

Mathematical Statistics Stockholm University Bachelor Thesis **2017:13** http://www.math.su.se

## Real currency exchange rate prediction.A time series analysis.

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June 2017

## Abstract

The foreign exchange market is the largest financial market in the world and forecasting exchange rates are not solely an important task for investors, but also for policy makers. Since market participant do not have access to future information, they try to model the exchange rate by past information. In this thesis an ARIMA(1,1,0) and a VAR(1) model with the trade balance in the EU and the interest rate differential as additional variables are evaluated in a forecasting purpose. It is concluded that a VAR(1) generates the most accurate forecasts during a 1-month horizon, while the ARIMA(1,1,0) is the more suitable model during a 3-month horizon. Both model outperforms a random walk, which usually is considered to produce the most accurate forecasts.

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