

Return, Trading Volume, and Market Depth in Currency Futures Markets

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October 2008

Summary

Theoretically, there are links between variations in return, trading volume, and market depth. In the current exercise, we illustrate the advantage of using stochastic volatility models with multiple latent factors to investigate the joint dynamics of return, trading volume, and open interest (a proxy for market depth) in currency futures markets. In addition to their flexibility to capture unobserved market forces driving the futures market, these models yield estimates that allow us to infer the flows of information between these three aspects of futures contracts. In sum, consistent with theory, the empirical evidence indicates that there is more than one latent factor affecting these three variables. These three variables also display different patterns of information spillovers across currency futures.