

## Errata for CFA Program Level II Mock Exams

Updated 12 April 2013

To be fair to all candidates, CFA Institute does not respond directly to individual candidate inquiries. If you have a question concerning CFA Program content, please contact CFA Institute (info@cfa institute.org) to have potential errata investigated. Corrections below are in **bold** and new corrections will be shown in **red**.

### Morning Session

Question #4: Feedback should read as follows:

“Prem also violated **Standard V (B) Standard V (B) Communication with Clients and Prospective Clients** by citing dated tea production information.” and not “Prem also violated Standard IV (B) Communication with Clients by citing dated tea production information.”

### Afternoon Session

Question #10:

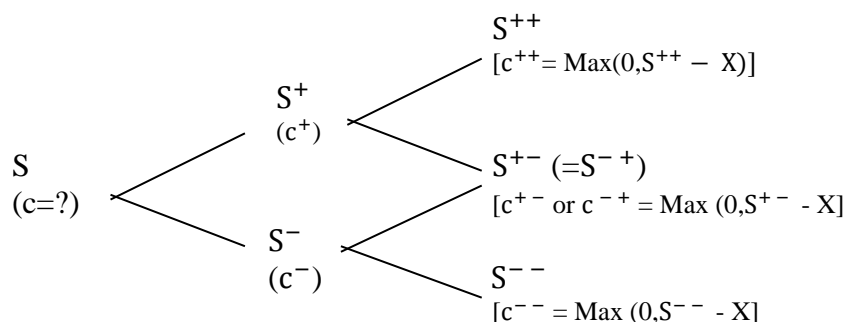
10. The price of IIG’s option on LAT Transport valued according to a two-period binomial model is *closest* to:

- A. EUR 2.0 million
- B. EUR 3.7 million
- C. EUR 5.6 million

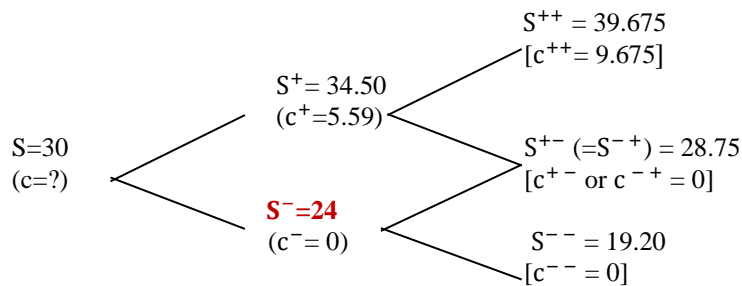
“Option Markets and Contracts” by Don M. Chance, CFA  
2013 Modular Level II, Vol 6, Reading 50, Section 6.2  
Study Session 17-50-b

Calculate and interpret prices of interest rate options and options on assets using one- and two-period binomial models.

**B is correct.** According to the two-period binomial model:



where  $S$  = value of the underlying equity or EUR 30 million (50% of EUR 60 million), therefore stated in EUR millions:



**The value of a call is:**

$$c^+ = \frac{\pi c^{++} + (1 - \pi) c^{+-}}{1 + r} = \frac{0.6286 \times 9.675 + [(1 - 0.6286) \times 0]}{1 + 0.02} = 5.96$$

$$c = \frac{\pi c^+ + (1 - \pi) c^-}{1 + r} = \frac{(0.6286 \times 5.96) + [(1 - 0.6286) \times 0]}{1 + 0.02} = 3.67$$

$$\text{Where } \pi = \frac{1 + r - d}{u - d} = \frac{1 + 0.02 - 0.80}{1.15 - 0.80} = 0.6286$$

Solving backwards over two periods,  **$c = \text{EUR } 3,670,000$** . IIG has an option to purchase a EUR 30 million share for the present value of EUR 2 million (32 million future purchase price – 30 million repayment of loan). The option is priced cheaper than the EUR 3.67 million fair value indicated in the two-step binomial model.