

# Exchange Rate Predictability Using Combined Forecasts

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## **ABSTRACT**

This paper examines the short-horizon exchange rate predictability of combined forecasts using data for the G10 currencies relative the US dollar. We begin by reviewing widely-used empirical exchange rate models: the random walk, uncovered interest parity, purchasing power parity, monetary fundamentals, and symmetric and asymmetric Taylor rule. We then construct combined forecasts using statistical and economic model averaging methods. We examine economic value of the out-of-sample forecasting power of the combined forecasts by evaluating the performance of these models using monthly FX excess returns on nine US dollar exchange rates. We find that the most recently best MSE(k) and the discounted SR combined forecasts outperform the driftless random walk model.