

Index

- AAA bond yields, 85, 257–259
Abel, Andrew, 147
Against the Odds: The Remarkable Story of Risk (Bernstein), 15
Allen, Franklen, 97
alpha games, 205–236
alpha seeking applications, 237–264
Altman, Edward I., 86, 200
Altman, Robert, 166
The American Paradox (Myers), 111
Amromin, Gene, 94
Anderson, Phillip, 175
Andrukonis, David A., 227–228
Ang, Andrew, 61, 71, 72
anomalies, investing in, 248–250
Arbitrage Pricing Theory (APT), 15–16, 25–27, 46, 50–52, 58–61, 267
arbitraging put-call parity, 179
Armstrong, Michael, 215
Arrow, Kenneth, 28
asset pricing theory, 4, 29. *See also* Capital Asset Pricing Model (CAPM)
audit, 229–231
automating activities, 196–202
Axelrod, Robert, 148

Balmer, Johann, 131
Banach Space extensions, 53
Bana, Gaurav, 86
Barber, Brad, 119, 123, 235
Barra company, 26
Barro, Robert, 117
Baruch, Bernard, 160
Barzun, Jacques, 266
Basu, Sanjoy, 249
BBB bond yields, 85, 257–258
Beat the Dealer (Thorpe), 168, 191
behavioral violations of investors, 101–106
benchmarking, 136–37, 143–151

benign deception, 210–214
Bernstein, Peter, 15, 129
Bernstein, William, 173–74
beta, 10, 23–24, 39, 128
beta arbitrage, 244–248
“The Beta Cult! The New Way to Measure Risk,” 39
beta-sorted portfolios, 72–75
bid-ask bounce, 248–249
Black, Fischer, 41–42, 49–50, 53, 68
Black-Scholes-Merton discovery about options, 130
Blodgett, Henry, 212–213
Blum, Michael, 119
B/M ratio, 58
Boehm, Christopher, 220
Bogle, John, 188–190, 210, 235
Bohr, Niels, 131
bonds, 5, 85–91, 190–194, 257–259
Booth, David, 188
Bosschaerts, Peter, 170–171
bosses, 208
Box, George E.P., 13
Bradbury, Ray, 166
Brahe, Tycho, 160
Brealey, Richard A., 97
Brickman, Phillip, 147
Bronkowsky, Jacob, 265
Brown, Donald, 145–146
bubbles, 53–254
Buffett, Warren, 86, 103, 160, 164, 189, 249, 266
Bush, George W., 229
business cycle forecasting, 53–68

call options, 75–76
Campbell, Donal, 147
Campbell, John, 132
“Can Stock Market Forecasters Forecast?” (Cowles), 186

- Capital Asset Pricing Model (CAPM), 1–2, 7, 9–10, 13, 15–25, 36–37, 39–68, 102, 127–33, 191, 238, 244, 247, 269
capital finding alpha strategies, 254–262
CAPM. *See* Capital Asset Pricing Model (CAPM)
Carhart, Mark, 58, 79
Carret, Philip, 189
Cecchetti, Stephen G., 130
CFOs, 192–193
Chen, Nai Fui, 50–51, 59, 61
Chomsky, Noam, 267
Citidel Investments, 191
Class, Status and Party (Weber), 146–147
Clinical versus Statistical Prediction (Meehl), 199
Clinton Administration, 216
Coase Theorem, 28
concavity of utility, 108–109
Constantinides, George, 147
convertible bonds, 190–194
convexity trade, futures and swaps, 179–183
copper, futures, 80
corporate bonds, 85–88
Coval, Joshua D., 75
covariance, 21
Cowles, Alfred, 186–187
credit evaluations, 1930s, 197
Credit Suisse/Tremont Fund Index, 87, 124
cross-sectional returns, total volatility and, 70–72
currencies, 82–84

Daniel, Kent, 55, 57
Darwin, Charles, 144
Das Capital (Marx), 17
Dawkins, Richard, 1
De Bondt, Werner, 49, 115, 249
Debreau, Gerard, 28, 159
Deephaven, 202
Dembo, Ron, 224
The Descent of Man (Darwin), 144
DeVany, Art, 84
Diamond-water paradox, 18–19
Dichev, Ilya, 57, 120–121
Diether, Karl, 95
Dimensional Fund Advisors, 63–64, 137, 174, 188
Discount Factors, 28–32
dishonesty, 207
distress risk, 91–92
diversification, 21–25
 under diversification, 102–103
Douglas, George, 40–42
Drexel Lambert, 86

