

BIG DATA & ALGORITHMIC FINANCE



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DOES SPECULATION IN FUTURES MARKETS IMPROVE COMMODITY HEDGING DECISIONS?

Adrian Fernandez-Perez, Ana-Maria Fuertes and Joëlle Miffre.

This article performs a comparative analysis of traditional and selective hedging strategies in commodity futures markets. Traditional hedging solely seeks to minimize risk, while selective hedging simultaneously pursues economic gains by predicting futures returns. The predictions, in turn, range from naïve historical averages to sophisticated forecasts based on, for example, style integration or machine learning. We compare the effectiveness of the various hedges in terms of their ability to maximize expected utility. An out-of-sample analysis applied to 24 commodities endorses traditional over selective hedging, as the latter increases risk but fails to capture alpha. The findings survive different specifications of the traditional and selective hedges, longer estimation windows, alternative rebalancing frequencies, inter alia.

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