Pairs Trading - Relative Value

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March 20, 2014

Outline

Introduction

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- Depends upon being able to short securities
    - Professionl ability to borrow securities
    - Use futures or contract-for-difference

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- Can use the Engle-Granger method and check that the residuals from the regression are *stationary*
- If the residuals are stationary, we expect the previous relationship to be restored
- An *Error-Correction Model* can be used to assess the speed of the return to the set relationship

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