Easterbook, Gregg, 111
Easterlin, Richard, 109, 147
Easterlin's Paradox, 108–112, 143
economic assumptions, 146–51
Eddington, Arthur, 43–44
efficient frontier, 22
Efficient Markets Hypothesis, 187
Einstein, Alfred, 39, 43, 175
Ellsberg, Richard, 35
Emanuel, Rahm, 216–217
empirical arc, 39–68
envy, 149–151
equilibrium result, 24–25
equity, 93–95
equity hedge funds, 194–196
equity risk premium, 113–125
Eurodollar futures, 180, 182
examples of alpha, 173–203
Exchange-Traded Funds (ETFs), 190

Fibonacci sequence, 183
factor analysis, 26
Falken Fund, 238–239
Fama, Eugene, 1, 4, 13, 41–42, 52–58, 72, 127, 137, 174, 188
Fama-French model, 55–61
Fechner's Law, 155
Fernald, Russell, 145
Feynman, Richard, 98
finding right alpha, 175–178
Fisher, Kenneth, 137
Fisher, Lawrence, 63
forward and futures, 181
Foundations of Economic Analysis (Samuelson), 265, 266
The Four Pillars of Investing (Bernstein), 173–74
Fractals and Scaling in Finance (Mandelbrot), 33
Frank, Robert, 149
Freakanomics, 273n. 6
French, Kenneth, 1, 4, 13, 52–58, 72, 119, 122, 174
Friedman, Milton, 20, 22, 99, 107

- fund innovations, 186–190
futures, 79–82, 179–183
- Galileo, 159–60
Gallup polls, 94
gambling, 160–162
game theory, 164
Gannon, Niall, 119
General Equilibrium Modeling, 27–28
General Theory (Keynes), 156
geometric versus arithmetic averaging, 115–16
Gibbard-Satterthwaite Theorem, 28
Gibbons, Michael R., 45, 53
Goetzmann, William, 102–103
gold, futures, 80
Goldman Sachs, 234
Gorelick, Jamie, 216
Graham, Benjamin, 160, 249
Griffith, Ken, 191
Gross National Product, 64
Grubman, Jack, 215
Gutman, Walter, 168
- happiness data, 109
Happiness: Lessons from a New Science (Layard), 111
Haugen, Robert, 72
Hayek, Friedrich, 206
H coefficient, 34
A History of the Theory of Investments (Rubinstein), 33
Hodrick, Robert, 57, 71, 83
home bias, 105–106
Home Mortgage Disclosure Act, 226
hope investing, 252–253
Houge, Todd, 56, 249–250
households, wealth data, 109–110
Human Universals (Brown), 145–146
- Impossibility Theorem, 28
inequality, 109–110
innovation, uncertainty in, 157–158
Insel, Thomas, 145
“Integrating Methodologists into Teams of Substantive Experts” (Johnston), 199
Interest Rate Parity, 82
interest rate risk, 5
Internal Rate of Return, 120
Internet bubble, 73, 212–213, 289n. 17
introspection, 169
investors and alpha, 233–236
IPOs, 07
- Jangannathan, Ravi, 59
January Effect, 47–48, 248
Jensen, Michael C., 39, 41–42, 53, 79, 163, 178
Jevons, Stanley, 18
Johnston, Rob, 199
Journal of Risk and Uncertainty, 168–170
junk bonds, 86, 256
- Kahneman, Danny, 15, 106
Kalman filter approach, 66, 83
Kelly Criterion, 250
KeyCorp, 196, 200, 214, 229–230, 238
Keynes, John Maynard, 31–36, 64, 81, 95, 156, 158, 254, 266, 286n. 3
Killy, Jean Claude, 158
KMV, 200
Knight, Frank, 17, 21, 23, 35–36, 95, 233
Kuhn, Thomas, 54
Kumar, Ajok, 102–103
kurtosis, 63
Kuznets, Simon, 64
- laboratory experiments, 169
Lange, Oscar, 206
latent factors, 51
Layard, Richard, 111
Leading Economic Indicators (LEI), 66
leverage, 77–78
Lewis, Michael, 207–208
Liar’s Poker (Lewis), 207
Liebowitz, Stan, 227, 228
lies, 207
Lintner, John, 23, 40
Lo, Andrew, 56, 184–186
long and short equity hedge funds, 194–196
Long Term Capital Management, 116
Long-Term Municipal Bond Buyer, 119
Lorie, James H., 63
lotteries, 84, 107
Loughran, Tim, 56, 249–250
Lowenstein, Roger, 234
Lucas, Robert E., 27, 178
Lueckett, Dudley, 100
Lynch, Peter, 164

