

## Construct arbitrage portfolios for mispriced forwards and similar derivatives

1. **Read** the problem.
2. Determine whether to be the **payer** or the **receiver**:

Condition in favor of being payer	Condition in favor of being receiver
$F(t, T)$ or $K$ is <b>too low</b> "I like paying too little"	$F(t, T)$ or $K$ is <b>too high</b> "I like being paid too much"
3. Draw **diagram** of processes promised to occur thanks to position in forward (or forward-esque) contract.
4. **Label original mispriced price** of forward (or forward-esque) contract.
5. Prepare at **present time holdings** (could be long, could be short) of assets that can be used **to make sure you can make each payment you are obliged to make.**
6. Prepare at **present time holdings** (could be long, could be short) of assets that can be used **to absorb each payment you are promised.**
7. Label values of all holdings so far illustrated at present time.
8. Add a bag of cash at present time to **bring present value of portfolio to zero.**
9. **Determine final value of portfolio** (probably amounts to determining final value of bag of cash).