](#). Wider international transparency is supported by the OECD's [Common Reporting Standard](#), under which financial-account information may be exchanged between tax authorities.

QUESTION NO: 15

The return on a **whole-of-life unit-linked policy** is:

- A. Directly related to the performance of the insurance company's fund
- B. Related to the Consumer Price Index (CPI)
- C. Linked to the rate of inflation
- D. Dependent on prevailing interest rates

ANSWER: A

Explanation:

Directly related to the performance of the insurance company's fund is correct because a unit-linked whole-of-life policy combines permanent life assurance with an investment element whose value is represented by units. Premiums, after applicable charges, are allocated to one or more linked funds, and the policy value changes as the price of those units changes. The investment return available to the policyholder is therefore driven by the performance of the assets held in the linked fund or funds, such as equities, bonds, property, or cash, rather than being a fixed contractual return declared by the insurer. Whole-of-life describes the duration of the life cover: it is intended to remain in force for the insured's lifetime, subject to policy terms and sufficient value or premiums to meet charges. It does not alter the unit-linked basis on which the investment value is calculated. In practice, the amount payable on death may be the policy's unit value, sometimes subject to a specified minimum death benefit, depending on the contract. The FCA's rules distinguish unit-linked business as long-term insurance where benefits are determined by reference to units linked to underlying assets. This structure means fund performance is the central determinant of return and policy value. See the [FCA Handbook, COBS 21](#) and the [Association of British Insurers' explanation of unit-linked policies](#).

QUESTION NO: 16

When redemption yields are quoted on a net-of-tax basis, this is so that:

- A. The default risk can be taken into account
- B. A risk of inflation rising unexpectedly and its effect on the real value of the bond's coupon payments and redemption payment can be taken into account
- C. An investor can reinvest the interest payment at the same net redemption yield
- D. A direct comparison can be made of the net return to the investor

ANSWER: D

Explanation:

A direct comparison can be made of the net return to the investor is correct because a net-of-tax redemption yield reflects the return remaining after the investor's applicable tax liability on income and/or gains has been allowed for. This presents the economic return that the investor actually retains, rather than a gross figure that may overstate the benefit available to them. Quoting yields on this basis is particularly useful when assessing investments with differing tax treatments, such as securities where returns arise in different forms or are subject to different rates of tax. It supports a like-for-like comparison of the investor's expected after-tax outcome over the instrument's life, assuming the stated tax treatment and yield assumptions apply. In wealth and investment management, suitability and performance assessment should focus on the client's personal circumstances, including tax status, because tax can materially affect the value of an investment return. The UK Financial Conduct Authority's guidance on communicating investment information emphasises that firms should provide information that is clear, fair and not misleading; using a net return where relevant helps convey the amount meaningful to the investor. See the [FCA COBS 4.2 fair, clear and not misleading communications rules](#) and HMRC's [guidance on tax on savings interest](#).

QUESTION NO: 17

A manager expects corporate bond yields to fall relative to government bond yields of similar maturity because investor concerns about corporate default risk are easing. Which positioning is most consistent with this view?

- A. Overweighting corporate bonds relative to government bonds
- B. Overweighting government bonds relative to corporate bonds
- C. Holding only cash until maturity
- D. Selling corporate bonds and buying short-dated government bonds

ANSWER: A

Explanation:

Overweighting corporate bonds relative to government bonds is correct. The additional yield demanded by investors for holding corporate bonds rather than comparable government bonds is the credit spread. If credit spreads narrow, corporate bond prices should generally rise relative to government bonds, assuming other relevant factors remain unchanged.

Buying only short-dated government bonds primarily changes interest-rate exposure rather than expressing a view on credit-spread compression. Selling corporate bonds would be more consistent with an expectation that credit spreads will widen because of rising perceived default or liquidity risk.

QUESTION NO: 18

A stockbroking firm receives both buy and sell orders for the same security but from different clients. How can they best avoid a conflict of interest?

