

UNIVERSITY OF TEXAS AT AUSTIN

Lecture 3

Standing Assumptions and Conventions.

3.1. Standing Assumptions.

- Everyone has an infinite line of credit.
- There is one prevailing interest rate, the same for everyone and the same for both lending and borrowing.
- Shares of stock and monetary amounts can be subdivided into arbitrary amounts for sale and purchase.
- **NO ARBITRAGE!**

3.2. Conventions. Unless **explicitly** stated otherwise:

- Stocks do not pay dividends.
- The purchase price for any asset is the same as the selling price, i.e., there is no bid-ask spread.
- There are no transaction costs.
- Derivative securities are European-style.