Abstract
Empirical evidence suggests that models of the time-varying conditional minimum-variance hedge ratio (MVHR) are not able to significantly outperform the unconditional MVHR model. In view of the widely documented success of conditional volatility models (on which models of the conditional MVHR are usually based), this is somewhat surprising. In this paper, using the recently developed realized beta framework of Andersen, Bollerslev, Diebold and Wu (2005), we explore the reasons for this finding. We firstly show that the reduction in hedged portfolio variance that conditional MVHR models offer falls far short of the ex post maximal reduction in variance obtained using an estimate of the unobserved 'integrated' MVHR. We investigate the statistical properties of the forecasts of conditional MVHR models and show that while they do contain significant information about the integrated MVHR, they are systematically biased and inefficient. However, correcting for this bias and inefficiency does little to improve their hedging effectiveness, suggesting that their poor performance is more likely to be attributable to the unpredictability of the integrated MVHR

Speakers’ Biography
Evarist holds a PhD and MBA from Xfi Centre for Finance and Investment, University of Exeter. His research interests are in financial econometrics, particularly volatility modelling and applications to portfolio construction

(Tea and Coffee from 14.15 in 8West Common Room opposite 8West3.14)