

Q10) If the following 2 assets are correctly priced according to the security market line, what is the return of the market portfolio? What is the risk free return?

$$M_1 = 9.5\% \quad M_2 = 13.5\% \quad \beta_1 = 0.8 \quad \beta_2 = 1.3$$

Now,

$$0.095 - r_f = 0.8(r_m - r_f)$$

$$0.135 - r_f = 1.3(r_m - r_f)$$

Solving these 2 equations we get

$$r_f = 0.031 \quad r_m = 0.111$$

Therefore r_m / R_f return is 3.1%.

Return on market portfolio is 11.1%.