

Quiz: 1/23/12

Name & Class Time _____

Assume that risk-free bonds earn a return of 3.5% and that an investment today of \$1000 in the market index fund will pay off either \$1200 (strong economy) or \$850 (weak economy) one year from today. Assume also that an investment of \$720 today in SFNY Inc. will pay off either \$925 (strong) or \$575 (weak) one year from today. List all transactions or events and the resulting cash flows both today and one year from today that would generate an arbitrage profit today. Note: Feel free to create a table to answer this question.