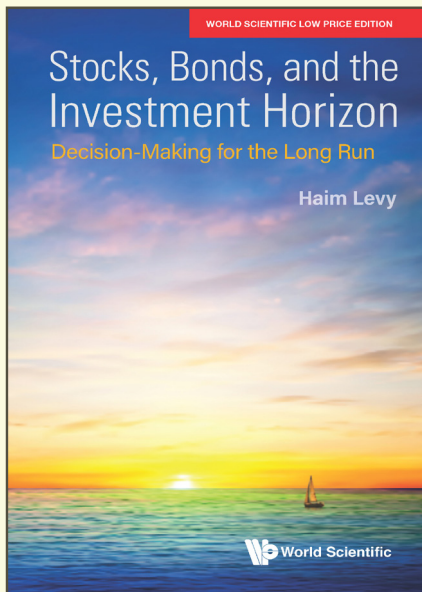


# Stocks, Bonds, and the Investment Horizon

## Decision-Making for the Long Run



By **Haim Levy**  
(The Hebrew University of Jerusalem, Israel)

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### ABOUT THE BOOK

A century ago, life expectancy was roughly 40 years, hence all income could be consumed, as for most people, there was no need to save for retirement. Today, things have drastically changed: Life expectancy exceeds 80 years in many countries, and one should expect to live and consume many years after retirement. Thus, we have many investors with various investment horizons, where the length of the investment horizon becomes a crucial factor in determining the best investment diversification.

This book analyzes the effect of the investment horizon on the optimal diversification, specifically between stocks and bonds: Should a young investor and an older investor have the same portfolio? Is it recommended to savers for retirement to change the asset allocation between stocks and bonds as they grow older, as life cycle mutual funds do in practice? Is the idiom “stocks for the long run” backed by scientific evidence? We analyze for which horizons it is recommended to employ the popular Mean–Variance rule and for which horizons employing this rule induces an economic distortion, hence a loss to the investors. It is shown that all relevant parameters for investment choice (means, variances, and correlations) change in a non-linear way with the horizon, a fact that makes the investment horizon crucial for investment choices. Similarly, the popular Sharpe, Treynor, and Jensen performance indices vary with the assumed horizon even in the case of independence over time. To analyze all the above issues, we employ the Mean–Variance rule and Stochastic Dominance rules, as well as direct expected utility calculations.

### READERSHIP

MBA, MA and PhD students and researchers specialising in economics and finance. Practitioners who rely on reported Sharpe ratio in selecting their investment, as well as those who employ the Mean-Variance rule for optimal diversification.

### CONTENTS

- Asset Allocation and the Horizon: The Ongoing Disputes
- The Distribution of Returns and the Horizon
- Mean–Variance, Stochastic Dominance, and the Investment Horizon
- Performance Indices and the Investment Horizon

- Stocks Versus Bonds: Mean–Variance and Expected Utility Paradigms
- Risk and the Horizon: The Discounting Cash-Flows Approach with Rothschild and Stiglitz's Definition of Risk
- Stock Risk: Do Historical Crashes Tell the Whole Story? The Black Swan Hypothesis
- Discrete and Continuous Returns and the Investment Horizon
- Almost Stochastic Dominance Rules and the Horizon
- Prospect Theory and the Horizon
- The Change in the Relative Attractiveness of Stocks and Bonds with the Horizon with a Riskless Asset

## ABOUT THE AUTHOR

**Haim Levy** is the Miles Robinson Professor of Finance at The Hebrew University of Jerusalem, and has also taught at leading universities in the United States. He has authored 20 books and published over 250 papers in leading academic journals. Levy is one of the founders of the “Stochastic Dominance” paradigm, which provides distribution-free investment decision rules, and is known for his works on the effects of the investment horizon on optimal investment and on market equilibrium. He has also written pioneering studies on international diversification, and on generalizations of the Capital Asset Pricing Model (CAPM). Levy was awarded the EMET Prize and the Israel Prize for his academic work. In parallel to his academic career, Levy has been active in the practice of investments, being a member and chair of investment boards and bank boards.

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