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Abstract

An overlapping generations model with investors having heterogeneous investment horizons leads to a two-factor asset pricing model. The risk premiums are determined by the exposure to the market (myopic betas) and the future return on the efficient portfolio (non-myopic betas), which is identified nonparametrically from equilibrium. Non-myopic betas are priced in the cross-section of stocks, producing increasing and economically significant risk-return relation. In the model with funding constraints, low non-myopic beta stocks deliver higher risk-adjusted returns. Empirically, a betting against non-myopic beta portfolio generates superior performance relative to common factor models and is negatively correlated with the market betting against beta portfolio.

Keywords: Asset prices, Beta, CAPM, Hedging, Strategic asset allocation

JEL classificaiton: G01, G11, G12, G14, G15

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