Issues and Errata for Level II Curriculum Printed Volumes

March 21, 2022

Note: All issues and errata are corrected as they are discovered in the digital version of the curriculum

- **In LII, vol. 1, page 259**, section 8.2 **should read** section 3.3
- **In LII, vol. 1, page 354**, section 10.4.1 and 10.4.2 **should read** section 3.5
- **In LII, vol. 2, page 199**, section 20.4-20.8 **should read** section 5.5

LII, Vol. 1, page 307, Application B:

"Given that L ¼ **0.08** and δ ¼ 0.02, find the optimal portfolio allocation, *w*, of the risky asset."

Should be

"Given that L ¼ **0.8** and δ ¼ 0.02, find the optimal portfolio allocation, *w*, of the risky asset."

LII, Vol. 3, page 392

section 40.1 **should read** section 9.5

LII, Vol. 2, page 300

Revise Learning Objective-

Define sentiment and sentiment sensitivity
to
Define sentiment and list the six sentiment indicators

LII, Vol. 2, page 301

Revise subsection title

Sentiment Sensitivity
to
Indicators of Market Sentiment

Continue to next page

LII, Vol. 2, pages 90 & 91 (last paragraph on page 90)

> For example, if an investor wants to invest with a CTA that requires a minimum investment of $600,000, the investor could either fully fund the account with $600,000 or, if notional funding was offered, partially fund the account (e.g., a funding level of $400,000) but still have it traded as if it were funded with $600,000. The account would therefore have a notional funding level of $200,000. In this case, the trading level—which is also the amount on which investor fees and returns are calculated—would be $600,000 with the account funded 67%. If the CTA returned 10% that year (on the trading level), the investor would have made $60,000 (a 10% gain on the trading level), but it would be a 16.7% gain on the funding level. Of course, if the CTA were to lose 10%, the loss would be magnified to 16.7%.

16.7% **should be changed to** 15% twice, once for the gain and once for the loss.

LII, Vol 2, page 189 5.4 Review Questions

Questions 1, 2, 3 are missing their actual questions. **Please add:**

1. What is the call option's delta?

2. In order to properly delta hedge the option's position, should the analyst take a long or short position in the underlying shares of the company stock?

3. How my shares should the analyst buy (long) or sell (short)?

LII, Vol. 2, page 385 6.4 Review Questions

Questions 1, 2, 3 are missing their actual questions. **Please add:**

1. What positions (long or short) should she take in July and December light sweet crude oil futures?

2. Suppose that the spreader takes a position of long 5 July contracts and short 5 December contracts, and that in June an oversupply of crude in the world markets causes the price of the July contract to decline to $45.33, while the December contract declines to $49.03. Calculate the total gain (loss) of the spread.

3. Suppose that the spreader takes 5 long July positions and 5 short December positions, and that in May political turmoil in oil-producing countries causes the price of the July contract to increase to $63.08 and the December contract to increase to $69.63. Calculate the total gain (loss) of the spread.

LII, Vol. 2, Page 585 for printed version

The 6th definition down

Please disregard or delete the highlighted area below:

Co-Investments: Side letters may create co-investing relationships and specify the terms of those relationships. as discussed in the next lesson, Co-Investments.

Also, please disregard or delete Review Questions 5, 6, 7, and 8.

LII, Vol. 1, Page 203

"A Two-Period Black–Derman–Toy (BDT) Binomial Tree" in the box at the top of the page

Should look like this:

ru = 6.50%

r0 = 5.00% <

rd = 4.7%

LII, Vol 2, Page 511

Disregard the 3rd Learning Objective listed on this page.

LII, Vol. 2, Page 518

Disregard Review Question #7

LII, Vol. 2. Page 522

Disregard Review Q & A #7

LII, V2, Page 479 Q & A #8

Profit-and-Loss Statement for the Example Merger Arbitrage Trade

Description		**Amount**
Gain on Target's long position	1,000 X [($27.50 X 2.3) – 45.16)]	$ 18,090.00
Loss on Acquirer's short position	–1,000 X 2 X ($27.50 – 24.00)	$ (7,000.00)
Short Rebate at 0.50% rate	1,000 X 2 X 24.00 X 0.50% X 149/365	$ 134.94
Total profit (loss) from strategy		$ 11,224.94
Initial Investment	1,000 X 45.16	$ 45,160.00
Return on investment over 149 days	11,224.94 / 45,160.00	40.06%
Annualized Return	(1 þ 40.06%) ^ (365/149) – 1	128.25%

Should Be:

