UNIVERSITÄT PASSAU
Wirtschaftswissenschaftliche Fakultät

Chapter #6 and #7

Summer term 2020

Estimating the UIP

$$(1+i) = (1+i_a)\frac{w^e_{+1}}{w} \qquad w^e_{+1} = E(w_{+1})$$

ln

$$\ln(1+i) = \ln(1+i_a) + \ln(w_{+1}) - \ln(w)$$

$$\ln(1+x) \approx x$$

assumption: correct exp | w_{+1} unbiased estimator

$$w_{+1} = w^e_{+1} + u_{+1}$$

$$\ln(w_{+1}) - \ln(w) = i - i_a$$

$$= \underset{0}{\alpha} + \underset{1}{\beta}(i - i_a) + \varepsilon$$

managed floating

1. risk premia for f_{+1}
2. ~~Peso problem~~
3. Bubbles
4. Learning
5. endogeneity

w^e

Peso Problem

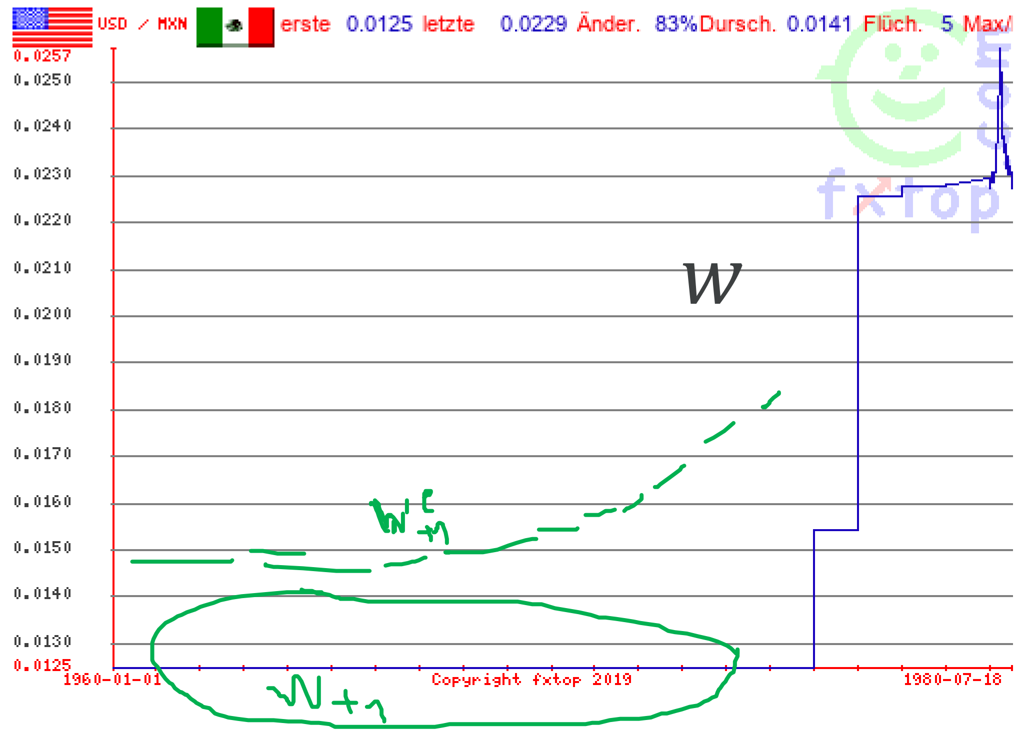
Mexiko $i > i_a$

but $w_{+1} = w$

Correct expectations

$$w^e_{+1} = p w^{flex} + (1-p) w^{fix}$$

10%   90%



But time frame is too short

$$w^e_{+1} \neq w_{+1}$$

w_{+1} is a biased estimator for w^e_{+1}

Problem 8.2

dom. €

$i = 3.6\%$ $\quad i_a = 4.8\%$

a) $\ln(w_{+1}) - \ln(w) = i - i_a = \underline{-1.2\%}$

UP: $w \downarrow$ by $\approx 1.2\%$