

Professor Yihong Xia was an expert in studying the behavior of asset returns and its economic and financial implications. Her research covered a broad area of the asset-pricing branch of finance, including individual investors portfolio management, the behavior of asset returns and intertemporal asset pricing models, and the informational role of asset returns.

One strong and influential theme of her research work focused on how investors could and should make optimal portfolio decisions in a time-varying investment condition – a timely topic of considerable importance. The best representation of her work in this area is entitled “In Learning about Predictability: the Effect of Parameter Uncertainty on Dynamic Asset Allocation,” published in the *Journal of Finance* in 2001. In this pioneering paper, Yihong pointed out that learning about stock return predictability is economically important for long-run investors making consumption and portfolio decisions. She wrote this paper as a doctoral student at the UCLA Anderson School of Management, and later joined the faculty of the Wharton School of the University of Pennsylvania in 2000. In her brief five years as an assistant professor, Yihong, working jointly with her co-authors, wrote seven more papers on this topic alone and managed to make an extensive contribution to this important area of Finance.

The second theme of her research work concerns the behavior of asset returns within the framework of inter-temporal asset pricing models. In a 2004 *Journal of Finance* paper entitled “Estimation and Test of a Simple Model of Intertemporal Asset Pricing,” Yihong, working jointly with Michael Brennan and Ashley Wang, investigated the implications of time-varying risk premia on expected bond and equity returns in a unified framework. They showed that their simple and parsimonious Intertemporal Asset Pricing Model can fully explain the well-known size and value premiums. She later expanded her work in this area in several important dimensions, including the implications of the ICAPM models on the international capital markets and the options market.

The third theme of Yihong’s research work focused on the informational role of asset returns. The driving force of her research agenda in this particular topic can be best described in Yihong’s own words: “*In a relatively efficient market, asset prices aggregate and reflect useful and up-to-date information. As a result, they offer us an alternative vehicle for measuring short-term fluctuations in key macroeconomic variables such as inflation, which are unavailable at high frequency.*” Indeed, in “Extracting Inflation from

Stock Returns to Test Purchasing Power Parity,” published in the *American Economic Review* in 2005, Yihong, working jointly with Bhagwan Chowdhry and Richard Roll, used a novel approach to extract the nominal return on a real risk-free asset from stock returns. They further used this information as a surrogate for realized pure price inflation to test the Purchasing Power Parity at various frequencies. They showed that the inflation measure extracted from asset prices better captures temporary swings in inflation and inflation scares.

In her all too brief time as a financial economist, Professor Yihong Xia managed to make a lasting impact to the area of financial economics in general and asset pricing in particular. Her work was rooted in rich economic insights and strong technical abilities, and covered a broad breadth and expanded deep in depth. Her work has been and will remain to be cited by fellow researchers working in her areas of expertise.