INDIFFERENCE SWAP RATES IN INCOMPLETE MARKETS

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Abstract

We study portfolio optimization and indifference pricing in markets where illiquidity may affect the transfer of wealth over time and between asset classes. We extend certain fundamental results on arbitrage bounds, attainable claims and duality to illiquid markets and general swap contracts where both claims and premiums may have multiple pay-out dates. The results are illustrated with applications to overnight index swaps, equity index options and defined benefit pensions.