

FX Comovements: Disentangling the Role of Market Factors, Carry Trades and Idiosyncratic Components

Discussion by Ric Colacito



THE UNIVERSITY
of NORTH CAROLINA
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- 1 Long-run volatility of common risk factors increased after 2008
- 2 Long-run volatility of idiosyncratic risk factors decreased after 2008
- 3 Long-run correlations increased after 2008
- 4 What macro variables can explain FX volatility?

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- Weekly data for G-7 countries from 1988 to 2009.

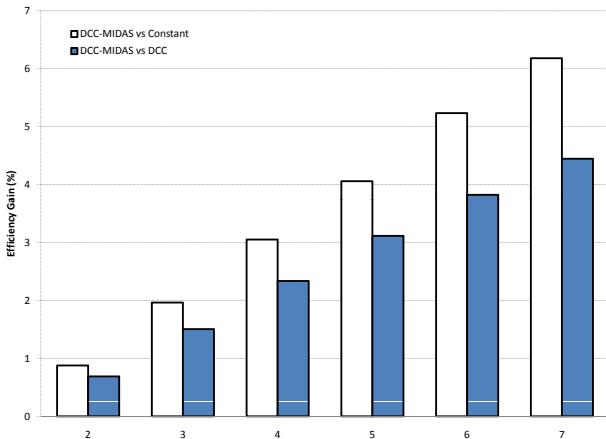
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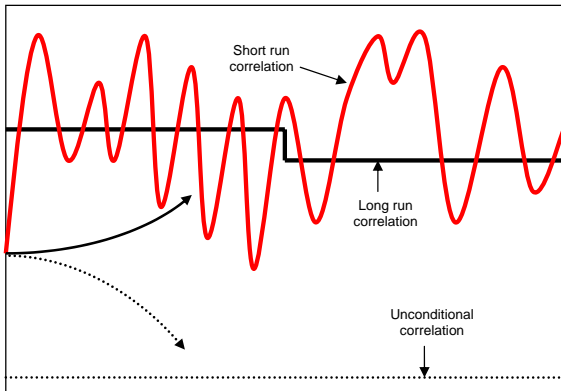
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- Comparison of methodologies?
- Why focus only on carry-trade?
- What fraction of the results is driven by emerging markets?

Other trends?

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- International debt vs consumption growth volatility?
- International correlation of stock market returns and FX volatility?

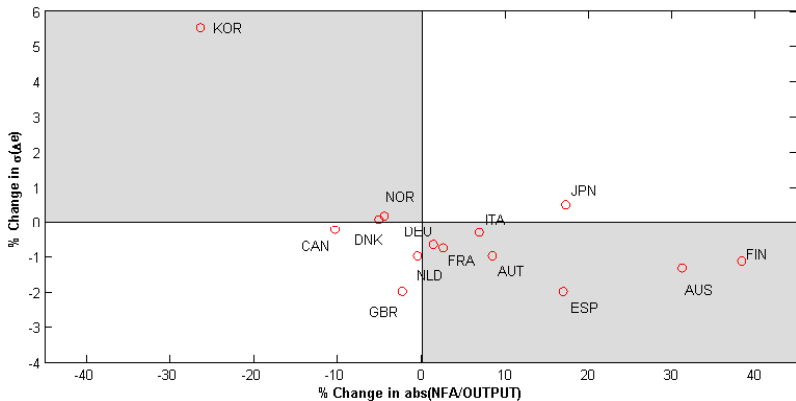
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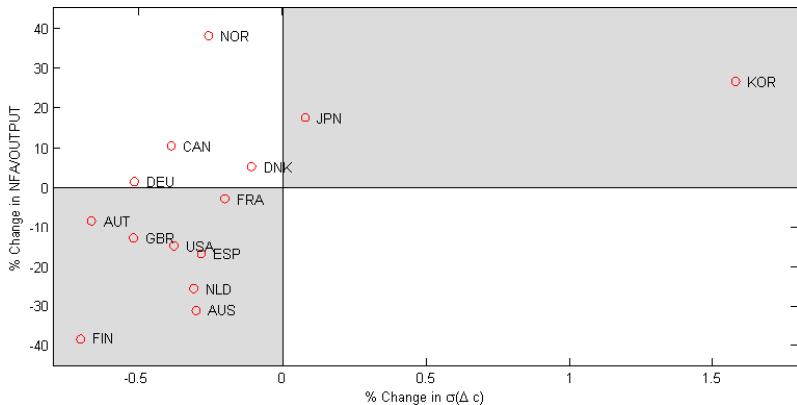
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→ Provide richer set of restrictions for international finance models.

