

Association for Financial Professionals (AFP) Practice Exam (Sample)

Study Guide



Everything you need from our exam experts!

This is a sample study guide. To access the full version with hundreds of questions,

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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Don't worry about getting everything right, your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 - 45 minutes). Review a handful of questions, reflect on the explanations, and take breaks to retain information better.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning.

7. Use Other Tools

Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly — adapt the tips above to fit your pace and learning style. You've got this!

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Questions

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- 1. Which risk is associated with purchasing asset-backed commercial paper (ABCP) denominated in a foreign currency?**
 - A. Liquidity risk only**
 - B. Price risk only**
 - C. Liquidity and foreign exchange risk**
 - D. Credit risk only**
- 2. Which risk increases when market interest rates fall?**
 - A. Price risk**
 - B. Marketability risk**
 - C. Reinvestment risk**
 - D. Liquidity risk**
- 3. Why might a company initiate a reverse stock split?**
 - A. To increase share liquidity**
 - B. To lower the stock price for greater accessibility**
 - C. To prevent shares from being delisted**
 - D. To enhance dividend payouts**
- 4. What is a bond's coupon rate?**
 - A. The total return an investor can expect from a bond**
 - B. The interest rate that a bond issuer pays to bondholders**
 - C. The price at which the bond is issued**
 - D. The risk premium associated with the bond**
- 5. Which characteristic distinguishes off-balance-sheet financing?**
 - A. It involves high-interest rates for short-term loans**
 - B. It appears on the balance sheet**
 - C. It does not appear on the balance sheet**
 - D. It requires significant collateral**

6. Which provision is NOT typically included in a debt contract?

- A. Terms by which the company will provide funds for redemption**
- B. Parent corporation comfort letters**
- C. Covenants**
- D. Representations and warranties**

7. In treasury management, which is a key activity?

- A. Conducting audits for compliance**
- B. Managing financial obligations**
- C. Evaluating investment opportunities**
- D. Consolidating financial reporting**

8. When a central bank sells government securities, what is the likely outcome?

- A. Increase in money supply**
- B. Decrease in money supply**
- C. Stable economic conditions**
- D. Inflation of currency value**

9. Which of the following is a characteristic of physical pooling?

- A. Funds can automatically transfer between different banks**
- B. All accounts are required to be in multiple currencies**
- C. Physical pooling usually requires the use of a single currency**
- D. Physical pooling involves only the bank's management**

10. What is the role of the advising bank in a letter of credit transaction?

- A. It issues the L/C on behalf of the buyer**
- B. It confirms the payment will be made**
- C. It advises the exporter of the L/C**
- D. It processes the payment from the buyer**

Answers

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1. C
2. C
3. C
4. B
5. C
6. B
7. B
8. B
9. C
10. C

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Explanations

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1. Which risk is associated with purchasing asset-backed commercial paper (ABCP) denominated in a foreign currency?

- A. Liquidity risk only**
- B. Price risk only**
- C. Liquidity and foreign exchange risk**
- D. Credit risk only**

Purchasing asset-backed commercial paper (ABCP) that is denominated in a foreign currency introduces both liquidity risk and foreign exchange risk. Liquidity risk arises because ABCP is typically a short-term investment, and if market conditions change or if there are any issues with the underlying assets, the ability to sell or rollover the investment can be severely impacted, especially in foreign markets where liquidity may be less favorable. Foreign exchange risk is critical when dealing with assets in a foreign currency. Fluctuations in exchange rates can affect the value of the ABCP when it is converted back to the investor's home currency. If the foreign currency weakens against the investor's domestic currency, the investment could yield a lower return or even a loss when the ABCP matures, even if the underlying assets performed well. Therefore, the combination of these two risks is significant when investing in ABCP denominated in foreign currency, making the correct answer that both liquidity risk and foreign exchange risk are involved in such an investment.

