

Quiz B: 8/8/16

Name _____

Assume that the risk-free rate equals 2%, that Blend stock currently trades for \$70 per share, and that for each of the next two years Blend's stock will either rise by \$6 per share or fall by \$3 per share. Assume that you would like to create a portfolio that generates the same payoffs as a put on Blend with a \$75 strike price.

- a. What transactions would be required today to create the portfolio? What would be the total cost to set up the portfolio?
- b. Assume the price of Blend Corp. falls a year from today. What transactions would be required to balance your portfolio? What cash flows will each transaction create? What is your total net cash flow a year from today?
- c. Assume the price of Blend Corp. rises a year from today and again two years from today. What transactions will be required to liquidate your portfolio? What cash flows will each transaction create? What is your total net cash flow two years from today?