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Common Volatility across Latin American Foreign Exchange Markets

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Abstract:

This paper uses high frequency exchange rate data for a group of twelve Latin American countries to analyze volatility comovements. Particular interest is posed on understanding the existence of a common volatility process during the 1994–2005 period. The analysis relies on bivariate common factor models. We test for second-order common features using the common ARCH-feature methodology developed by Engle and Kozicki (1993). Overall, the results of this paper indicate that while most currencies display evidence of time-varying variance, the volatility movements in the Latin American foreign exchange markets seems to be mainly country specific. Only a few markets show evidence of a common volatility process.