Theory of portfolio selection

Terence M. Ryan

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Ever since the theory of portfolio selection was invented in the 1950s by Harry Markowitz, a scholarly academic 'computerick' type with a most varied background, studies on the subject have filled the financial and investment journals. Keeping a lot of academics so busy is no mean feat.

Portfolio selection simply gives a rigorous mathematical justification for the time-honoured investment maximum that diversification is a sensible strategy for individuals who would like to reduce their risks. It also tells investors how to combine shares in their portfolios to give them the minimal risk consistent with the return they seek. But the mathematics of portfolio theory is recondite and forbidding; a fact which must have disillusioned many an enthusiastic student.

The proliferation of articles on the subject and the mathematical hurdles they have created, make Mr Ryan's contribution especially acceptable. Working within the objective of the editors of the series of books (of which this forms a part) to give students a relatively straightforward but up-to-date overview of the subject, Mr Ryan has assembled the basic structures of the classic works of Fama, Lintner, Archer, Sharpe, *et al.*, together with many worked numerical examples. It is a refreshing review from across the Atlantic.

Mr Ryan analyses the utility theory foundations of the subject and the theory of asset selection firstly without, and then with, the element of risk. Index models and the efficiency of security models are then considered. The work is concluded with a discussion on multi-period portfolio management. In its objective to give an up-to-date view, the book suffers from the usual long time interval between writing and publishing. However, the inclusion of a reference to the beginnings of the work of people like Barr Rosenberg on alpha coefficients would have added value.

This work falls midway between the lucid, incisive and simplistic brilliance of Burton Malkiel's 'A Random Walk Down Wall Street' and the complex, heavy-going original contributions of the Chicago and Carnegie-Mellon academics. It is suggested that anyone, wishing to gain full benefit from this book, should read it in that sequence or context.

Patrick Kilroe, Senior Lecturer in Organization, Strategy and Finance, School of Business Leadership, University of South Africa