2. Which risk increases when market interest rates fall?

- A. Price risk**
- B. Marketability risk**
- C. Reinvestment risk**
- D. Liquidity risk**

When market interest rates fall, reinvestment risk increases. Reinvestment risk refers to the possibility that an investor may have to reinvest cash flows from an investment at lower interest rates than the original investment. When market rates decline, any interest or principal payments that are received may need to be reinvested at these lower rates, resulting in a reduced return on investment over time. For example, if you've invested in bonds that yield a certain interest rate and they pay off or mature during a period of declining rates, you may find it challenging to reinvest those proceeds at a yield that is comparable to your original investment. This scenario underscores the nature of reinvestment risk being more pronounced in a declining interest rate environment, where the potential earnings from reinvested funds diminish. Understanding this relationship is critical for financial professionals, as it highlights the importance of interest rate movements on an investment portfolio's overall performance and return expectations.

3. Why might a company initiate a reverse stock split?

- A. To increase share liquidity
- B. To lower the stock price for greater accessibility
- C. To prevent shares from being delisted**
- D. To enhance dividend payouts

A company may initiate a reverse stock split primarily to prevent its shares from being delisted. This situation often arises when a company's stock price falls below the minimum price required for listing on a stock exchange, such as the New York Stock Exchange or NASDAQ. By consolidating shares through a reverse stock split, the company reduces the total number of shares outstanding while increasing the price per share proportionately. This adjustment can help bring the stock price back above the required threshold, thus avoiding delisting, which could have dire implications for the company's visibility and ability to raise capital. While other considerations exist for reverse stock splits, such as enhancing the perception of the company's stock value, the immediate and pressing concern is often compliance with exchange regulations to maintain a listing.

4. What is a bond's coupon rate?

- A. The total return an investor can expect from a bond
- B. The interest rate that a bond issuer pays to bondholders**
- C. The price at which the bond is issued
- D. The risk premium associated with the bond

The coupon rate of a bond is defined as the interest rate that the bond issuer agrees to pay to bondholders, typically expressed as a percentage of the face value of the bond. This rate determines the periodic interest payments that an investor will receive until the bond reaches maturity. For example, if a bond has a face value of \$1,000 and a coupon rate of 5%, the bondholder would receive \$50 in interest payments each year. Understanding the coupon rate is essential for investors, as it directly impacts the income they can expect to earn from their investment in bonds. It also plays a significant role in determining the bond's market value, especially as market interest rates fluctuate. If market interest rates rise above the bond's coupon rate, the bond may trade at a discount; conversely, if market rates fall below the coupon rate, the bond may trade at a premium. The other options do not accurately describe the coupon rate: the total return an investor can expect from a bond encompasses various factors, including capital gains and reinvestment income; the price at which the bond is issued refers to the issue price rather than the coupon rate; and the risk premium is related to the additional yield required by investors to compensate for the risk of default.

5. Which characteristic distinguishes off-balance-sheet financing?

- A. It involves high-interest rates for short-term loans
- B. It appears on the balance sheet
- C. It does not appear on the balance sheet**
- D. It requires significant collateral

Off-balance-sheet financing is characterized by the fact that it does not appear on the balance sheet of a company. This type of financing allows a company to obtain funds or resources without directly impacting its liabilities or equity as recorded in the balance sheet. Companies often utilize off-balance-sheet financing to improve their financial ratios or to keep debt levels low, which can enhance their appeal to investors and creditors. This method can include arrangements like operating leases, joint ventures, or certain contractual agreements where the assets and liabilities are not recorded in the financial statements, thereby keeping the company's financial health looking stronger than it might actually be. Understanding this characteristic is crucial for assessing the true financial position of a company, as off-balance-sheet financing can significantly affect risk assessments and financial analysis.

6. Which provision is NOT typically included in a debt contract?

- A. Terms by which the company will provide funds for redemption
- B. Parent corporation comfort letters**
- C. Covenants
- D. Representations and warranties

The provision that is not typically included in a debt contract is the parent corporation comfort letters. Comfort letters are not standard contractual obligations found in debt agreements. They are primarily used to provide assurance or comfort regarding a company's financial status or to clarify certain matters related to the financial representations made in other documents, such as an underwriting agreement. While these letters can play a role in financing transactions, they do not constitute binding commitments or terms of repayment as seen in typical debt contracts. In contrast, the other provisions mentioned are essential components of debt contracts. Terms for redemption outline how and when a borrower may repay the principal before the maturity date, offering flexibility in managing debt. Covenants are conditions imposed by lenders that require the borrower to meet certain performance criteria, ensuring that the borrower's financial health remains satisfactory throughout the term of the loan. Representations and warranties serve as assertions made by the borrower that the information provided to the lender is accurate, providing the lender with a degree of security regarding the borrower's operational and financial integrity.