Profit-and-Loss Statement for the Example Merger Arbitrage Trade

Description		Amount
Gain on Target's long position	1,000 X [($27.50 X 2.3) – 45.16)]	$ 18,090.00
Loss on Acquirer's short position	–1,000 X 2 X ($27.50 – 24.00)	$ (7,000.00)
Short Rebate at 0.50% rate	1,000 X 2 X 24.00 X 0.50% X 149/365	$ 97.97
Total profit (loss) from strategy		$ 11,187.97
Initial Investment	1,000 X 45.16	$ 45,160.00
Return on investment over 149 days	11,224.94 / 45,160.00	40.06%
Annualized Return	(1 + 24.77%) ^ (365/149) – 1	128.25%

LII, V1, page 215

Disregard the first Learning Objective on the list

- Recognize the general characteristics of credit instruments typically traded by hedge funds

---

LII, V2, Page 385 Review Questions #1 & #2

#1 Should read:

Assume the following scenario. In April, a spreader observes contango in the crude oil forward curve. July and December light sweet crude oil futures on the NYMEX are trading at $55.45 and $62.27, respectively. The size of the NYMEX light sweet crude oil contract is 1,000 barrels. The spreader anticipates a flattening of the curve and narrowing of the spread between the two maturities.

What positions (long or short) should she take in July and December light sweet crude oil futures?

#2 Should read:

Assume the following scenario. In April, a spreader observes contango in the crude oil forward curve. July and December light sweet crude oil futures on the NYMEX are trading at $55.45 and $62.27, respectively. The size of the NYMEX light sweet crude oil contract is 1,000 barrels. The spreader anticipates a flattening of the curve and narrowing of the spread between the two maturities.

Suppose that the spreader takes a position of long 5 July contracts and short

5 December contracts, and that in June an oversupply of crude in the world markets causes the price of the July contract to decline to $45.33, while the December contract declines to $49.03. Calculate the total gain (loss) of the spread.

LII, V2, Page 387 Review Questions and Answers #1 & #2

#1 Should read:

QUESTION

Assume the following scenario. In April, a spreader observes contango in the crude oil forward curve. July and December light sweet crude oil futures on the NYMEX are trading at $55.45 and $62.27, respectively. The size of the NYMEX light sweet crude oil contract is 1,000 barrels. The spreader anticipates a flattening of the curve and narrowing of the spread between the two maturities.

What positions (long or short) should she take in July and December light sweet crude oil futures?

ANSWER

The spreader should go long July and short December light sweet crude oil futures.

#2 Should read:

QUESTION

Assume the following scenario. In April, a spreader observes contango in the crude oil forward curve. July and December light sweet crude oil futures on the NYMEX are trading at $55.45 and $62.27, respectively. The size of the NYMEX light sweet crude oil contract is 1,000 barrels. The spreader anticipates a flattening of the curve and narrowing of the spread between the two maturities.

Suppose that the spreader takes a position of long 5 July contracts and short 5 December contracts, and that in June an oversupply of crude in the world markets causes the price of the July contract to decline to $45.33, while the December contract declines to $49.03. Calculate the total gain (loss) of the spread.

ANSWER

The loss on the long July contract is: −$55.45 + $45.33 = −$10.12
The gain on the short December contract is: $62.27 − $49.03 = $13.24
Total gain on the spread = −$10.12 + $13.24 = $3.12
The total gain of the spread is:
Position P&L = P&L barrel × Contract size × Position size
= $3.12 × 1,000 × 5 = $15,600

Continue to next page

LII, V 2, page 98 Equations 3 & 4
Parametric VaR Using a Variance based on Unequal Return Weighting

$$\mu_{T-1} = (1-\lambda)\,\mu_{T-2} + \lambda\left(\mu_{T-2} - R_{T-1}\right)$$

$$\sigma_T^2 = (1-\lambda)\times\sigma_{T-1}^2 + \lambda\times\left(\mu_{T-1} - R_T\right)^2$$

Should read:

$$\mu_{T-1} = (1-\lambda)\,\mu_{T-2} + \lambda R_{T-1}$$

$$\sigma_T^2 = (1-\lambda)\times\sigma_{T-1}^2 + \lambda\times\left(R_T - \mu_{T-1}\right)^2$$

LII, Vol 3, page 246 (within the paragraph under the chart)

The exhibit indicates ITM options as having higher implied volatility than ATM options, which in turn have higher implied volatility than OTM options. In equity index options, the graph for a single expiration date seems to look like a smile or a smirk. A volatility structure with a **smile or a smirk** is where out-of-the-money put options have higher levels of implied volatility than other options.

Should read:

The exhibit indicates a general observation that implied volatility for many options is lowest for strikes closer to at-the-money, with strikes further in-the-money or out-of-the-money having higher levels of implied volatility. In equity index options, the graph for a single expiration date seems to look like a smile or a smirk. When implied volatility exhibits a **smile or a smirk**, options with strike prices further in-the-money or out-of-the-money have higher levels of implied volatility than options closer to at-the-money.
