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## The Impact of Uncertainty on Professional Exchange Rate Forecasts

Joscha Beckmann, Robert Czudaj

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## The Impact of Uncertainty on Professional Exchange Rate Forecasts

Joscha Beckmann\*

Robert Czudaj†

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**Abstract**

This paper analyzes the role of uncertainty on both exchange rate expectations and forecast errors of professionals for four major currencies based on survey data provided by FX4casts. We consider economic policy, macroeconomic, and financial uncertainty as well as disagreement among CPI inflation forecasters to account for different dimensions of uncertainty. Based on a Bayesian VAR approach, we observe that uncertainty effects on forecast errors of professionals turn out to be more significant compared to the adjustment of exchange rate expectations. Our findings are robust to different forecasting horizons and point to an unpredictable link between exchange rates and fundamentals. Furthermore, we illustrate the importance of considering common unpredictable components for a large number of variables. We also focus on the post-crisis period and the relationship between uncertainty and disagreement among exchange rate forecasters and identify a strong relationship between them.

*Keywords:* Bayesian VAR, Exchange rates, Expectations, Forecast, Uncertainty

*JEL classification:* F31, F37

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\*Ruhr University of Bochum, Chair for International Economics, D-44801 Bochum, e-mail: joscha.beckmann@rub.de, University of Duisburg-Essen, Department of Economics, Chair for Macroeconomics, D-45117 Essen and Kiel Institute for the World Economy, Hindenburgufer 66, D-24105 Kiel.

†Chemnitz University of Technology, Department of Economics, Chair for Empirical Economics, D-09126 Chemnitz, e-mail: robert-lukas.czudaj@wirtschaft.tu-chemnitz.de, phone: (0049)-371-531-31323, fax: (0049)-371-531-831323 and FOM Hochschule für Oekonomie & Management, University of Applied Sciences, Herkulesstr. 32, D-45127 Essen.

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