Risk: Applying a New Portfolio Risk/Return Measurement Methodology Based on Recent Advances in Quantifying Stable Paretian Fat Tailed Distributions and Investor Loss Aversion Preferences*

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Abstract

Based on recent work by Kevin Dowd on investor loss aversion preferences and work by Benoit Mandelbrot on Stable Paretian distributions with Huston McCulloch's parameter estimation procedures, this paper recommends the practical application of new portfolio risk/return measurements to achieved and back tested stock portfolio performance. This new risk measurement process addresses the issue of infinite variances empirically observed in most stock return distributions.