



## DIPLOMA IN PROFESSIONAL FINANCIAL ADVICE

### UNIT 3: INVESTMENT PRINCIPLES AND RISK

#### Learning Outcomes:

1. Demonstrate an ability to analyse the characteristics, inherent risks, behaviour and correlation of asset classes
2. Demonstrate an understanding of the macro-economic environment and its impact on asset classes
3. Demonstrate an understanding of the merits and limitations of the main investment theories
4. Demonstrate the ability to apply the principles of the time value of money
5. Demonstrate an ability to analyse and explain the nature and impact of the main types of risk on investment performance
6. Demonstrate an ability to analyse the characteristics, inherent risks, behaviours and relevant tax considerations of investment products
7. Demonstrate the ability to apply the investment advice process
8. Demonstrate an understanding of the principles of investment planning
9. Demonstrate an ability to analyse the performance of investments

**Syllabus Points:**

**1. Demonstrate an ability to analyse the characteristics, inherent risks, behaviour and correlation of asset classes**

- 1.1 Cash and cash equivalents: Main types, costs and charges
- 1.2 Fixed interest securities: Main types, Running and redemption yields, interest rates and yield curves, Markets and indices, Transaction costs – purchase and sale
- 1.3 Equities: Main types, private equity, Valuation measures – Price/Earnings (P/E) ratio, dividend yield and cover, Net Asset Value (NAV), Stock markets – indices, listings, Transaction costs
- 1.4 Property: Main types, residential and commercial, income profile and gearing, Valuation, Performance benchmarking, Transaction and on-going costs
- 1.5 Alternative investments such as commodities, and physical assets.
- 1.6 Pricing, liquidity and fair value
- 1.7 Correlation of asset classes – relevance to asset allocation

**2. Demonstrate an understanding of the macro-economic environment and its impact on asset classes**

- 2.1 Main long term UK and global socio-economic trends
- 2.2 Overview of world economies and globalisation of markets
- 2.3 Economic and financial cycles – predictability, regional economy differences
- 2.4 The key economic indicators – trends and their interpretation
- 2.5 Significance of monetary and fiscal policy
- 2.6 Relevance of money, inflation, deflation, interest rates and exchange rates
- 2.7 Balance of payments and international capital flows
- 2.8 The role of financial investment in the economy

**3. Demonstrate an understanding of the merits and limitations of the main investment theories**

- 3.1 Key features of the main investment theories: □ Modern portfolio theory, Multi factor model, Efficient market hypothesis, Capital asset pricing model (CAPM)
- 3.2 Portfolio theory, diversification and hedging, Correlation between asset classes, Total return and an awareness of beta and alpha, Risk adjusted returns
- 3.3 Basics of behavioural finance – market and individual behaviours

**4. Demonstrate the ability to apply the principles of the time value of money**

- 4.1 Compound interest and discounting
- 4.2 Real returns and nominal returns

**5. Demonstrate an ability to analyse and explain the nature and impact of the main types of risk on investment performance**

- 5.1 Liquidity and access
- 5.2 Income and capital growth, including shortfall
- 5.3 Short term volatility
- 5.4 Long term performance
- 5.5 Gearing
- 5.6 Currency
- 5.7 Time, inflation and interest rates
- 5.8 Institutional, systematic and non-systemic, including fraud and counterparty, market timing

**6. Demonstrate an ability to analyse the characteristics, inherent risks, behaviours and relevant tax considerations of investment products**

- 6.1 The advantages and disadvantages of direct investment in securities and assets compared to indirect investment through collectives and other products
- 6.2 Investment structures: Collective investment funds – onshore and offshore, Exchange Traded Funds (ETFs) and Exchange Traded Commodities (ETCs), Closed ended funds/investment companies – onshore and offshore, Individual Savings Accounts (ISAs) and Child Trust Funds (CTFs), National Savings and Investments, Life assurance based investments – onshore and offshore, Defined contribution (DC) pension arrangements, Real Estate Investment Trusts (REITs) and other property based products, Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs) – basic structures and uses, Broker funds and distributor influenced funds (DIFs)
- 6.3 Derivatives: Basic structure, main types and uses
- 6.4 Investment strategy based products - Hedge funds and funds of hedge funds, Absolute return funds, Structured products – income and capital growth, structure and analysis, With profit funds – main principles

## **7. Demonstrate the ability to apply the investment advice process**

- 7.1 Explain the investment process
- 7.2 Establish client relationships, capability and circumstances including assets and debts
- 7.3 Agree and prioritise needs and wants
- 7.4 Agree investment objectives, growth, income, time horizons, debt and credit management and repayment
- 7.5 Determine and agree risk profile – objective and subjective factors
- 7.6 Assess affordability and other suitability considerations, ethical, social responsibility and religious preferences
- 7.7 Agree strategy and rationale to achieve the objectives
- 7.8 Agree benchmark/performance measures and review process
- 7.9 Asset allocation: Alignment with client risk profile and requirements, Diversification and correlation benefits, Accumulation and decumulation

## **8. Demonstrate an understanding of the principles of investment planning**

- 8.1 Asset allocation, Stochastic modelling, Strategic and tactical asset allocation
- 8.2 Portfolio construction: Stock and fund selection, Diversification by sector, geographical area and currency, Main fund management strategies and styles, Costs, charges, Total Expense Ratios (TERs), Portfolio Turnover Ratios (PTRs), Selection of products, tax wrapper and services, Provider selection and due diligence, Recommendations and suitability
- 8.3 Wrap and other platforms: Concept and uses, Benefits and risks, Costs/charges

## **9. Demonstrate an ability to analyse the performance of investments**

- 9.1 Portfolio performance: Methods of evaluating portfolio performance, Selection and use of benchmarks, New money and timing factors
- 9.2 Portfolio review and administration: Changes in client circumstances, Changes in financial environment, New products and services available, Maintenance of products and services, Use of external services/benchmarking, Rebalancing