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Forecasting Exchange Rates I

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Techniques, Survey Data, and Implications for the Foreign Exchange Market **Forecasting Exchange Rates with Generalized Principal Components** **Meese-Rogoff Redux Exchange Rate Forecasting** Forecasting Financial Markets *Forecasting Exchange Rates On Forecasting Exchange Rate* **How Well Do Monetary Fundamentals Forecast Exchange Rates?** Forecasting Exchange Rates Out-of-sample with Panel Methods and Real-time Data **Forecasting Exchange Rates** **Forecasting Exchange Rates Under Parameter and Model Uncertainty** *Forecasting Exchange Rates* Forecasting Exchange Rates Nonlinear Exchange Rate Models **Long** *Forecasting foreign exchange rates* *Forecasting Exchange Rates with Linear and Nonlinear Models* **Forecasting Exchange Rates** Forecasting Exchange Rates in the Presence of Instabilities

Cover subtitle: An approach to the theory of exchange rates forecasts for the accountant and manager. This paper shows that error correction models assuming that long-maturity forward rates are stationary outperform the random walk in out of sample forecasting at forecasting horizons mostly above one year, for US dollar exchange rates against nine industrial countries' currencies, using the 1990-2006 period for evaluating the out of sample forecasts. The improvement in forecast accuracy of our models is economically significant for most of the exchange rate series, and statistically significant according to a

bootstrap test. Our results are robust to the specification of the error correction model and to the underlying data frequency. With the internationalization of Renminbi (RMB), the gradual liberalization of China's capital account and the recent reform of the RMB pricing mechanism, the RMB exchange rate has been volatile. This book examines how we can forecast exchange rate reliably. It explains how we can do so through a new methodology for exchange rate forecasting. The book also analyzes the dynamic relationship between exchange rate and the exchange rate data decomposition and integration, the domestic economic situation, the international economic situation and the public's expectations and how these interactions would affect the exchange rate. The book also explains why this comprehensive integrated approach is the best model for optimizing accuracy in exchange rate forecasting. Forecasting exchange rates is a variable that preoccupies economists, businesses and governments, being more critical to more people than any other variable. In Exchange Rate Forecasting the author sets out to provide a concise survey of the techniques of forecasting - bringing together the various forecasting methods and applying them to the exchange rate in a highly accessible and readable manner. Highly practical in approach, the book provides an understanding of the techniques of forecasting with an emphasis on its applications and use in business decision-making, such as hedging,

speculation, investment, financing and capital budgeting. In addition, the author also considers recent developments in the field, notably neural networks and chaos, again, with easy-to-understand explanations of these "rocket science" areas. The practical approach to forecasting is also reflected in the number of examples that pepper the text, whilst descriptions of some of the software packages that are used in practice to generate forecasts are also provided. Since Meese and Rogoff (1983) results showed that no model could outperform a random walk in predicting exchange rates. Many papers have tried to find a forecasting methodology that could beat the random walk, at least for certain forecasting periods. This Element compares the Purchasing Power Parity, the Uncovered Interest Rate, the Sticky Price, the Bayesian Model Averaging, and the Bayesian Vector Autoregression models to the random walk benchmark in forecasting exchange rates between most South American currencies and the US Dollar, and between the Paraguayan Guarani and the Brazilian Real and the Argentinian Peso. Forecasts are evaluated under the criteria of Root Mean Square Error, Direction of Change, and the Diebold-Mariano statistic. The results indicate that the two Bayesian models have greater forecasting power and that there is little evidence in favor of using the other three fundamentals models, except Purchasing Power Parity at longer forecasting horizons. The paper presents new empirical results that elucidate the dynamics of

the foreign exchange market. The first half of the paper is an updated study of the exchange rate expectations held by market participants, as reflected in responses to surveys, and contains the following conclusions. First, the bias observed in the forward discount as a predictor of the future spot rate is not attributable to an exchange risk premium, as is conventionally believed. Second, at short horizons forecasters tend to extrapolate recent trends, while at long horizons they tend to forecast a reversal. Third, the bias in expectations is robust in the samples, based on eight years of data across five currencies. The second half of the paper abandons the framework in which all market participants share the same forecast, to focus on the importance of heterogeneous expectations. Tests suggest that dispersion of opinion, as reflected in the standard deviation across respondents in the survey, affects the volume of trading in the market, and, in turn, the degree of volatility of the exchange rate. An example of how conflicting forecasts can lead to swings in the exchange rate is the model of "chartists and fundamentalists." The market weights assigned to the two models fluctuate over time in response to recent developments, leading to fluctuations in the demand for foreign currency. The paper ends with one piece of evidence to support the model: the fraction of foreign exchange forecasting services that use "technical analysis" did indeed increase sharply during 1983-85, but declined subsequently We re-examine the

