



Contents lists available at ScienceDirect

Journal of International Financial Markets, Institutions & Money

journal homepage: www.elsevier.com/locate/intfin



Two currencies, one model? Evidence from the Wall Street Journal forecast poll

Michael Frenkel^a, Jan-Christoph Rülke^a, Georg Stadtmann^{b,*}

^a WHU – Otto Beisheim School of Management, Vallendar, Germany

^b University of Southern Denmark, Odense, Denmark

ARTICLE INFO

Article history:

Received 21 May 2007

Accepted 20 August 2008

Available online 2 September 2008

JEL classification:

F31

D84

C33

Keywords:

Foreign exchange market

Expectations

Models with panel data

ABSTRACT

We use the foreign exchange forecasts of the Wall Street Journal (WSJ) poll to analyze the expectation formation process of forecasters for the exchange rates of the euro and the yen vis-à-vis the U.S. dollar for the period 1999–2005. We also compare the expectation formation process with the actual exchange rate process. We find that most forecasters have contrarian exchange rate expectations, but our results also indicate significant heterogeneity between forecasters. While the actual exchange rate process of the yen/dollar exchange rate shows negative autocorrelation, the dollar/euro exchange rate exhibits positive autocorrelation.

© 2008 Elsevier B.V. All rights reserved.

1. Introduction

In empirical studies of exchange rate models, researchers test the validity of the examined model and rational expectations. Hence, one of the reasons why empirical studies often find little empirical support for the investigated exchange rate model could be the violation of the rational expectation assumption in the foreign exchange market. In fact, a number of studies have raised doubts about the validity of the rational expectations assumption in this market (e.g., Frankel and Froot, 1987; Frankel and Rose, 1995; Menkhoff, 1998, 2001). In addition, most empirical exchange rate studies implicitly follow the assumption of traditional exchange rate models which claim that financial agents can be viewed as homogenous. However, studies of market microstructure suggest that there are different

* Corresponding author. Tel.: +45 6550 4479.

E-mail address: geo@sam.sdu.dk (G. Stadtmann).

groups of traders in the market. This has led several researchers to develop models with a relaxed rational expectation assumption and a consideration of different types of actors in the currency market (e.g., Frankel and Froot, 1988, 1990; DeLong et al., 1990).

In this paper, we use data from the Wall Street Journal (WSJ) poll to compare the characteristics of the expectation formation process in two different currencies. The WSJ data set enables us to perform this comparison because it contains expectations for both the dollar/euro and the yen/dollar exchange rate. We therefore apply this survey to shed light on two aspects of the expectation formation process. The first aspect refers to the question whether the same expectation formation process applies to both currencies. The second aspect deals with the question whether there are differences between the two foreign exchange markets with respect to the homogeneity or heterogeneity of foreign exchange market forecasters.¹

The remainder of the paper is structured as follows. In the next section, we describe some details of the WSJ data set. In Section 3, we examine the question whether expectations are formed rationally. Section 4 investigates the expectation formation process and Section 5 compares the specific characteristics of the expectation formation process in the dollar/euro and the yen/dollar market. In Section 6, we summarize our findings and conclude.

2. The WSJ data set

The WSJ regularly conducts a survey among financial market participants about their forecasts of several financial variables for a 6-month horizon. The survey is published biannually in the beginning of January and July. When the survey was launched in 1981, the focus was on the expected development of the prime rate. Over time, the number of economic variables covered by the survey increased considerably.² Two changes in the survey are of particular interest for our analysis. First, since 1989, the survey includes a 6-month forecast for the yen/dollar exchange rate. Second, in mid-1999, the WSJ added a 6-month forecast for the dollar/euro exchange rate. While the survey was initially limited to 12 participants, it gradually increased to a maximum of 64 participants in January 1996 and has been very stable around 55 participants since 1997.

The WSJ data set has already been used in some other studies. However, these studies focus on questions different than our analysis. For example, Greer (2003) examines the accuracy of the 1-year forecast of the 30-year U.S. Treasury bond. The analysis concentrates on the question of whether economists can predict the direction of change correctly and finds some evidence that this is indeed the case. Cho and Hersch (1998) analyze whether the characteristics of forecasters contribute to the forecast accuracy (i.e., the size of error) and/or the forecast bias (i.e., the sign of the error). While the authors do not find that the characteristics of the forecasters can explain forecast accuracy, some characteristics like the professional experience of the forecasters with the Federal Reserve System seem to explain the forecast direction error. Kolb and Stekler (1996) test whether a consensus exists among WSJ forecasters. The results suggest the existence of a high degree of heterogeneity so that central moments should not be used as consensus predictions. Eisenbeis et al. (2002) question the methodology used by the WSJ to construct an overall ranking of the polled economists. Since the WSJ ranks the forecasts on the sum of the weighted absolute percentage deviation from the actual realized value of each series, this methodology neglects the correlations among the forecasted variables. Mitchell and Pearce (2007) examine the unbiasedness and forecast accuracy of individual forecasters with respect to their interest rate and exchange rate forecasts. They find that several forecasters produce biased forecasts and most forecasters cannot out-predict a random walk model.

Our study focuses on the expectation formation process in the foreign exchange market, uses the semiannual forecasts of the WSJ data set and compares the forecasts for the dollar/euro and the yen/dollar exchange rate. As the former exchange rate has been included in the survey only since

¹ The foreign exchange forecasters cannot be regarded as foreign exchange traders. However, they frequently work as economists in commercial and investment banks, economic consultancies and universities.

² For example, survey participants have also been asked to forecast the GNP growth rate since 1985 and the GDP growth rate since 1991. Inflation and unemployment rates have been incorporated into the survey since 1989. Additionally, since 2002 the WSJ has published forecasts of the Federal Funds Rate.

متن کامل مقاله

دریافت فوری ←

ISIArticles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات