Common and idiosyncratic movements in Latin-American exchange rates

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Authors:
Fredy Alejandro Gamboa-Estrada,
José Vicente Romero-Chamorro
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We propose a simple theoretical and empirical approach to differentiate between common and idiosyncratic exchange rate movements in 5 Latin-American economies: Brazil, Chile, Colombia, Mexico, and Peru. Our approach allows us to distinguish the effects of a regional exchange rate common factor and macroeconomic fundamentals differentials on exchange rates. The methodology and estimation strategy are suitable for both low- and high-frequency settings. We provide evidence that the regional common factor is important to assess the dynamics of the Latin-American exchange rates. In our estimations, the relation between exchange rates and the common factor is contemporaneous and stable during the studied period.