Portfolio Theory
Homework 1

Sembenico, Alvise
12380288

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As in this exercise we are looking at several stochastic processes and have to classify as predictable or just adapted, we will first show that the indicator function is adapted/predictable if the argument is adapted/predictable. This is true almost just by definition as the preimage is the following.

$$\mathbb{1}_A^{-1}(x) = \begin{cases} A \text{ if } x = 1 \\ \Omega \setminus A \text{ if } x = 0 \end{cases} \tag{1}$$

Where $A \in \mathcal{F}$ so does $\Omega \setminus A = A^C$. With this in mind, we can proceed on considering the following processes.

- $\varphi_t = \mathbb{1}_{\{S_t^{(1)} > S_{t-1}^{(1)}\}}$;

  ϕ_t is merely adapted as S_t is just adapted.

- $\varphi_1 = 1$ and $\varphi_t = \mathbb{1}_{\{S_{t-1}^{(1)} > S_{t-2}^{(1)}\}}$ for $t \geq 2$;

  ϕ_t is predictable as both process are $\mathcal{F}_t$ measurable, thus, ϕ_{t-1} is $\mathcal{F}_t$ measurable.

- $\varphi_t = \mathbb{1}_A \cdot \mathbb{1}_{\{t > t_0\}}$, where $t_0 \in \{0, \ldots, T\}$ and $A \in \mathcal{F}_{t_0}$;

  We can see that $\mathbb{1}_A$ and $\mathbb{1}_{t > t_0}$ are both deterministic functions, moreover, given that $A \in \mathcal{F}_0$, we have that for every $t \geq 1$, ϕ_t is F_{t+1} measurable, therefore the process is predictable.

- $\varphi_t = \mathbb{1}_{\{S_t^{(1)} > S_0^{(1)}\}}$;

  Again by looking at the argument of the argument of the indicator function, we see that S_t is merely adapted. It follows that ϕ_t is also just adapted...

- $\varphi_1 = 1$ and $\varphi_t = 2\varphi_{t-1}\mathbb{1}_{\{S_{t-1}^{(1)} < S_0^{(1)}\}}$ for $t \geq 2$.

  We can see that the argument of the indicator function is again predictable. We have to be careful about the ϕ_{t-1} component. However, using an induction argument, we can see that each ϕ_{t-1} is $\mathcal{F}_t$ measurable, making it predictable. It follows that ϕ_t is predictable as well.

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