

CHIH-CHIANG WU

College of Management, Yuan Ze University, Taiwan

MEICHI HUANG

Department of Business Administration, National Taipei University, Taiwan

CHANG-CHE WU

College of Management, Yuan Ze University, Taiwan

JOINT DYNAMICS IN FOREX TRADING STRATEGY AND GENERAL FINANCIAL MARKETS

Abstract:

This study comprehensively investigates the roles of asymmetry and dynamics in dependence structures across returns to carry trade, stock and bond markets using a novel dynamic asymmetric copula model. We show evidence of a significant increase in carry trade-stock dependence and substantially negative carry trade-bond and stock-bond comovements after the start of the global financial crisis of 2007-2008. We also assess the out-of-sample predictability of dependence timing in the context of asset-allocation strategies, and find that risk-averse investors can generate significant economic value by incorporating asymmetry and dynamics into dependence timing, particularly in the 2007-2008 crisis. Investors would be willing to pay annualized fees of 59 to 861 basis points and 135 to 1554 basis points for strategies that account for asymmetry and dynamics in dependence, respectively. These findings provide new implications for asset-allocation and risk management during turbulent market phases.

Keywords:

Asset-allocation strategies, Asymmetric dependence, Carry trade, Diversification, Dynamic copula