

Dynamic Investing

User's Manual

Main Fields

Each sheet contains two main fields, one including the main assumptions and one summarizing the results.

The field "**Key Assumptions**" contains information about the market conditions and the investor's preferences. The market conditions are characterized by asset returns and state probabilities. Under mean reversion or momentum, the user needs to distinguish between two previous market conditions: "up" and "down". This is important as the future probabilities change in dependence of the previous market conditions. The button RUN generates the results.

The field "**Results**" reports the results of the calculations: the asset allocation, the associated utility and income distribution. The asset allocation describes the optimal split of wealth between cash and risky assets in the current period and in the case that the market goes up or down in the period ahead. The utility level refers to the current utility of the investor following this strategy. The income distribution describes the development of investor's financial capital over time.

Description of the Included Sheets

The sheet "CRRA TAA" calculates the optimal tactical asset allocation of an expected utility maximizer with CRRA. It is based on a period-by-period optimization.

The sheet "CRRA SAA" calculates the strategic asset allocation of a CRRA investor. His optimal asset allocation takes into account future adjustments in dependence of the expected asset returns/wealth and its probability distribution.

The sheet "CRRA SAA forced" calculates the optimal strategic asset allocation of a CRRA investor without timing abilities on a mean reversion.

The sheet "PT TAA" calculates the tactical asset allocation of a Prospect Theory investor. It is based on a period-by-period optimization. The reference point of the investor is his initial wealth.

The sheet "PT SAA" calculates the strategic asset allocation of a Prospect Theory investor. His optimal asset allocation takes into account future adjustments in dependence of the expected asset returns/wealth relative to his initial wealth and its probability distribution.

The sheet "PT SAA forced" calculates the optimal strategic asset allocation of a Prospect Theory investor without timing abilities on a mean reversion.

Problem Shooting

If you have problems to generate results visit the site:
<http://www.egr.msu.edu/~lira/supp/macro.htm#pointing>
or send an email: kremena@isb.uzh.ch