

Investment Funds in Canada (IFIC) Practice Exam (Sample)

Study Guide



Everything you need from our exam experts!

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Questions

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- 1. What is the main function of pension funds within the investment landscape?**
 - A. To trade on the primary market**
 - B. To invest for future retirement benefits**
 - C. To provide venture capital**
 - D. To engage in direct investments only**
- 2. What is a common feature of a defined benefit pension plan?**
 - A. Contributions vary year by year**
 - B. Benefits depend on market performance**
 - C. Benefits are guaranteed based on service and earnings**
 - D. Only employee contributions are considered**
- 3. What characterizes demand-pull inflation?**
 - A. Supply exceeds demand**
 - B. Increased production costs**
 - C. High consumer spending leading to price increases**
 - D. Stagnant economic activity**
- 4. What happens if RESP beneficiaries do not attend qualified post-secondary institutions?**
 - A. The funds are lost.**
 - B. The funds can be transferred to a sibling's RESP.**
 - C. The funds must be paid back.**
 - D. The funds can be rolled over into an RRSP.**
- 5. What concept is associated with the potential for risk and reward in trading strategies?**
 - A. Liquidity**
 - B. Drawdown**
 - C. Leverage**
 - D. Risk-return profile**

- 6. Which formula is used to calculate dividend yield?**
- A. Annual Dividend / Stock Price**
 - B. Stock Price / Annual Dividend**
 - C. Annual Earnings / Dividend Amount**
 - D. Dividend Amount / Total Shares Issued**
- 7. What must clients typically have in common to open a joint account?**
- A. Risk tolerance**
 - B. Investment horizon**
 - C. Investment objectives**
 - D. All of the above**
- 8. What is a characteristic feature of a perpetual preferred share relevant to dividends?**
- A. It offers variable dividend options**
 - B. It comes with a fixed maturity date**
 - C. It has no maturity date and pays dividends indefinitely**
 - D. It is redeemable by the holder**
- 9. What is the primary purpose of the statement of comprehensive income?**
- A. To report the company's total liabilities**
 - B. To provide a detailed account of equity changes**
 - C. To summarize revenue and expenses over time**
 - D. To reflect changes in asset valuation**
- 10. What type of fund consists of multiple mutual funds organized around a specific asset allocation model?**
- A. Target-date funds**
 - B. Fund wrap**
 - C. Fund of funds**
 - D. Portfolio allocation service**

Answers

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

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Explanations

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1. What is the main function of pension funds within the investment landscape?

- A. To trade on the primary market**
- B. To invest for future retirement benefits**
- C. To provide venture capital**
- D. To engage in direct investments only**

The primary function of pension funds is to invest for future retirement benefits. These funds collect and manage contributions from employees and employers during an individual's working life. The goal is to grow these contributions through various investment strategies to ensure that the fund can provide sufficient income to retirees once they reach retirement age. Pension funds typically invest in a diversified portfolio that may include stocks, bonds, real estate, and other assets, aiming to balance risk and growth to meet future payout obligations. This long-term investment strategy is crucial for ensuring the financial security of individuals in retirement, which is the core purpose of a pension fund. The other options do not align with the fundamental role of pension funds in the investment landscape. Trading on the primary market and providing venture capital are activities more closely related to investment firms or venture capital funds, while engaging in direct investments suggests a narrower investment strategy that doesn't encompass the primary objective of pension funds.

2. What is a common feature of a defined benefit pension plan?

- A. Contributions vary year by year**
- B. Benefits depend on market performance**
- C. Benefits are guaranteed based on service and earnings**
- D. Only employee contributions are considered**

A defined benefit pension plan is characterized by providing specified benefits to retirees based on predetermined factors, primarily the employee's earnings and years of service. This feature guarantees that employees will receive a certain amount of income during retirement, which is calculated using a formula that typically accounts for their salary and the duration of their employment with the company. This guarantee is a core aspect of defined benefit plans, as it offers a predictable income stream for retirees. The other options do not align with the fundamental nature of defined benefit pension plans. For example, contributions do not typically vary year by year in a defined benefit plan; instead, the employer usually makes consistent contributions based on actuarial assessments to fulfill the promised benefits. Additionally, benefits are not contingent upon market performance, as defined benefit plans operate on a set formula rather than fluctuating investment returns. Finally, defined benefit plans generally consider both employee and employer contributions as part of the funding, rather than only focusing on employee contributions. This highlights the collaborative nature of funding such pension plans, ensuring that both parties play a role in securing the promised benefits for the employee.

