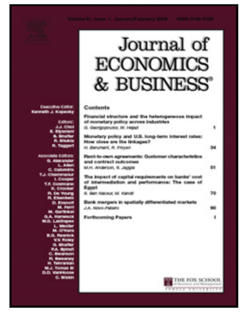
Accepted Manuscript



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PII: S0148-6195(16)00015-1
DOI: http://dx.doi.org/doi:10.1016/j.jeconbus.2016.02.005
Reference: JEB 5740

To appear in: *Journal of Economics and Business*

Received date: 20-5-2015
Revised date: 6-2-2016
Accepted date: 11-2-2016

Monetary policy regimes and the forward bias for foreign exchange *

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February 16, 2016

Abstract

This paper provides a theoretical discussion of the forward premium anomaly. We reformulate the well-known Lucas (1982) model by allowing for the existence of monetary policy regimes. The monetary supply is viewed as having two stochastic components: a) a persistent component that reflects the preferences of the central bank regarding the long-run money supply or inflation target, and b) a transitory component that represents short-lived interventions. To generate agents' forecasts, we consider two scenarios: a) consumers can distinguish the permanent and the transitory components of the money supply (complete information), and b) consumers face a signal-extraction problem to disentangle permanent and transitory components of the money supply (incomplete information). We simulate the model from a careful estimate of the parameters involved

*The authors wish to thank O. Jordà, A.M. Taylor, A. Novales, seminar participants at UC Davis, XVII Finance Forum and the 4th CSDA International Conference on Computational and Financial Econometrics for helpful comments and suggestions. Financial support from the Spanish Ministry of Education through the ECO2012-31941 grant, the Fundación Ramon Areces through its program of economics research grants, the Valencian Regional Government through the PrometeoII/2013/015 grant and the University Jaume I through the P1.1A2012-09 grant is gratefully acknowledged. The usual disclaimer applies.

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