



ALTERNATIVE INVESTING

Optimal Currency Hedging for International Equity Portfolios

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We explore optimal currency exposures in international equity portfolios through the lens of a modified mean-variance optimization framework. We decompose the optimal currency portfolio into a “hedge portfolio” which minimizes equity volatility using a dynamic risk model and an “alpha seeking portfolio” based on the well-documented currency styles of value, momentum and carry. This is an integrated and economically intuitive approach to currency management that simultaneously provides lower risk and higher returns compared to both hedged and unhedged benchmarks. Crucially, the solution is practical with realistic and implementable leverage, turnover and tail risk characteristics.

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