3. What characterizes demand-pull inflation?

- A. Supply exceeds demand
- B. Increased production costs
- C. High consumer spending leading to price increases**
- D. Stagnant economic activity

Demand-pull inflation is characterized by high consumer spending leading to price increases. This phenomenon occurs when the overall demand for goods and services in an economy outpaces the available supply. When consumers have a higher appetite for products—often due to factors such as increased wages, consumer confidence, or government spending—businesses may struggle to keep up with this demand. As a result, they raise prices, which contributes to inflation. The core of demand-pull inflation lies in its relationship with demand: when consumers are eager to buy more than what is available, the pressure on prices increases. This inflationary pressure can manifest in various ways, including rising prices for goods and services across the board, not just a few areas of the economy. In contrast, elements like supply exceeding demand, increased production costs, or stagnant economic activity describe different scenarios that do not align with the mechanism of demand-pull inflation. For instance, if supply exceeds demand, it typically leads to deflationary pressure instead of inflation. Increased production costs might cause cost-push inflation where the focus is on rising prices due to higher costs of inputs. Stagnant economic activity reflects a lack of growth or demand rather than excessive demand, which is contrary to the essence of demand-pull inflation.

4. What happens if RESP beneficiaries do not attend qualified post-secondary institutions?

- A. The funds are lost.
- B. The funds can be transferred to a sibling's RESP.
- C. The funds must be paid back.**
- D. The funds can be rolled over into an RRSP.

When a Registered Education Savings Plan (RESP) beneficiary does not attend a qualified post-secondary institution, the consequences for the funds in the account can be significant. The correct understanding is that the accumulated grants and any income generated in the RESP may need to be returned to the government if the beneficiaries do not utilize the funds for their intended educational purpose. Specifically, if the beneficiary does not enroll in a qualifying educational program, the government grants that were added to the RESP will usually be returned, often requiring the subscriber or account holder to pay back those amounts. This is because the purpose of the RESP is to encourage savings for post-secondary education, and the government grants are contingent upon the beneficiary's attendance at an eligible institution. In contrast, it is also possible to avoid losing all benefits from the RESP. The funds contributed by the account holder (the subscriber) can remain in the plan, and there are options for the funds, such as transferring them to another sibling's RESP or potentially rolling over contributions into a Registered Retirement Savings Plan (RRSP) under specific circumstances, but these options depend on the specific situation and regulations in place. In summary, while the contributions can potentially be preserved or redirected under certain conditions, the obligation to return government contributions arises if the

5. What concept is associated with the potential for risk and reward in trading strategies?

- A. Liquidity**
- B. Drawdown**
- C. Leverage**
- D. Risk-return profile**

The concept that illustrates the potential for risk and reward in trading strategies is the risk-return profile. This term describes the relationship between the amount of risk taken on an investment and the potential return that can be expected. In investing, typically, higher returns are associated with taking on greater risks, while lower risks generally correlate with lower returns. Understanding the risk-return profile is crucial for investors as it enables them to assess how much risk they are willing to tolerate in pursuit of potential rewards. Different investments may offer different risk-return profiles, and knowing these profiles helps investors make informed decisions that align with their financial goals, investment horizon, and risk tolerance. Liquidity refers to how easily an asset can be converted into cash, which can impact the ability to realize gains but does not directly express the relationship between risk and reward. Drawdown refers to the reduction of one's capital after a series of losing trades but does not capture the broader spectrum of potential returns related to risk. Leverage involves using borrowed funds to increase investment potential, which can amplify both returns and risks, but does not capture the entire context of risk-reward dynamics in the same way that the risk-return profile does.

6. Which formula is used to calculate dividend yield?

- A. Annual Dividend / Stock Price**
- B. Stock Price / Annual Dividend**
- C. Annual Earnings / Dividend Amount**
- D. Dividend Amount / Total Shares Issued**

The formula used to calculate dividend yield is the annual dividend divided by the stock price. This calculation provides an indication of the return on investment for a stock in terms of dividends received relative to the price of the stock. To elaborate, dividend yield expresses the amount of cash flow an investor can expect to generate for each dollar invested in a company's stock, which is particularly useful for evaluating the income potential of stocks, especially for income-focused investors. By calculating this yield, investors can compare the income-generating capabilities of various investments, helping them make informed decisions. The annual dividend represents the cash payments made to shareholders, while the stock price reflects the current market value of the shares, yielding a percentage that represents the income return. This makes it a fundamental metric in assessing investments, particularly in income-generating assets.

