

Def'n.

continuously compounded, risk-free interest rate r satisfies

$$a(t) = e^{r \cdot t}$$

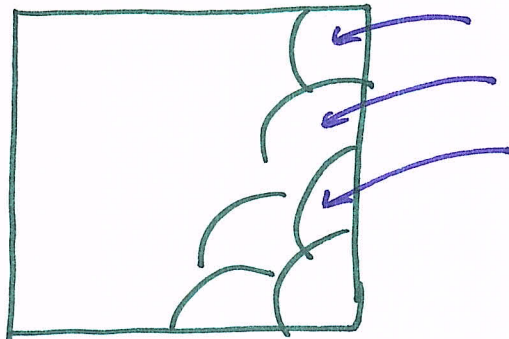
Single PREVAILING interest rate:

- the same for borrowing and lending
- the same for everyone
- deterministic and constant

For convenience:

- Infinite line of credit for everyone.
- Money is continuously valued;

e.g., $\$e^{0.06}$ is fine ;)

CompanyShares of stock

We assume that they are arbitrarily divisible as well, e.g.,

• $\frac{2}{3}$ is fine.

• $e^{-0.06}$ is fine

Investors buy stocks (RISKY ASSETS!) because they hope to be compensated.

They receive compensation in the form of dividends and stock appreciation.