monetary approach to the exchange rate from a number of perspectives, using monthly data on the deutschemark-dollar exchange rate. Using the Campbell-Shiller technique for testing present value models, we reject the restrictions imposed upon the data by the forward-looking rational expectations monetary model. We demonstrate, however, that the monetary model is validated as a long-run equilibrium condition. Moreover, imposing the long-run monetary model restrictions in a dynamic error correction framework leads to exchange rate forecasts which are superior to those generated by a random walk forecasting model. We introduce a forecasting method that closely matches the econometric properties required by the theory of exchange rate prediction. Our approach formally models (i) when (and if) predictor variables enter or leave a regression model, (ii) the degree of parameter instability, (iii) the (potentially) rapidly changing relevance of regressors, and (iv) the appropriate shrinkage intensity over time. We consider (short-term) forecasting of six major US dollar exchange rates using a standard set of macro fundamentals. Our results indicate the importance of shrinkage and flexible model selection criteria to avoid poor forecasting results. "This paper compares the true, ex-ante forecasting performance of a micro-based model against both a standard macro model and a random walk. In contrast to existing literature, which is focused on longer horizon forecasting, we examine forecasting over horizons from one day to one

month (the one-month horizon being where micro and macro analysis begin to overlap). Over our 3-year forecasting sample, we find that the micro-based model consistently out-performs both the random walk and the macro model. Micro-based forecasts account for almost 16 per cent of the sample variance in monthly spot rate changes. These results provide a level of empirical validation as yet unattained by other models. Our result that the micro-based model out-performs the macro model does not imply that macro fundamentals will never explain exchange rates. Quite the contrary, our findings are in fact consistent with the view that the principal driver of exchange rates is standard macro fundamentals. In Evans and Lyons (2004b) we report firm evidence that the non-public information that we exploit here for forecasting exchange rates is also useful for forecasting macro fundamentals themselves"--NBER website

This book focuses on forecasting foreign exchange rates via artificial neural networks (ANNs), creating and applying the highly useful computational techniques of Artificial Neural Networks (ANNs) to foreign-exchange rate forecasting. The result is an up-to-date review of the most recent research developments in forecasting foreign exchange rates coupled with a highly useful methodological approach to predicting rate changes in foreign currency exchanges. Several authors have recently investigated the predictability of exchange rates by fitting a sequence of long-horizon error-correction regressions. By considering the implied

vector error-correction model, we show that little is to be gained from estimating such regressions for horizons greater than one time period. We also show that in small to medium samples the long-horizon procedure gives rise to spurious evidence of predictive power. A simulation study demonstrates that even when using this technique on two independent series, estimates, diagnostic statistics and graphical evidence incorrectly suggest a high degree of predictability of the dependent variable. Seminar paper from the year 2015 in the subject Business economics - Investment and Finance, grade: A, , course: International Financial Management, language: English, abstract: The exchange rate on a daily basis is an indispensable factor in the foreign exchange market as well as in international trade. Many traders make a profit based on the pip in the foreign exchange market. Moreover, inflation and deflation of a currency against another currency is the root of making a profit in the foreign exchange market. Even in the international trade many individual traders and multi-national corporations always carefully observes the fluctuation of the exchange rate in order to determine the exchange rate efficiently and accurately. Because the more accurate the forecasted exchange rate is, the higher the chance becomes to make a profit only by investing a little amount of money in the foreign exchange market. The exchange rate has also significant impact on the export, import, foreign direct investment etc. This paper pursues the goal to explain