7. In treasury management, which is a key activity?

- A. Conducting audits for compliance**
- B. Managing financial obligations**
- C. Evaluating investment opportunities**
- D. Consolidating financial reporting**

Managing financial obligations is a fundamental activity in treasury management as it directly relates to ensuring that a company's cash flow is sufficient to meet its short-term liabilities. This involves monitoring and controlling cash inflows and outflows, which helps to maintain liquidity and optimize the use of financial resources. By effectively managing financial obligations, treasury professionals can prevent cash shortages, enable timely payments, and avoid costly penalties or interest expenses associated with late payments. In the context of treasury operations, this activity also encompasses cash forecasting, managing working capital, and aligning funding strategies with investment policies. Overall, successful management of financial obligations supports the organization's financial stability and strategic objectives.

8. When a central bank sells government securities, what is the likely outcome?

- A. Increase in money supply**
- B. Decrease in money supply**
- C. Stable economic conditions**
- D. Inflation of currency value**

When a central bank sells government securities, it is effectively taking money out of circulation, which leads to a decrease in the money supply. When securities are sold, financial institutions and investors pay cash for these securities. The funds used for the purchase are effectively transferred from the buyers' accounts to the central bank's account, reducing the amount of money available in the banking system for lending and spending. This action is part of a contractionary monetary policy. By decreasing the money supply, the central bank can help control inflation and stabilize the economy if it is overheating. A smaller money supply generally leads to higher interest rates and reduced consumer and business borrowing, further contributing to a slower rate of economic growth. In contrast, the other choices imply effects that do not align with the action of selling government securities. An increase in money supply, stable economic conditions, and inflation of currency value would not typically result from this action. Instead, selling government securities is a tool used by central banks to manage economic variables by tightening the money supply.

9. Which of the following is a characteristic of physical pooling?

- A. Funds can automatically transfer between different banks**
- B. All accounts are required to be in multiple currencies**
- C. Physical pooling usually requires the use of a single currency**
- D. Physical pooling involves only the bank's management**

Physical pooling is a treasury management strategy that allows organizations to optimize cash flow by consolidating funds from various bank accounts into a single account, which typically involves the use of a single currency. This characteristic simplifies the management of liquidity and reduces the costs associated with managing multiple bank accounts in different currencies. With a single currency, organizations can easily monitor their cash position and manage their working capital effectively, making it easier to fulfill obligations, optimize interest earning, and reduce transaction costs. The focus on a single currency also helps to mitigate foreign exchange risk, as organizations are less exposed to fluctuations in currency values when maintaining accounts in just one currency. This aspect of physical pooling enables better financial forecasting and strategic planning. While aspects such as automatic transfers between banks, multiple currency accounts, and bank management roles may be relevant in discussions around cash management strategies, they do not specifically define the characteristics of physical pooling as effectively as the requirement of using a single currency does.

10. What is the role of the advising bank in a letter of credit transaction?

- A. It issues the L/C on behalf of the buyer**
- B. It confirms the payment will be made**
- C. It advises the exporter of the L/C**
- D. It processes the payment from the buyer**

In a letter of credit transaction, the advising bank plays a critical role by informing the exporter about the issuance of the letter of credit. This is essential because the advising bank provides assurance to the exporter that the letter of credit has been issued and includes details relevant to the transaction, such as terms, conditions, and the payment process. By advising the exporter, the advising bank acts as an intermediary that facilitates communication between the buyer's issuing bank and the exporter, ensuring that the exporter is aware of the terms of the credit they will be working under. The advising bank's role is crucial in establishing trust in international trade, as it verifies the authenticity of the credit and provides guidance to the exporter on how to present the necessary documents to receive payment. Additionally, the advising bank may help the exporter understand the specific requirements set forth in the letter of credit, which is vital for smooth transaction execution.

Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

<https://afp.examzify.com>

We wish you the very best on your exam journey. You've got this!

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