

PORTFOLIO THEORY AND INVESTMENT POLICY

Teaching Session
EDWIN J. ELTON*

1. An examination of modern portfolio theory
2. Alternative method of attaining input to the portfolio selection process
3. Alternative method of validating portfolio performance.

Dr. Elton presented an overview of modern portfolio theory. He also described an interesting application on which he is currently working. The bibliography for his presentation follows:

BIBLIOGRAPHY

I. Standard Treatments of Portfolio Theory

- (1) Markowitz, Harry, Portfolio Selection, Efficient Diversification of Investments, (John Wiley and Sons, New York, N.Y.) 1959.

Discusses the classic treatment by the founder of Portfolio Theory, very readable and still very much up to date.

- (2) Sharpe, William, Portfolio Theory and Capital Markets, (McGraw Hill, New York, N.Y.) 1970.

The best of recent treatments.

II. Obtaining Inputs

- (1) Sharpe, William, "A Simplified Model of Portfolio Analysis," Management Science, (January, 1963) pp. 277-293 or a chapter in the Sharpe book referenced above.

The presentation of the single index model.

*Dr. Elton, not a member of the Society, is Professor, Graduate School of Business, New York University, New York, New York.

- (2) Cohen, Kalman and Pogue, Jerry, "An Empirical Evaluation of Alternative Portfolio Selection Models," Journal of Business (April, 1967) pp. 166-193.

Compares single and multi-index models.

- (3) Elton, Edwin J. and Gruber, Martin J., "Estimating the Dependence Structure of Share Prices - Implications for Portfolio Selection," Journal of Finance (December, 1973) pp. 1023-33.

Compares single index, multi-index and correlation models.

III. Simple Criteria for Optional Portfolio Selection

This is traced out in a series of papers available from the Solomon Center at the Graduate School of Business, New York University, 90 Trinity Place, New York, N. Y. Representative are:

- (1) Elton, Edwin J., Gruber, Martin J. and Padberg, Manfred, "Simple Criteria for Optional Portfolio Selection."
 (2) Elton, Gruber, Padberg, "Optional Portfolio Selection Via Simple Decision Rules."

IV. Use of Historical Data in Estimating Inputs

- (1) II-2 and II-3 above for correlation or covariance structure
 (2) Blume, Marshall, "The Assessment of Risk," Journal of Finance (March, 1971) pp. 1-10.

Discusses the stability of Beta.

- (3) Fama, Eugene, "The Behavior of Stock Market Prices," Journal of Business (January, 1965) pp. 34-105.

Discusses the use of historical data to forecast future returns.

V. The Effect of Portfolio Size on Diversification

- (1) Fisher, Lawrence and Lorie, James, "Some Studies on Variability of Returns on Investment in Common Stocks," Journal of Business (July, 1968) pp. 291-316.

This is a simulation study.

- (2) Elton, Edwin J. and Gruber, Martin J., "The Effect on the Number of Securities on Risk."