

You will be endowed with some cash and a certain number of three risky securities, Stocks A, B and C, and one risk free security, Notes. You will be able to trade these for about 45 minutes. Shortsales will be allowed *in notes* (up to a certain level).

After markets close, the securities pay a liquidating dividend, depending on the drawing of one of four possible states X, Y, W or Z. These states are equally likely to occur. Liquidating dividends depend on the states as follows:

If State Is...	X	Y	W	Z
Stock A Pays	10	0	7.5	2.5
Stock B Pays	0	2.5	7.5	10
Stock C Pays	0	7.5	2.5	10
Note Pays	5	5	5	5

Your performance will NOT depend on drawing of just one state, but on averages across states. Specifically, your performance will be based on the final composition of your portfolio. We will evaluate how high its expected payoff is, while penalising risk (payoff variance). Use the accompanying excel spreadsheet to compute performance, and to study the effect of trading on performance.

The performance formula equals:

$$Performance = Expected Payoff - b * Payoff Variance$$

Where b (penalty for risk) depends on your student ID. If your ID is **1082500** or higher, set  $b = 0.0175$ . Otherwise (if your ID is below 1082500) set  $b = 0.007$ .\*

(Cash has no payoff variance; nor does the Note.)

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\* In the spreadsheet, b is set equal to 0.01. You need to change that.