EXCHANGE RATES AND MONETARY FUNDAMENTALS: A LONG-RUN ANALYSIS IN THE PRESENCE OF STRUCTURAL BREAKS

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ABSTRACT

In this paper, we aim to examine the flexible-price monetary model on the Turkish Lira/US Dollar and Turkish Lira/Euro covering the post floating and managed floating exchange rates period from 2001 to 2015. In our model, the association interest in between exchange rates and relative monetary fundamentals including relative money supply, relative output, and relative long-term interest rate. In order to estimate this model, we use Johansen et al. (2000) cointegration procedure which allows for the existence of structural breaks in long-run relationships. According to preliminary results of the analysis, there are three cointegrating vectors in both models for Turkish Lira/US Dollar and Turkish Lira/Euro exchange rates. Additionally, it can be said that some popular monetary restrictions were rejected in both models.

Key Words: Exchange rates, monetary fundamentals, cointegration, structural breaks.