Low-Frequency Movements of Exchange Rates

by Pau Rabanal & Juan Rubio-Ramirez

Discussion by Dave Backus
International Workshop | Atlanta Fed | November 30, 2012
Two good questions

What **frequencies** do we care about in business-cycle research?

- Traditional answer: Hodrick-Prescott filter
- Their answer: in principle, all of them

Where do **real exchange rates** come from?

- Traditional answer: who knows, maybe something nominal?
- Their answer: persistent differences in productivity
Frequencies
Net exports (a traumatic memory)
Real exchange rate

![Graph showing the log of real exchange rate from 1980 to 2012 with data points at regular intervals and a trend line]

- Frequencies
- Real exchange rate
- Log of Real Exchange Rate
- Dave Backus (NYU)
- Rabanal & Rubio-Ramirez
- November 28, 2012
Cross-correlations of GDP and consumption growth
Cross-correlation functions

![Graph showing cross-correlation functions]

- Cross-correlation
- Raw data
- HP filtered

Lag $k$ of TOT behind NX

Dave Backus (NYU)  Rabanal & Rubio-Ramirez  November 28, 2012
Real Exchange Rates
Where do real exchange rates come from?

What we (think we) know

- Real and nominal roughly the same
- Uncorrelated with pretty much everything
- More variable in floating regimes (nominal trigger?)

Rabanal & Rubio-Ramirez

- Persistent differences in productivity
- Variation in Pareto weights via incomplete markets

Things to think about

- Comovements? with what?
- Quantitative significance of incomplete markets?
- Similar to recursive preferences? other mechanisms?
Last thoughts

Two good ideas

- Look at fluctuations by frequency
- Explore sources of real exchange rate movements

Open questions

- Comovements: which ones? can we reproduce them?
- Pareto weights: how important? comparison with other mechanisms?