Forecasting the CNH-CNY pricing differential: the role of investor attention

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Abstract: As the exponential expansion in the international use of RMB, the issues concerning “one currency, two markets” have attracted increasing attentions from both policymakers and academics. We investigate the predictability of investor attention on the CNH-CNY pricing differential for the period March 2011 until November 2015. Our results show that investor attention displays economically and statistically significant in-sample and out-of-sample predictabilities for the CNH-CNY pricing gap at both monthly and weekly frequencies. In addition, investor attention could generate substantial economic values in asset allocation at both monthly and weekly frequencies. Furthermore, we find that investor attention provides economically and statistically significant out-of-sample forecast for the CNY carry trade on weekly basis.

Key words: CNH-CNY pricing differential; investor attention; macroeconomic variables; out-of-sample forecast; carry trade