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On the Value–Volatility Relationship in a Real Options Model

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Abstract: In the analytical real options approach, the most important proposition that the value of the investment opportunity increases as the volatility increases has been proved by assuming the convexity of the drift of the stochastic differential equationdefined as the state variable. This paper demonstrates numerically that the convexity of the drift is not necessary for that proposition in the real options approach.

Keywords: investment analysis; option-pricing theory; finance; nonlinear stochastic differential equation

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