- A. Withdraw their services for the transaction
- B. Place orders as they are received from the clients
- C. Openly disclose all orders received to the clients
- D. Process the sell orders before the buy orders

ANSWER: B

Explanation:

“Place orders as they are received from the clients” is correct because objective, consistent sequencing is a core control for managing potential conflicts in client order handling. Where comparable client orders are received, processing them in the order of receipt limits the firm’s discretion to favour a particular client, account, or relationship. It supports fair treatment by ensuring that execution priority is determined by a documented and consistently applied process rather than by the firm’s own interests or preferences.

This approach reflects the client-order-handling requirements applicable to investment firms. The rules require firms to execute comparable client orders sequentially and promptly, unless the order characteristics or prevailing market conditions make that impracticable. A firm should also maintain arrangements that enable it to demonstrate fair allocation and execution of client orders. Appropriate records, clear procedures, and staff adherence to the order-handling policy are important in showing that all clients have been treated fairly when competing instructions arise.

The relevant UK requirements are set out in the FCA Handbook, [COBS 11.3: Client order handling](#), alongside the wider obligation to identify and manage conflicts in [SYSC 10.1: Conflicts of interest](#).

QUESTION NO: 19

Under an accumulation and maintenance trust, when does the trustees' discretion over payments normally cease (if at all)?

- A. On the death of the settlor
- B. On the death of the life tenant
- C. At the end of a prescribed period
- D. It continues indefinitely

ANSWER: C

Explanation:

“At the end of a prescribed period” is correct because an accumulation and maintenance trust is ordinarily drafted so that the trustees have powers to accumulate trust income and exercise discretion in applying income or capital for a beneficiary’s maintenance, education, or benefit during a defined trust period. The trust instrument specifies the event that ends that discretionary phase. This will commonly be expressed as a period ending when a beneficiary reaches a stated age, historically often no later than age 25 for the former inheritance-tax accumulation and maintenance trust regime. At that

endpoint, the beneficiary's interest typically becomes fixed or absolute under the terms of the settlement, so the trustees no longer have the same discretion over whether and when to make payments. The relevant period is therefore prescribed by the trust deed rather than being automatically determined by the settlor's or a life tenant's death. The historic statutory conditions for this type of trust included a requirement for the beneficiary to become absolutely entitled to the settled property by age 25; see section 71 of the Inheritance Tax Act 1984 at legislation.gov.uk. HMRC also discusses the former accumulation and maintenance trust rules in its [Inheritance Tax Manual](#).

QUESTION NO: 20

Your client estimates that they will require £50,000 of income annually to live off when they retire. Personal plus state pension will provide £40,000. They wish to retire in 25 years' time. It is estimated that they can earn 5% per annum, and inflation has been forecast at 2%. Interest rates are currently 1.5%. Allowing for inflation, what lump sum would they need to accrue to supplement their pension?

- A. £252,401
- B. £328,120
- C. £468,745
- D. £546,869

ANSWER: D

Explanation:

£546,869 is correct because the client has a current annual retirement-income shortfall of £10,000: required income of £50,000 less pension income of £40,000. This shortfall must first be increased for the expected 2% annual inflation over the 25 years to retirement. Thus, the first-year shortfall at retirement is $£10,000 \times 1.02^{25}$, or approximately £16,406. The expected nominal investment return is 5%; allowing for 2% inflation gives the exam-style real return of 3% per annum. Treating the required supplement as an inflation-linked income payable indefinitely, the capital required at retirement is calculated as a perpetuity: $£16,406 \div 0.03 =$ approximately £546,869 (with minor differences arising from rounding). The current 1.5% interest rate is not used because the question supplies the expected investment return and inflation assumptions needed to derive the real return. This approach reflects the core financial-planning principle that retirement-income needs should be assessed in real, inflation-adjusted terms, so that the purchasing power of withdrawals is maintained. The Bank of England explains the importance of inflation to changes in purchasing power: [Bank of England: Inflation](#). For the underlying perpetuity valuation relationship, see [Investopedia: Perpetuity](#).