- Macaulay, 131
MacKinlay, Craig, 184–185
Macroeconomics, 64–65
Madoff, Bernard, 261
Maestripereri, Dario, 146
Mailer, Norman, 162
Maldacena, John, 132
Malkiel, Burton, 79, 87, 97, 123, 188–190
managerial alpha, 218–221
marginal utility, decreasing, 18–20
Marglin, Stephen, 208
market decisions, data drawn from, 169
Market Efficiency, Long-Term Returns, and Market Efficiency (Fama), 108
market leverage, 77–78
market timing, 119–121
Market Wizards (Schwager), 203
Markowitz, Harry M., 15, 22, 33, 44, 100–101, 107–108, 129
Mark, Robert, 230
Martin, Steve, 211
Marx, Karl, 17, 128–129, 146–147
maximum likelihood approach, 45
McQuown, John, 188, 190
mean reversion, pairs and, 183–186
Meehl, Paul, 199
Mehra, Rajnish, 113–114, 117
Menger, Carl, 18
Merrill Lynch High Yield Index, 86–87
Merton, Robert C., 5
Merton's model of default, 200
The Methodology of Positive Economics (Friedman), 99
Milken, Michael, 86
Miller, Ed, 104–105
Miller, Merton, 16, 40–41, 137
Miller-Modigliani Theorem, 16, 77–78, 100
minimum volatility portfolio, 237–244
Minsky, Hyman, 34, 65, 115
The (Mis)Behavior of Markets: A Fractal View of Risk, Ruin and Reward (Mandelbrot and Hudson), 33
Modern Portfolio Theory (MPT), 15, 100–101, 176, 251, 265
Money, Banking, and Financial Markets (Cecchetti), 130
monkeys, relationships, 146
Moody's ratings, 56, 154–155, 200, 238, 255
“More is Different” (Anderson), 175
Morgan, J. P., 160
Morgenstern, Oscar, 20
Mossin, Jan, 23
Munnell, Alicia, 228
mutual funds, 79
Myers, David, 111
Myers, Stewart C., 97
NASDAQ, 94, 121
Nash, John, 175
National Income and Production Accounts, 60, 64
Newtonian mechanics, 39, 43
New York Stock Exchange, 73, 102
Ni, Sophi, 76
NITE Financial, 202
non-normality, 32–34
Nonzero (Wright), 148
NYSE/AMEX, 73, 119, 121, 206
Odean, Terance, 119, 123, 235
One-Fund Separation Theorem, 102
Only Three Questions That Count (Fisher), 137
operational risks, 226
overfitting, 60, 61
overpaid alpha deceptors, 231–233
Paine Webber, 94
pairs and mean reversion, 183–186
The Paradox of Choice (Schwartz), 111
Passions Within Reason (Frank), 149
P/E ratio, 58
peso problems, 117
Peter Principle, 156
Pinker, Steve, 210
Popper, Karl, 53
portfolio count, 21
Portfolio Selection: Efficient Diversification of Investments (Markowitz), 33
portfolio theory, 22
post-depression period, 118
Prescott, Edward C., 113–114, 117
priced risk, 156–157
Princeton Newport, 191
The Progress Paradox (Easterbook), 111
promotional risk and return, 223
Ptolemaic system, 6
puts and calls, 179