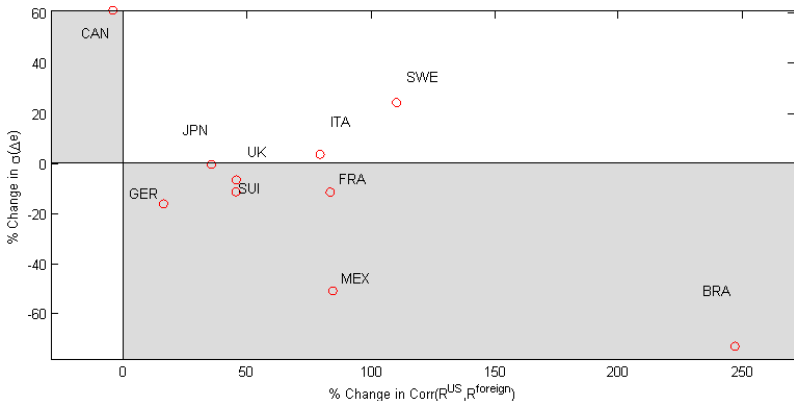
International Debt and FX Volatility



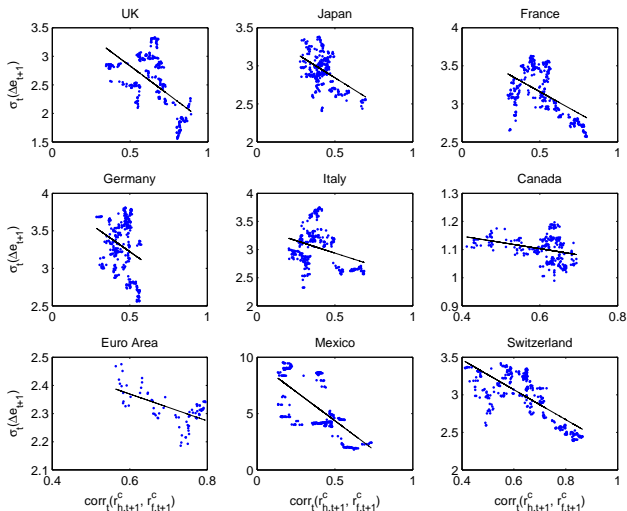
International Debt and Consumption Growth Volatility



Correlation of Stock Returns and FX Volatility



Correlation of Stock Returns and FX Volatility: high frequency



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- Better assessment of link between time-varying second moments and current accounts, net exports, ...
- Useful for international finance modeling, practitioners, and policy makers.

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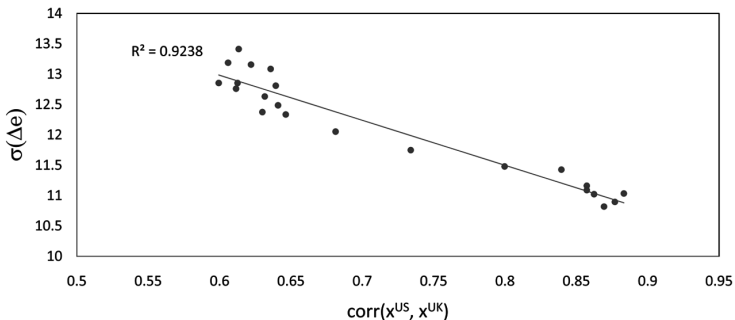
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- Go for it!
- Literature is trying to provide conclusive evidence on the dynamics of common international risk factors
 - Colacito and Croce (JPE, 2011)
 - Lustig, Roussanov, and Verdelhan (RFS, 2011)
 - Stathopoulos (2010)
 - ...

Long-run correlations and FX volatility

Can a better measure of long-run correlation help us to better understand FX volatility?



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- What about bilateral trade variables?
- How does this look in the cross-section of countries?
- What macro variables are responsible for the dynamics of international correlations?

Concluding remarks

- A very interesting paper!
- Suggestions:
 - 1 benefits?
 - 2 other trends?
 - 3 what variables are responsible for FX fluctuations?