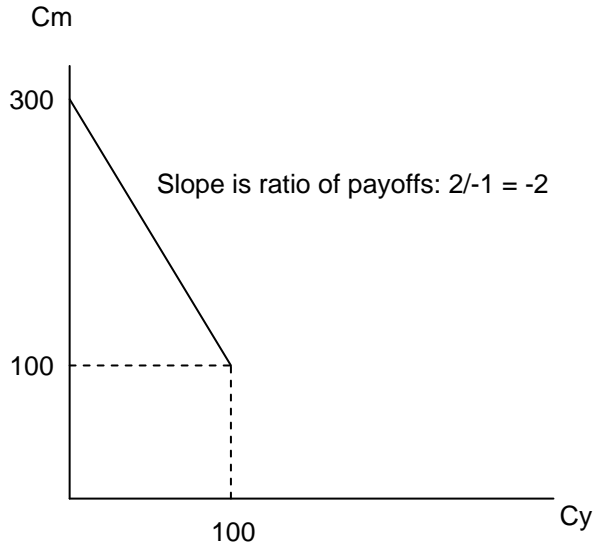Gambling on the World Series
Notes on Solution

1 Consumption possibilities accessible by betting on the Marlins:
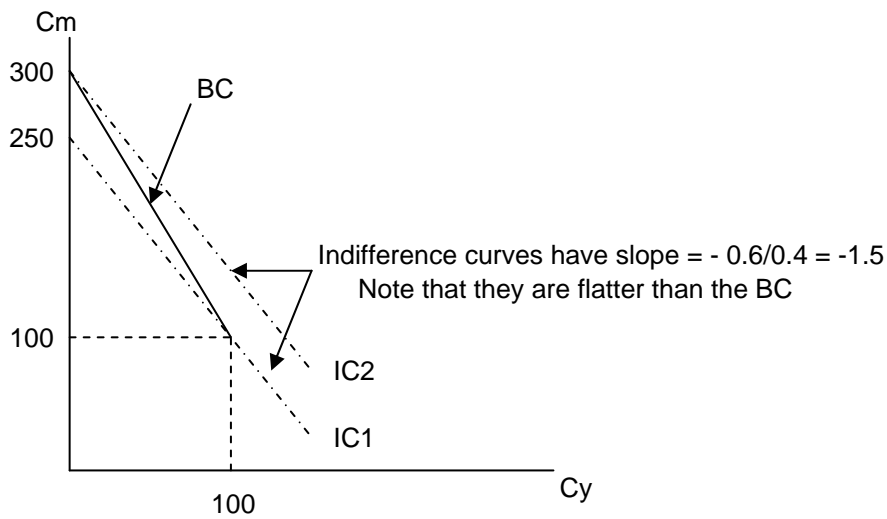
Cm

300

Slope is ratio of payoffs: 2/-1 = -2

100

100   Cy

2 Risk neutral indifference curves

Points indifferent to the endowment have the same expected value:

0.4*Cm + 0.6*Cy = 100
Cm = (100 - 0.6*Cy)/0.4
Cm = 250 - 1.5*Cy

Vertical intercept is at Cm=250; slope is -1.5

Cm

300   BC
250

Indifference curves have slope = - 0.6/0.4 = -1.5
Note that they are flatter than the BC

100

IC2

IC1

100   Cy

3 Expected value of a $1 bet is 0.4*(2) + 0.6*(-1) = 0.2
Bet is not fair because its EV is not zero. Given Pete's inside
information, the bet is better (more favorable) than fair.
Since he is risk-neutral and the bet has a positive expected
value, he would bet the entire $100.

```
                              40%          2
                                   Marlins win
                    ◯
                         Yankess win
              Yes         60%
                                   -1
        ▢
              No
     Bet?            0                      Payoffs
```