Introduction

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Biographical notes: Jose Olmo is Lecturer in the Economics Department at City University, London. His research interests cover financial econometrics, financial economics and risk management. He has published in top journals such as the *Journal of Business and Economic Statistics, Journal of Financial Econometrics and the Annals of Finance*. He has served as a referee for numerous scientific journals and is on the editorial board of IJMEF. Among other academic activities he has acted as external evaluator for ESRC in the UK, the Spanish Secretary of Education and Science and has acted as a referee in the Occasional Paper Series of the Financial Services Authority.

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When we were deciding upon a remit for the special edition of the *International Journal of Monetary Economics and Finance* there was, of course, a large range of topics worthy of consideration that merit serious academic and practical attention. However, in our discussions with the editor, it soon became clear to us that the measurement of risk in economics and finance would be an ideal topic for the journal. How to measure risk and the application of various measures to practical problems in economics and finance is an ongoing area of research that is unlikely to date in the foreseeable future. From the many paper submissions that were made, we have tried to ensure coverage of a wide range of topics whilst taking into account detailed recommendations from the referee reports. The result was that seven papers survived the process and are presented in this volume.

The paper by Juan Carlos Escanciano and Silvia Mayoral entitled, 'Semiparametric estimation of dynamic conditional expected shortfall models', proposes a simple estimator for a class of conditional expected shortfall risk measures. The quality of the estimator is tested using exchange rate data and is shown to be extremely useful under reasonable regularity conditions. We believe the paper will have many other

applications in areas such equities and the management of bond portfolios. The paper by Ahmed Ghorbel and Abdelwahed Trabelsi entitled 'Predictive performance of conditional Extreme Value Theory in Value-at-Risk estimation', provides a rigorous comparative evaluation of the predictive performance of various Value at Risk (VaR) models using stockmarket data. We believe the paper is important as it presents a systematic evaluation of alternative VaR modelling techniques. The paper has significant relevance to the banking system in light of the fact that the Basle II accord allows banks to adopt different internal risk based management approaches. It is highly desirable that the methods that they choose are tested against one another so that the most useful methods eventually emerge. The issue of value at risk is also taken up in the paper by Keith Pilbeam and Rehan Noronha entitled 'Risk budgeting and Value-at-Risk', the main contribution of this paper is to show that while VaR is not sub additive, it nonetheless remains a useful measure of risk, especially when supplemented by the tools of capital budgeting. The reported results are important as the tools of capital budgeting are extensively used by many financial institutions and fund managers.

The issue of political risk is never far investors minds and is taken up in a novel fashion by Dimitrios Asteriou in his paper entitled 'Country financial and political risk: the case of Indonesia, Malaysia and Philippines'. The paper uses insights from option pricing to estimate financial risk premia, and then the impact of the estimated risk premia on stockmarket performance. The key result of this paper is that a 1% increase in financial risk premia led to a 0.3% fall in expected returns over the period 1990–2004. Given the growing importance of emerging markets in recent years the paper contains useful empirical applications and results for fund managers. The paper by Carla Ysusi entitled, 'Estimating integrated volatility using absolute high-frequency returns', shows that when high-frequency data is used in the context of a stochastic volatility model then realised absolute variation can estimate integrated spot volatility. It is also shown that while the use of absolute values are empirically attractive since they are less sensitive to possible large movements in high-frequency data, there are problems in that realised absolute variation does not estimate integrated variance. We believe the paper highlights in a rigorous fashion some significant problems concerning the use of realised absolute returns in finite data sets that are often overlooked by researchers and practictioners alike.

The paper by Everton Dockery and Miltos Efentakis entitled, 'An empirical comparison of alternative models in estimating Value-at-Risk: evidence and application from the LSE', compares a selection of VaR models using daily data from the London stock exchange. The results reported by the authors suggest that a simple equally weighted moving average model can furnish more accurate estimated VaR than the use of more sophisticated GARCH methods. We believe these results are important because the trend in risk management in recent years has been to utilise increasingly sophisticated econometric models when more simple approaches can often suffice. Finally, the paper by Jose Olmo entitled 'On the role of volatility for modelling risk exposure', looks at the usefulness of volatility as a measure of risk. The paper proposes the use of semi parametric estimators of the distribution function of the return on the asset based on Extreme Value Theory (EVT) for computing VaR and also discusses the validity of different volatility models within this framework. The key contribution of the paper is to show that volatility measures need to be supplemented by estimators of the distribution function of the error term. Another contribution of the paper is to show the effect of choosing the model *ad hoc* rather than minimising the square of the residuals or

maximising the likelihood of some parametric distribution. The paper yields genuine new insights into how to model risk both in theory and in practice.

In sum, this volume represents a real contribution to the ongoing research into the measurement of risk at both the theoretical and empirical level. Of course, the volume would not have been possible without the assistance of many referees. As editors of the special edition we should like to thank them for their contributions which led to some very useful ideas and significant improvements in many of the papers submitted.