QUESTION NO: 21

During a period of growth in consumer income the demand curve for a normal product would:

- A. Shift to the left
- B. Remain static
- C. Shift to the right
- D. Begin to curve upwards

ANSWER: C

Explanation:

"Shift to the right" is correct because a normal product has a positive income elasticity of demand: as consumers' incomes rise, they are both willing and able to buy a greater quantity at each given price. This is represented by an outward, or rightward, shift of the entire demand curve. The shift is distinct from movement along the existing curve, which occurs when the product's own price changes. Here, the relevant change is consumer income, a non-price determinant of demand, so the relationship between price and quantity demanded is recalculated at every price level. For example, higher disposable income may lead consumers to purchase more restaurant meals, branded clothing, or other goods and services regarded as

normal products. The extent of the shift depends on the size of the income increase and the product's income elasticity, but its direction is rightward so long as the good remains normal. This basic distinction between changes in demand and changes in quantity demanded is central to interpreting supply-and-demand diagrams and assessing how economic growth can affect markets. See the [Encyclopaedia Britannica explanation of demand](#) and the [OpenStax discussion of shifts in demand](#).

QUESTION NO: 22

A market which employs an electronic order book to match buyers with sellers in strict order by price is known as:

- A. Order-driven
- B. Quote-driven
- C. On-exchange
- D. Over-the-counter

ANSWER: A

Explanation:

Order-driven is correct because this market structure uses a central order book containing participants' executable buy and sell orders. The trading system automatically matches compatible orders according to defined priority rules, principally price priority: higher-priced buy orders take precedence over lower-priced buy orders, while lower-priced sell orders take precedence over higher-priced sell orders. Where orders are at the same price, time priority will commonly determine which order is executed first. This is often described as price-time priority. The order book therefore provides the mechanism through which supply and demand interact and transactions are formed, rather than relying on a dealer to continuously quote bid and offer prices. The London Stock Exchange describes its electronic order book as matching orders using price and time priority, illustrating the core operation of an order-driven market. This structure supports orderly execution by applying consistent matching rules to orders entered into the book. See the London Stock Exchange's [trading services information](#) and the Financial Conduct Authority's [market conduct guidance](#) for related UK market-structure context.

QUESTION NO: 23

An inherent disadvantage with a defined contribution pension scheme is that:

- A. The level of retirement income is not known before retirement
- B. Employers never contribute to the scheme
- C. Gains within the scheme are subject to capital gains tax
- D. Employees always have to contribute more than employers

ANSWER: A

Explanation:

The level of retirement income is not known before retirement is correct because, in a defined contribution pension scheme, contributions are paid into an individual pension pot and invested. The eventual value of that pot depends on the amount contributed, investment performance, charges, the period over which money remains invested, and the choices made when benefits are taken. These variables cannot be known with certainty at the outset. Unlike a pension arrangement that promises a specified retirement income according to a formula, a defined contribution arrangement does not guarantee the level of income that the accumulated fund will provide in retirement.

This uncertainty is an inherent consideration for scheme members and advisers when assessing whether projected savings are likely to meet retirement objectives. A member may obtain illustrations and use pension-planning tools, but these are estimates based on assumptions rather than assured outcomes. The UK Government explains that the value of a defined contribution pension pot can rise or fall according to investment performance, and that the retirement income it can produce

depends on the value of the pot and how it is accessed. See [GOV.UK: Pension types](#) and [MoneyHelper: Defined contribution pensions](#).

QUESTION NO: 24

How would an active fund manager seek to avoid underperforming their peer group when deciding on asset allocation?

- A. Through the use of asset allocation by consensus
- B. By assessing the prospects for each main asset class
- C. By hedging currency and market risk
- D. Through the use of quantitative models

ANSWER: A

Explanation:

Through the use of asset allocation by consensus is correct because the objective described is relative performance against a peer group, rather than simply maximising absolute return. A consensus asset allocation reflects the broad market view held by investment professionals on the relative attractions of the principal asset classes. By positioning the portfolio broadly in line with that consensus, the manager reduces the risk of making a large, idiosyncratic allocation call that differs materially from competitors. This helps control peer-relative risk: if a major asset class performs particularly strongly or weakly, the portfolio is less likely to be substantially underweight or overweight compared with comparable funds.

This approach is particularly relevant where a manager is assessed against a peer universe and wishes to avoid a materially poor ranking. The manager may still make limited active deviations from consensus where they have conviction, but consensus provides a practical central position from which to manage the risk of underperforming the group. This distinction between absolute and relative risk is consistent with the CFA Institute's discussion of benchmark-relative portfolio management and active risk. See [CFA Institute: Active Equity Investing and Portfolio Construction](#) and [CFA Institute: Active Share and Tracking Error](#).

