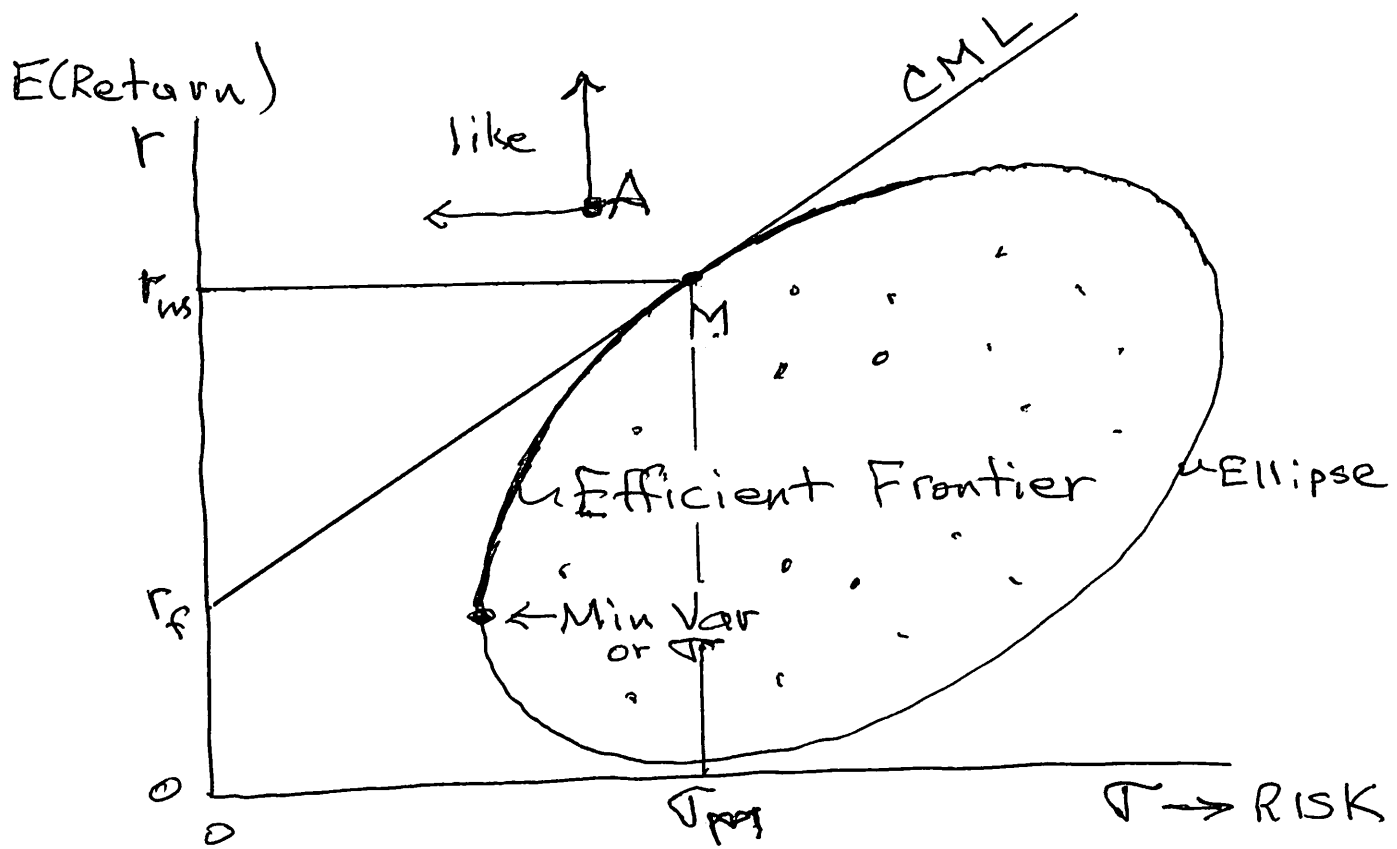
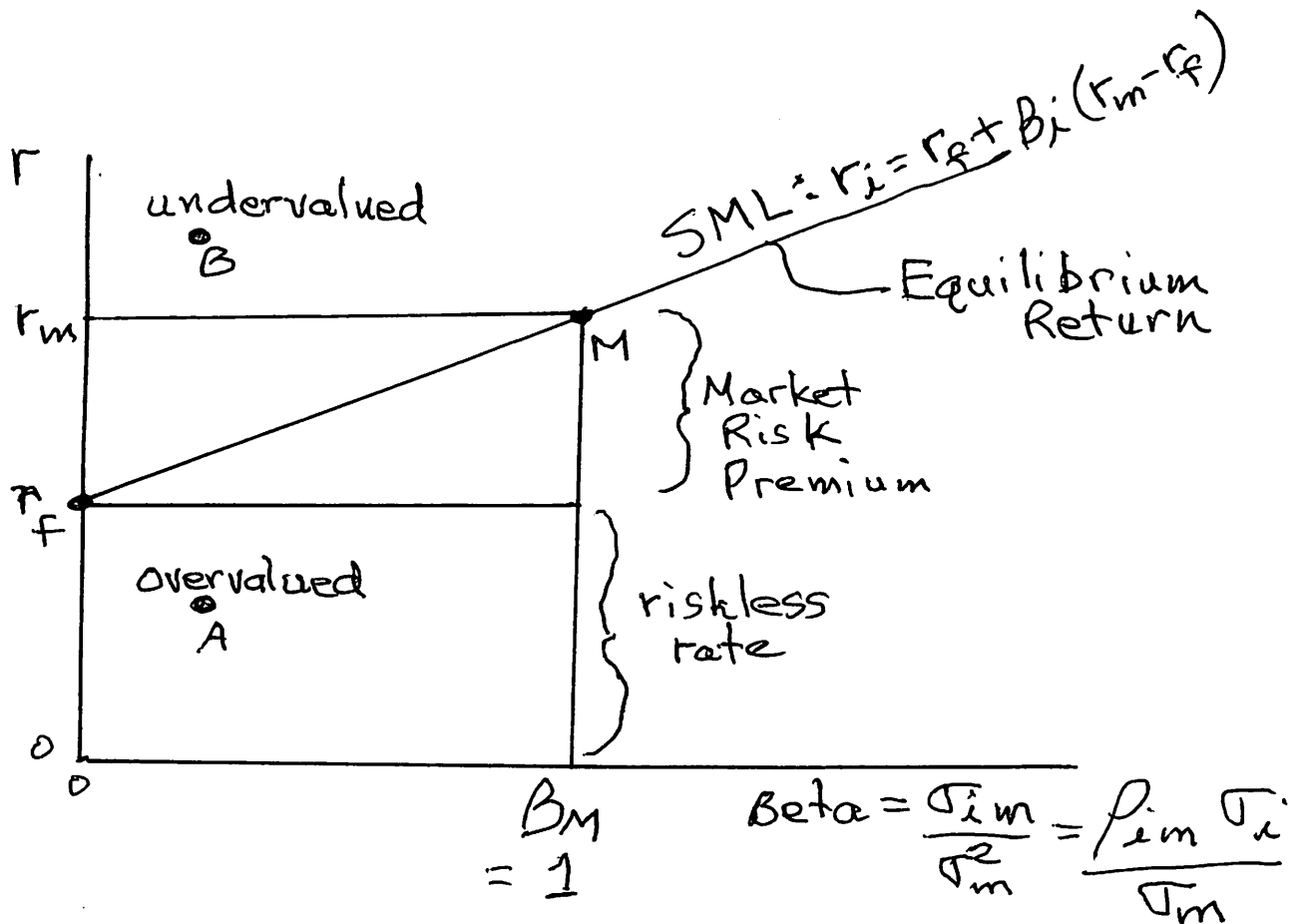




CML Shows 2 fund separation:
 Investors pick a combination
 of riskless asset & market portfolio



SML shows how assets
should be priced

One Portfolio :

Var/Cov of n assets

$$\sigma_P^2 = W S W'$$

$(1 \times n) \quad (n \times n) \quad \downarrow$
 $\swarrow \quad \nwarrow \quad \downarrow$
 $(1 \times n) \quad (n \times 1)$
 $\swarrow \quad \nwarrow$
 (1×1)

3 Portfolios composed of 10 assets :

$$\sigma_P^2 = W S W'$$

$(3 \times 10) \quad (10 \times 10) \quad \downarrow$
 $\swarrow \quad \nwarrow \quad \downarrow$
 $(3 \times 10) \quad (10 \times 3)$
 $\swarrow \quad \nwarrow$
 (3×3)

P_1	$\sigma_{P_1}^2$		
P_2		$\sigma_{P_2}^2$	
P_3			$\sigma_{P_3}^2$
	P_1	P_2	P_3

See Chapter 8, xlsm Pages 207-209