Two-Fund Separation under Homogeneous Ambiguity

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This paper derives two-fund separation for an economy with agents of multiple-priors utility: Given homogeneous sets of priors and linear risk tolerance felicity functions, an interior equilibrium is Pareto efficient and all agents hold a combination of the riskless security and the market portfolio (i.e., aggregate endowment). This result permits the construction of a representative agent whose preferences follow the multiple-priors model with a utilitarian von-Neumann–Morgenstern utility function.