how an individual or an organization can formulate future exchange rate of any currency in an efficient and time effective way. To meet this demand, this paper utilizes the help of panel data and a regression model. As a sample, this paper considers USD/BDT for a forecast. It must be noted that, with different panel data of different currencies, the method will remain same if anyone wants to forecast exchange rates of different currencies. Today's financial markets are characterised by a large number of participants, with different appetites for risk, different time horizons, different motivations and reactions to unexpected news. The mathematical techniques and models used in the forecasting of financial markets have therefore grown ever more sophisticated as traders, analysts and investors seek to gain an edge on their competitors. Written by leading international researchers and practitioners, this book focuses on three major themes of today's state of the art financial research: modelling with high frequency data, the information content of volatility markets, and applications of neural networks and genetic algorithms to financial time series. Forecasting Financial Markets includes empirical applications to present the very latest thinking on these complex techniques, including: High frequency exchange rates Intraday volatility Autocorrelation and variance ratio tests Conditional volatility GARCH processes Chaotic systems Nonlinearity Stochastic and EXPAR models Artificial neural networks Genetic algorithms This text

explains the methods and aspects of exchange rate forecasting, including purchasing power, parity, interest rate differentials and technical analysis. Guidelines for reducing risk with forecasting strategies are included, as are techniques for co The medium-term predictability of exchange rate movements is examined using three models of fundamentals: purchasing power parity, the monetary model, and uncovered interest parity. While the first two approaches yield favorable in-sample results, these largely reflect finite-sample estimation biases. Adjusting for these biases, there is little evidence of predictability, consistent with the lack of systematic improvement in out-of-sample forecasting performance relative to a random walk. Uncovered interest parity fares better at long horizons, but reflects information already embodied in market prices; in this sense, it may not be useful as an indicator of exchange rate misalignment. While more elaborate models of fundamentals might have better medium-term forecasting properties, careful attention must be paid to finite-sample biases in assessing predictability. This paper provides a selective overview of nonlinear exchange rate models recently proposed in the literature and assesses their contribution to understanding exchange rate behavior. Two key questions are examined. The first question is whether nonlinear autoregressive models of real exchange rates help resolve the "purchasing power parity (PPP) puzzles." The second question is whether

recently developed nonlinear, regime-switching vector equilibrium correction models of the nominal exchange rate can beat a random walk model, the standard benchmark in the exchange rate literature, in terms of out-of-sample forecasting performance. Finally, issues related to the adequateness of standard methods of evaluation of (linear and nonlinear) exchange rate models are discussed with reference to different forecast accuracy criteria. It is a well known fact that a naive random walk generates better exchange rate forecasts than economic models. The exchange rate is episodically unstable and the switching nature is inconsistent with a linear representation. However, empirical evidence in favour of non-linear models such as regime switching models, neural networks or non-parametric ones is weak. The present paper adopts an econometric method, which incorporates dynamic model averaging (DMA) and selection (DMS). The DMA / DMS framework adds additionally layers of flexibility by allowing parameters as well as the entire forecasting model to evolve over time. In addition this paper takes a different approach by forecasting exchange rates at a daily frequency. Thereby financial data is used as a proxy for macro-economic fundamentals and technical indicators are included in the set of potential predictor variables. The paper shows strong empirical evidence in favour of the employed model in the period before the bankruptcy of Lehman Brothers. During the financial crisis predictability in terms of the mean squared

forecast error breaks down. The time-varying evolution of fundamental and technical forecasts allows investigating the evolution of the influence of two types of agents (fundamentalists and chartists) believed to operate in the foreign exchange market. This is a literature review on exchange rate modeling. This is taken from my doctoral dissertation (My copyright registration number: TX 8-435-669). This may be helpful if you're seeking information on exchange rate, interest rates, gross domestic product, inflation, and money supply. It may also be helpful in understanding the origins of the sticky-price monetary model. This book provides an overview of Chinese RMB exchange markets and its risk management strategies. The view that RMB is playing an increasingly international role has been widely accepted by practitioners as well as scholars worldwide. Moreover, the Chinese government is opening the control of RMB exchange market step by step. However, some related topics are under heated debate, such as how to manage and warn of the currency crisis, what the trend of RMB exchange rate in the future is, and how to hedge the exchange risk in the process of RMB internationalization. In this book, we will give distinct answers to the above questions. We extract principal components from a panel of 17 exchange rates and use the deviations from the components to forecast future exchange rate movements, following the idea in Engel, Mark, and West (2015). Instead of using the standard method, we

apply a generalized principal components analysis that captures temporal and cross-sectional variation and covariation among the exchange rates. We find that the method dominates forecasts by existing standard methods and random walk, with or without including macroeconomic fundamentals. Praise for Handbook of Exchange Rates “This book is remarkable. I expect it to become the anchor reference for people working in the foreign exchange field.” —Richard K. Lyons, Dean and Professor of Finance, Haas School of Business, University of California Berkeley “It is quite easily the most wide ranging treasury of expertise on the forex market I have ever come across. I will be keeping a copy close to my fingertips.” —Jim O’Neill, Chairman, Goldman Sachs Asset Management