7. What must clients typically have in common to open a joint account?

- A. Risk tolerance**
- B. Investment horizon**
- C. Investment objectives**
- D. All of the above**

To open a joint account, it is essential that clients typically share common characteristics in terms of risk tolerance, investment horizon, and investment objectives. This alignment is crucial for several reasons. When individuals partake in a joint account, they are essentially combining their financial resources to achieve shared financial goals. If clients have similar risk tolerances, it helps ensure that both parties are comfortable with the level of risk associated with the investments made within the account. For example, if one client is very risk-averse while the other is open to high-risk investments, conflicts may arise in decision-making, causing stress in their financial partnership. Moreover, having a similar investment horizon is important as it dictates how long the individuals plan to hold their investments before needing to access the funds. If one party aims for short-term gains while the other is focused on long-term growth, they may not agree on suitable investment strategies. Lastly, shared investment objectives—whether it's saving for retirement, a major purchase, or another goal—are also critical. Discrepancies in these objectives can lead to disagreements regarding the strategies employed and the types of investments selected within the joint account. In essence, having clients align on risk tolerance, investment horizon, and investment objectives fosters collaboration, minimizes potential conflicts

8. What is a characteristic feature of a perpetual preferred share relevant to dividends?

- A. It offers variable dividend options**
- B. It comes with a fixed maturity date**
- C. It has no maturity date and pays dividends indefinitely**
- D. It is redeemable by the holder**

Perpetual preferred shares are unique financial instruments that are designed to provide dividends without a specified maturity date, which means they can continue to pay dividends indefinitely. This characteristic is particularly appealing to investors looking for a steady income stream, as these shares do not have an expiration, allowing holders to receive dividend payments for as long as the company remains in operation and continues to declare them. The dividends on perpetual preferred shares are typically fixed and are paid out based on the terms set when the shares were issued. This structure contrasts with common shares, which might offer variable dividends depending on the company's performance and board decisions. Therefore, the absence of a maturity date is a defining feature of perpetual preferred shares, making them distinct in a portfolio of investments. The option about coming with a fixed maturity date is inaccurate because perpetual shares, by definition, do not have a maturity. Similarly, being redeemable by the holder does not align with the nature of perpetual preferred shares, as they are not typically structured to allow for redemption at the option of the shareholder. Lastly, variable dividend options are not characteristic of perpetual preferred shares since they usually entail fixed dividend payouts. All of these distinctions reinforce the correctness of the option identifying that perpetual preferred shares have no maturity date and pay dividends indefinitely.

9. What is the primary purpose of the statement of comprehensive income?

- A. To report the company's total liabilities**
- B. To provide a detailed account of equity changes**
- C. To summarize revenue and expenses over time**
- D. To reflect changes in asset valuation**

The primary purpose of the statement of comprehensive income is to summarize revenue and expenses over a specific period, ultimately revealing how these factors contribute to the overall profit or loss of an organization. This statement allows stakeholders to understand the financial performance of the company over time by providing key metrics such as net income, and it can include other comprehensive income items that might not be reflected in net income. This can help inform investment decisions and provide insights into operational effectiveness. While the other options focus on different aspects of the financial statements, they do not align with the specific function of the statement of comprehensive income. Reporting total liabilities is part of the balance sheet, detailing what the company owes. A detailed account of equity changes is typically included in the statement of changes in equity, which tracks movements in ownership interest. Reflecting changes in asset valuation is associated with the balance sheet and specific reporting standards, focusing more on the assessment of the company's overall worth rather than its operating performance over time.

10. What type of fund consists of multiple mutual funds organized around a specific asset allocation model?

- A. Target-date funds**
- B. Fund wrap**
- C. Fund of funds**
- D. Portfolio allocation service**

The correct choice is referred to as a fund of funds. A fund of funds is designed specifically to hold a variety of underlying mutual funds rather than investing directly in stocks, bonds, or other securities. This structure provides investors with diversification across multiple mutual funds that might have different investment strategies or asset classes. By utilizing a specific asset allocation model, a fund of funds can enhance its risk-adjusted returns by selecting a mix of funds that aligns with its investment objectives. Investors benefit from the expertise of professional fund managers overseeing the selection and ongoing management of these underlying funds. Target-date funds, while similar in that they may invest in a variety of other funds, specifically aim at a particular retirement date, automatically adjusting their asset allocation over time as that date approaches. Fund wraps typically provide a comprehensive service that may include a variety of investment options and advice, but they are not strictly defined by holding multiple mutual funds exclusively. Portfolio allocation services often refer to consultative services that help clients choose a mix of investments but do not necessarily imply the fund structure that a fund of funds represents.