# Equities

**Chartered Financial Analyst (CFA®) Program Level I exam**

11–14% of the exam · 12 learning modules · 2027 curriculum

Equities covers what shares are and how they trade, how shareholders earn returns, and how analysts value a company with present value models, multiples and forecast models built on industry and company analysis. Level I questions mix definitions and structure with short valuation calculations: dividend discount models, preferred shares, multiples, enterprise value, float, total return and the CAPM.

**You should be able to:** You should be able to describe share types, markets and returns, value a share with dividend, preferred and multiples models, and estimate a required return with the CAPM.

## Every learning module: the key point and the trap

### EQ.1 Shares: types and core features

Common shares carry the residual claim: they are paid last in liquidation but keep all value above other claims, and usually carry the votes.

**Trap:** Cumulative, participating and convertible are different features: only cumulative creates dividend arrears.

### EQ.2 Share classes, votes and proxy advice

Jurisdictions differ in shareholder rights: how directors are elected, which decisions need a shareholder vote, and how easily minorities can challenge the board.

**Trap:** Extra votes do not mean extra dividends or priority in liquidation; the classes usually share the same economic claim.

### EQ.3 Equity markets, trading venues and indexes

The primary market is where issuers sell new shares (an IPO, a seasoned offering, a private placement); the secondary market is where investors trade existing shares.

**Trap:** Float excludes every closely held block, not only insiders' shares: strategic and government stakes count too.

### EQ.4 Dividends, buybacks, splits and share returns

Returns come from price change and distributions: total return = (P1 − P0 + D) / P0; price return leaves out the dividend.

**Trap:** The ex-dividend date, not the record date, decides who gets the dividend when buying in the market.

### EQ.5 Price, value and families of valuation models

Price is what the market charges; intrinsic value is the analyst's estimate of what the share is worth. Value above price suggests undervaluation, below price overvaluation.

**Trap:** Cash is subtracted, not added, when moving from market capitalization to enterprise value.

### EQ.6 Present value models for shares

Dividend discount model: value = present value of expected dividends at the required return on equity. FCFE is discounted at the cost of equity and gives equity value directly; FCFF is discounted at the WACC and gives firm value, from which debt is subtracted.

**Trap:** The terminal value at year n uses the dividend of year n + 1 and is discounted n years, not n + 1.

### EQ.7 Valuing shares with price and EV multiples

Method of comparables: apply a benchmark multiple (often a peer median) to the company's own fundamental, assuming peers are fairly priced.

**Trap:** Dividing EBITDA into market capitalization instead of enterprise value mixes equity and firm measures.

### EQ.8 Building forecast models to value equity

A forecast model projects the income statement, balance sheet and cash flow statement together, starting from revenue.

**Trap:** Forecasting costs or capital spending without linking them to revenue gives a model whose cash flow ignores its own growth.

### EQ.9 Analysing industries and competitive forces

Industry analysis: define the industry, measure its size, growth and profitability, assess its structure and external influences, then position the company.

**Trap:** A tax or regulation change is political or legal, a change in tastes is social: classify the factor by its source.

### EQ.10 Company strategy, drivers and capital needs

Competitive strategy: cost leadership, differentiation or a focus on a niche; position shows in margins and returns relative to peers.

**Trap:** A margin rise from spreading fixed costs over more volume is operating leverage, not pricing power.

### EQ.11 Writing and reading equity research

A full company report covers the investment thesis, the business and industry, financial analysis and forecasts, valuation, risks, and a recommendation or target price.

**Trap:** Wide distribution and public ratings belong to sell-side research, not buy-side.

### EQ.12 CAPM and factor models for required return

CAPM: required return = rf + beta x (E(Rm) − rf), where E(Rm) − rf is the market (equity) risk premium.

**Trap:** Multiply beta by the risk premium, not by the market return, unless the risk-free rate is subtracted first.

## Key terms

**Float:** Shares available to trade: shares outstanding less closely held and restricted shares.

**Ex-dividend date:** The first day a share trades without the right to the declared dividend.

**Enterprise value:** Market capitalization plus debt, preferred and minority interest, less cash.

**Intrinsic value:** An analyst's estimate of a share's worth from its expected cash flows and risk.

**Gordon growth model:** Value equals next year's dividend divided by the required return less a constant growth rate.

**Justified multiple:** A multiple derived from fundamentals such as payout, required return and growth.

**Five forces:** Entry, suppliers, buyers, substitutes and rivalry, which together shape industry profitability.

**Cash conversion cycle:** Days of inventory plus days of receivables less days of payables.

**Beta:** A share's sensitivity to market returns, the slope of the market model.

**Arbitrage pricing theory:** A no-arbitrage model pricing several systematic risk factors.

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