

Quiz A for 2:30 Class: 8/27/12

Name _____

Assume that you can borrow or lend at a risk-free interest rate of 3.5% per year. Assume also that the bid and ask prices for a risk-free bond that matures one year from today for \$7000 are as follows: Bid = \$6699 , Ask = \$6701. What set of transactions today will generate an arbitrage profit for you today. In your answer list all transactions required today and a year from today and all individual and total cash flows today and a year from today. Use a "+" for an inflow of cash and a "-" for an outflow of cash. Note: I recommend setting up a table like is in the notes, but this is not required.

Wall Street Journal Questions are on the back of this page.