

Assignment for May 27th

Anna is willing to pay up to 5,65 Euros for a lottery ticket which gives her 100 Euros now with a probability 10%. But she will pay only 5,09 Euros for the same ticket if the draw is not now but in one month.

1. How much is Anna willing to participate in a lottery with two independent draws, one which gives her 50 Euros with a probability 5% and the other 200 Euros with a probability 20% (you can win both)
2. How much is she willing to pay now to participate in the same lottery if the draws happen in one year ?
3. Anna is betting 100 Euros now two to one (meaning she earns 200 if she wins and nothing if she loses) on Real winning the soccer final against Liverpool in one month's time. What is the probability she gives to Real winning ?

You will assume that Anna conforms exactly to the standard model, with a utility function $u(m) = m^\alpha$. ass