QUESTION NO: 25

Which of the following instruments is currently outside of those covered by insider dealing rules?

- A. Bonds
- B. Commodities
- C. Depositary Receipts
- D. Warrants

ANSWER: B

Explanation:

Commodities is correct when it means the underlying physical commodity, such as physical gold, crude oil or wheat. The UK market-abuse regime prohibits insider dealing in relation to financial instruments within its scope. That scope includes instruments admitted to trading, or for which admission has been requested, on regulated markets, multilateral trading facilities or organised trading facilities, as well as related instruments whose value depends on those instruments. Bonds, depositary receipts and warrants can all be financial instruments within this regime when the relevant trading and scope conditions are met.

A physical commodity itself is not a financial instrument merely because it is traded or has a market price. It is therefore outside the core insider-dealing prohibition applicable to financial instruments. This distinction is important: commodity *derivatives*, such as futures, options and swaps, may fall within the market-abuse rules, including provisions relating to commodity derivatives and related spot commodity contracts. Physical commodity markets may also be subject to other laws and regulatory controls, including rules addressing manipulation or misconduct. The relevant scope of the UK Market Abuse

Regulation is set out in Article 2, while the FCA provides practical market-abuse guidance at [UK MAR, Article 2](#) and [FCA: Market abuse](#).

QUESTION NO: 26

A manufacturing company has increased its level of output to the point where marginal costs start to exceed average total costs. What does this indicate?

- A. Fixed costs are likely to fall
- B. The market has become saturated
- C. Variable costs are now negligible
- D. Productive capacity is constrained

ANSWER: D

Explanation:

Productive capacity is constrained is correct because marginal cost is the additional cost of producing one more unit, whereas average total cost is total cost per unit across all output. Marginal cost pulls the average: when marginal cost exceeds average total cost, each additional unit costs more than the existing average, so average total cost begins to rise. This occurs after the firm has reached the output level that minimises average total cost, often called its minimum efficient scale in the relevant short-run context.

For a manufacturing business, this pattern commonly reflects constraints in productive capacity. As output is pushed beyond the most efficient operating level, fixed plant, machinery, workspace, and supervisory resources may be used more intensively. Bottlenecks, overtime, congestion, extra maintenance, and diminishing marginal productivity of variable inputs can make every further unit relatively more expensive to produce. The relationship between marginal cost and average total cost is therefore a useful signal that the business is operating beyond its lowest-cost output range and that capacity expansion or operational changes may be needed if higher output is to be sustained efficiently.

See [OpenStax, Costs in the Short Run](#) and [Economics Help, relationship between marginal and average cost](#).

QUESTION NO: 27

What is the expected outcome of an assessment of a client's health protection priorities?

- A. It will generate a new health policy
- B. It will remove the need to focus on other financial planning areas
- C. It will minimise the risk that policy exclusions will be imposed
- D. It will quantify the extent to which the client should consider action

ANSWER: D

Explanation:

It will quantify the extent to which the client should consider action. A health-protection assessment is a fact-finding and needs-analysis exercise: its purpose is to establish the financial consequences if illness or injury prevents the client from working or creates additional care-related costs. The adviser gathers information on income, regular expenditure, liabilities, dependants, employer sick-pay arrangements, existing insurance, savings and the client's ability to maintain their lifestyle during a prolonged absence from work. This permits the adviser and client to identify any shortfall, estimate the amount and duration of protection that may be appropriate, and decide how urgently action should be considered.

This outcome supports a suitability-led advice process. The assessment supplies evidence about the client's needs, objectives and financial circumstances before any recommendation is made; it does not itself dictate a particular product or underwriting outcome. The Financial Conduct Authority's suitability requirements require firms to obtain the information

necessary to understand a client's needs and recommend a personally suitable course of action. See the FCA's [COBS 9A suitability rules](#). For consumer context on assessing the financial impact of illness and considering income protection, see [MoneyHelper's income protection guidance](#).