How should we evaluate the forecasting power of models? What are appropriate loss functions for major market participants? Is the exchange rate the only means of adjustment? Handbook of Exchange Rates answers these questions and many more, equipping readers with the relevant concepts and policies for working in today’s international economic climate. Featuring contributions written by leading specialists from the global financial arena, this handbook provides a collection of original ideas on foreign exchange (FX) rates in four succinct sections:

- Overview introduces the history of the FX market and exchange rate regimes, discussing key instruments in the trading environment as well as macro and micro approaches to FX determination.
- Exchange Rate Models and

Methods focuses on forecasting exchange rates, featuring methodological contributions on the statistical methods for evaluating forecast performance, parity relationships, fair value models, and flow-based models. • FX Markets and Products outlines active currency management, currency hedging, hedge accounting; high frequency and algorithmic trading in FX; and FX strategy-based products. • FX Markets and Policy explores the current policies in place in global markets and presents a framework for analyzing financial crises. Throughout the book, topics are explored in-depth alongside their founding principles. Each chapter uses real-world examples from the financial industry and concludes with a summary that outlines key points and concepts. Handbook of Exchange Rates is an essential reference for fund managers and investors as well as practitioners and researchers working in finance, banking, business, and econometrics. The book also serves as a valuable supplement for courses on economics, business, and international finance at the upper-undergraduate and graduate levels. "This paper attacks the Meese-Rogoff puzzle from a different perspective: out-of-sample interval forecasting. Most studies in the literature focus on point forecasts. In this paper, we apply Robust Semiparametric (RS) interval forecasting to a group of Taylor rule models. Forecast intervals for twelve OECD exchange rates are generated and modified tests of Giacomini and White (2006) are conducted to

compare the performance of Taylor rule models and the random walk. Our contribution is twofold. First, we find that in general, Taylor rule models generate tighter forecast intervals than the random walk, given that their intervals cover out-of-sample exchange rate realizations equally well. This result is more pronounced at longer horizons. Our results suggest a connection between exchange rates and economic fundamentals: economic variables contain information useful in forecasting the distributions of exchange rates. The benchmark Taylor rule model is also found to perform better than the monetary and PPP models. Second, the inference framework proposed in this paper for forecast-interval evaluation can be applied in a broader context, such as inflation forecasting, not just to the models and interval forecasting methods used in this paper"--P. [2]. This paper examines the dynamics of the foreign exchange market. The first half addresses a number of key questions regarding the forecasts of future exchange rates made by market participants, by means of updated estimates using survey data. Here we follow most of the theoretical and empirical literature in acting as if all market participants share the same expectation. The second half then addresses the possibility of heterogeneous expectations, particularly the distinction between "chartists" and "fundamentalists," and the implications for trading in the foreign exchange market and for the formation of speculative bubbles. Forecasting exchange rates is a variable that

preoccupies economists, businesses and governments, being more critical to more people than any other variable. In *Exchange Rate Forecasting* the author sets out to provide a concise survey of the techniques of forecasting - bringing together the various forecasting methods and applying them to the exchange rate in a highly accessible and readable manner. Highly practical in approach, the book provides an understanding of the techniques of forecasting with an emphasis on its applications and use in business decision-making, such as hedging, speculation, investment, financing and capital budgeting. In addition, the author also considers recent developments in the field, notably neural networks and chaos, again, with easy-to-understand explanations of these "rocket science" areas. The practical approach to forecasting is also reflected in the number of examples that pepper the text, whilst descriptions of some of the software packages that are used in practice to generate forecasts are also provided.

Models and Strategies for Exchange Rate Forecasting Michael R. Rosenberg Getting an accurate exchange rate is critical for any company doing business in today's global economy. *Exchange Rate Determination*--written by the number one-ranked foreign exchange team in the world--examines the methods used to accurately and profitably forecast foreign exchange rates. This hands-on guidebook uses extensive charts and tables to examine currency option markets, productivity trends and exchange

rates; technical analysis methods to improve currency forecasting accuracy; and more.

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