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Letter from Editors

The fourth issue of volume 3 consists of three papers, which represent different problems and methods of quantitative and empirical finance.

In the first paper, Łukasz Kwiatkowski proposes a stochastic volatility model incorporating Markov switching in-mean effect (SV-MS-M). It is argued that neglecting possible regime changes in the relation between expected return and volatility may lead to spurious insignificance of the risk premium parameter (as being 'averaged out' over the regimes). The model is analysed within Bayesian framework, which allows to fully account for specification uncertainty. MCMC numerical tools are used and the risk-return relationship for shares of individual companies quoted at the Warsaw Stock Exchange is examined.

In the second paper, Piotr Kębłowski uses the panel VEC framework in order to test whether the floating exchange rates of the EU New Member States against the euro are determined jointly. The main result states that the exchange rates of Czech koruna, Polish zloty and Hungarian forint follow the same long-run relationship. However, it is not true for the Romanian currency (leu).

In the third paper, by Ying Chen and Bo Li, a new methodology (based on functional principal component analysis) is proposed to adaptively forecast yield curves. The local AR(1) model with time-dependent parameters is used to forecast each factor. Simulation and empirical studies reveal the superiority of this method over the dynamic Nelson-Siegel model. In their empirical application the authors focus on the forecasting performance of their method in the case of the yield curves of the U.S. and China.