Beyond the short run: The longer time scale volatility of investment value

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Abstract
Fund and other investments often exhibit longer run volatility associated with macroeconomic or other dynamics to an extent inconsistent with the efficient market accumulation model. Volatility and performance models or metrics based on one-period returns or simple extensions can fail to pick this up, resulting in suboptimal investment policies, or welfare losses if exit happens to be forced at the wrong time. We show how to use wavelet analysis to resolve problems of detection, attribution and welfare measurement, including assigning volatility metrics and path risk, while dynamic value at risk ideas can be applied to establish clearance points relative to any benchmark comparator path. Generalizations of the spectral utility function can guide investment policy or be used to design optimal portfolios. Band pass portfolios can be designed that smooth investor exposure to long or short run instabilities in investment value.

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