

**CAIA Level 2 “Issues and Errata”
For 4th edition of core book & Workbook
Updated February 23, 2021**

Note: In deciding whether an “issue” rises to the need to be posted as errata, the emphasis is on assisting the candidate to prepare for the exam. Errata should be posted when the benefit to the candidate’s preparation for the exam (especially in the context of responding to a specific learning objective) exceeds the cost to the candidate of allocating time to digesting the correction.

Workbook Page 80, Solution #9

9. To find the value of the option, we follow a similar process to Exercise 8, only this time by examining the value of the option at each node. Since this is a call option, the value can be equal to $\max(S - X, 0)$. The strike price is \$53.

In exercise 7, we calculated the values of S_u and S_d , so we can use these values to determine the values of the options at those respective nodes.

Option Value at S_u node: $\max(\$55 - \$53, 0) = \$2$

Option Value at S_d node: $\max(\$45.50 - \$53, 0) = \$0$

Next, we calculate the call option value using the same approach as exercise 8.

$$c = [(0.6316 * \$2) + (0.3684 * \$0)] = \$1.26$$

Add this next step:

Now that we have found the weighted value of the node, we must discount it to the present. Therefore $1.26 / 1.03 = 1.22$

Workbook Page 137, Solution #1

1. Since the delta of the option is 0.522, the position will be delta hedged by shorting $\Delta = 0.522 \times \$100 = \52.2 worth of the underlying index.

Should be:

1. Since the delta of the option is 0.522, and each option contract is for 100 shares, the position will be delta hedged by shorting $\Delta = 0.522 \times 1 \text{ option} \times 100 \text{ share} = 52.2$ shares of the underlying index.

Workbook Page 138, #8

A short position in an iron condor is created when a trader sells an out-of-the-money bull spread and an out-of-the-money bear spread. A bull spread CAIA Level II Workbook, March 2021 139 is created shorting a call and going long another call having a strike price that is lower than that of the long call. A bear spread is created shorting a call and going long another call having a strike price that is greater than **that of the long call**. Bull

and bear spreads can also be created using put options. Bull spreads and bear spreads were detailed in CAIA Level I.

Should be:

A short position in an iron condor is created when a trader sells an out-of-the-money bull spread and an out-of-the-money bear spread. A bull spread is created by going long a call option with a lower strike price and shorting a call with a higher strike price. A bear spread is created by going long a call option with a higher strike price and shorting a call option with a lower strike price. Bull and bear spreads can also be created using put options. Bull spreads and bear spreads were detailed in CAIA Level I.

Core Book:

Page 113 Section 7.3.5

In Equation 7.11 remove “X” in “ln X”

In Equation 7.12 change “d” to “ $d - \sigma_A \sqrt{\tau}$ ”

Page 144 Section 8.7.2

In the fourth and fifth line of the section Change “\$60” to “\$50” in two locations:

...flow and \$14 for the \$60 potential cash flow:

$$\text{Bond Price} = (\$100 \times 60\% \times 0.833) + (\$60 \times 40\% \times 0.70)$$

to

...flow and \$14 for the \$50 potential cash flow:

$$\text{Bond Price} = (\$100 \times 60\% \times 0.833) + (\$50 \times 40\% \times 0.70)$$

Page 152 Application 9.1.5

The squared terms should be removed from the solved answer.

$$\text{Investment A: } E[U(W)] = 0.10 - \left(\frac{0.8}{2}\right) \times (.04) = 0.084$$

$$\text{Investment B: } E[U(W)] = 0.13 - \left(\frac{0.8}{2}\right) \times (.09) = 0.094$$

Page 158 Application 9.2.3

In the fourth line of text inside Application 9.2.3”

Replace “L = 0.02”

with “L=0.8 and $\delta=0.02$ ”

Page 169 Section 9.8.2

In the first sentence of the third paragraph change “five asset classes” to “eight asset classes”

Page 198 Section 11.2 (Item 4)

In the last paragraph (#4) change “Individually managed accounts” in two places to “Individually managed retirement accounts”

Page 251, Section 13.3

In the 9th line of Section 13.3 change “15%” to “1.5%”

Page 263 Equation 13.3

Change 1 in numerator of first fraction to “-1” (as correctly shown in Application 13.6.3)

Page 373 Exhibit 18.4

In Row “Mean” change 20% to 2.5%

Page 490 Section 23.5.2

At end of last line immediately above Exhibit 23.5.2 change “-3.8%” to “-3.7%”

Page 543 Section 26.1

The bolded term in the bottom paragraph should be changed from:

algorithmic factor replication approach

to:

algorithmic replication approach

Page 650, Section 28.6.3

The left side of Equation 30.6 should be FV(C) rather than FV(D)

Page 795 Section 36.5.2

The third sentence in the second paragraph:

“Exhibit 36.5 indicates ITM options as having lower implied volatility than ATM options, which in turn have lower implied volatility than OTM options.”

Should have the word “lower” changed to “higher” in two locations:

“Exhibit 36.5 indicates ITM options as having higher implied volatility than ATM options, which in turn have lower higher volatility than OTM options.”