Quiz B for 4:00 Class: 10/01/12 Name ____________________________

Note: Answer all of the following on a single graph. Be sure to clearly label which part of the graph answers which question.

Assume that the risk-free interest rate is 2% and that the expected return and standard deviation of returns on Merck and Barnes & Noble are as follows: .

Asset	Expected Return	Standard Deviation
Merck	11%	17%
Barnes & Noble	30%	40%

The correlation between the returns on Merck and Barnes & Noble is 0.25

a. Sketch a graph of all possible portfolios you could build if you limit yourself to Merck and Barnes & Noble. Identify your portfolio if you have invested $900,000 in Merck and invested $100,000 in Barnes & Noble.

b. Assume that you have also decided to add risk-free Treasuries to your portfolio and that you wish to maintain the standard deviation of returns you had in part a. Show how much better off you are due to the change in your portfolio.

c. Based on your graphs, list the transactions you would have to make as you adjust from the portfolio in part a. to the portfolio in part b.

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