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Abstract:

We extract a left tail factor from option contracts and analyze its predictive power for future returns of the Euro Stoxx 50 index and constituents. The estimation procedure is documented and adapted from a methodology applied to the S&P500 option market. The volatility and the negative jump intensity are extracted from option contracts, and explored. The model can be used either with risk-neutral cumulants or with option surfaces as input.

The results show that using the aggregate information with the cumulants provides a good alternative if the computing power is limited. We show that the extracted left tail factor has a predictive power for the Euro Stoxx 50 index future returns over the 15-30 weeks horizon. However, the left tail factor extracted from the Euro Stoxx 50 single stocks options does not have any predictive power over the 1-12 months horizon.