Quiz A for 2:30 Class: 11/07/12 Name ____________________________

Recount Inc. has a current price of \$60 per share. For each of the next two years, Recount's stock price will either rise \$12 per share or fall \$8 per share. Thus, Recount's stock price will equal either \$72 or \$52 per share one year from today, and Recount's stock price will equal either \$84 or \$64 or \$44 per share two years from today. Assume that the risk-free interest rate equals 6% and that replicating portfolios for a particular call on Recount would need to consist of the following:

Today: $\Delta = +0.8743$, $B = -35.9644$
One year from today:
If Recount's stock price climbs to \$72: $\Delta = +1.0$, $B = -47.1698$
If Recount's stock price falls to \$52: $\Delta = +0.7$, $B = -29.0566$

a. What transactions would be required today and one year from today to build the replicating portfolios?
b. Assume Recount's stock price climbs to \$72 next year. Calculate the possible payoffs two years from today on the portfolio you built one year from today ($\Delta = +1.0$, $B = -47.1698$)?
c. Assume Recount's stock price falls to \$52 next year. Calculate the possible payoffs two years from today on the portfolio you build one year from today ($\Delta = +0.7$, $B = -29.0566$) ?

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