- quants, 179
- Rabin, Matthew, 106
- RAND Corporation, 100–101
- Random Walk down Wall Street* (Malkiel), 97, 188
- Recursive Methods in Economic Dynamics* (Stokey and Lucas), 178
- Redleaf, Andy, 179
- Reed, John, 215
- relative risk, 253–254
- relativity theory, 43–44
- Reno, Janet, 227
- returns, 72–75, 87, 95–97. *See also* risk and return
- risk. *See also* risk and return
- alpha contradiction, 163–165
 - aversion and decreasing marginal utility, 18–20
 - and experiments, 168–172
 - gambling, compared, 160–162
 - innovation, uncertainty in, 157–158
 - minimization of, 9–14
 - priced risk, 156–157
 - reason for taking, 165–68
- risk and return:
- academy, response to theory, 4–5
 - and asset pricing theory, 4
 - call options, 75–76
 - creation of standard model, 15–37
 - cross-sectional returns, total volatility and, 70–72
 - small business, 76–78
 - sports books, 92–93
 - theory and practice, 2
 - and volatility, 69–93
 - world country returns, 84–85
- RiskCalc, 200
- risk management, 222–229
- risk-taking, 3, 158–160
- Risk, Uncertainty, and Profits* (Knight), 17, 233
- Ritter, Jay, 96
- Rocheffoucauld, Francois de la, 149–150
- Roll Richard, 45–46, 50–51, 59, 70
- Rosenberg, Barr, 26, 50
- Ross, Stephen, 25, 50–51, 53, 59, 70
- Rubinstein, Mark, 30, 33, 63, 104, 129
- safety, 154–155
- safety investing, 250–252
- Salomon Smith Barney, 215
- Samuelson, Paul A., 128–129, 187, 189, 235, 265, 266
- Savage, Leonard J., 20, 107
- scale, 201
- Schneider, Harold, 220
- Scholes, Myron, 40–42, 53
- Schwager, Jack, 203
- Schwartz, Barry, 111
- Schwartz, Tal, 239–240
- Schwed, Fred, 187
- Schwert, Bill, 49, 248
- Second Order Stochastic Dominion (SOSD), 243
- Security Market Line, 23, 24
- self-deception, 210
- selfishness, 147–148
- seminal credit model, 200
- Senate's Committee on Banking, Housing, and Urban Affairs, 227
- Separation Theorem, 22–23
- Shanken, Jay, 45, 53
- Sharpe model, 3, 14, 59
- Sharpe ratio, 94, 190–191, 232–233, 238–240, 251, 254–255
- Sharpe, Steve, 94
- Sharpe, William, 15, 23, 39, 44, 50, 59, 100, 129
- Shepard's Lemma, 28
- Shiller, Robert, 289n. 17
- Shumway, Tyler, 48, 75
- Simms, Chris, 65
- Sinquefeld, Rex, 63–64, 174, 188, 190
- size of company, 48
- skewness, 61–63
- small business, 76–78
- Smith, Adam, 143–144, 148
- Smith, Fred, 161
- social comparisons, 111
- socialist economies, 206
- speech, 210
- sports books, 92–93
- Standard and Poor's 500, 120, 250
- status groups, 146–147
- Stein, Ben, 86
- Stigler, George, 108
- Stochastic Discount Factor (SDF), 5, 16, 27–32, 36–37, 58–59, 176, 267

- Stock Market Crash of 1987, 113
Stock-Watson model, 66–67
St. Petersburg Paradox, 169
survivorship bias, 116–117
swaps, convexity trade, 179–183
Syron, Richard, 226, 227
- tax effects, asymmetric, 118–19
T-bills, 89–90
Templeton, John, 189
Thaler, Richard, 49, 115, 249
The Theory of Games and Economic Behavior (von Neumann and Morganstern), 20
Theory of Value (Debreau), 159
Thorpe, Edward, 168, 191, 193
Tinbergen, Jan, 64
TIPS, 89–90
Titman, Sheridan, 55, 58
Tobin, James, 22–23
top-line equity risk premium, 125
trading volume, 96–97
transaction costs, 121–124
Treaties on Probability (Keynes), 35
Treyner, Jack, 23, 39
Trivers, Robert, 148
- uncertainty, 34–36, 95–96, 157–158
unit banking, 196
“The Use of Knowledge in Society” (Hayek), 206
U.S. Interest Rate Date: 1958–2008, 89
utility functions of investors, 99–112
- Value Weighted Average Price (VWAP), 122, 201
Vanguard, 188–189
Veblen, Thorstein, 147
Vector Autoregression (VAR), 65
VIX, 93–94
volatility, 7, 69–98, 71
 annual excess returns for G-7 equities, 71
 beta-sorted portfolios, 72–75
 call options, 75–76
 corporate bonds, 85–88
 cross-sectional returns, total volatility and, 70–72
 currencies, 82–84
 expected equity index returns, total volatility and, 93–95
 futures, 79–82
 implied volatilities, 94
 minimum volatility portfolio, 237–244
 mutual funds, 79
 and risk, generally, 97–98
 small business, 76–78
von Mises, Ludwig, 206
von Neuman, Johnny, 20
- Walras, Leon, 18
Wang, Kevin, 59
Wang, Yong, 59
Wang, Zhenyu, 59
Watson, Jim, 66–67
wealth, diminishing marginal utility of, 19
The Wealth of Nations (Smith), 143
Weber, Max, 146–147
Weekend Effect, 248
Weill, Sanford, 215
Wells Fargo, 188
Wenkers, Russ, 79, 189
“What Do Bosses Do?” (Marglin), 208
Where are the Customer’s Yachts? (Schwed), 187
While America Aged (Lowenstein), 234
Whitebox Chapel, 179
Wolfe, Thomas, 147
Wolfe, Tom, 214
world country returns, 84–85
WorldWide Equity Index versus Min Var Subsets of Indexes, 242
Wright, Robert, 148
- Xing, Yuhang, 62, 71
- yield curve, 88–91
Your Money & Your Brain (Zweig), 100
- zero-risk premiums, 135–141
zero-sum game, 9
“ziggurat of status,” 147
Zweig, Jason, 100