Internet Appendix to

Forward-Looking Policy Rules and Currency Premia

A.1. White (2000) Reality Check

We test the null hypothesis that the Taylor rule strategies do not outperform the benchmark model by following the Politis and Romano (1994) stationary bootstrap method. Specifically, the method follows the steps below:

Step 1. We resample the excess returns of each strategy ($k = 1,2$) for B=10,000 times with the optimal block length and denote the resulting returns as $R^*_{k,t}$.

Step 2. For each bootstrap iteration b=1,..,B, we compute the average excess return $\bar{R}^*_{k,b}$ of each strategy k.

Step 3. We construct the empirical null distribution for the test statistic as: $\bar{V} = \max_{k=1,2}\{\sqrt{N}(\bar{R}_k)\}$ and $\bar{V}^*_b = \max_{k=1,2} \sqrt{N}(\bar{R}^*_{k,b} - R^*_k)\, , b = 1, .. B$.

Step 4. The White's *p-value* is obtained based on the comparison of $\bar{V}$ to the quantiles of $\bar{V}^*_b$.

In a similar fashion we estimate the White's *p-value* for the Sharpe ratio and Jensen's alpha of the strategies.

A.2. Other Determinants of Currency Premia

In this section, we define alternative factors that drive the cross-section of currency returns such as global volatility, global illiquidity, global risk aversion and global political risk.

Global FX Volatility and Illiquidity. Our definition of global currency volatility (σ_t^{FX}) and global illiquidity (δ_t^{FX}) follow Menkhoff et al. (2012a). Specifically, we measure global FX volatility based on the cross-sectional average of individual daily absolute exchange rate returns that are averages each month.

$$\sigma_t^{FX} = \frac{1}{T_t} \sum_{d \in T_t} \left[\sum_{k \in K_d} \frac{|\Delta s_d|}{K_d} \right]$$

$$\delta_t^{FX} = \frac{1}{T_t} \sum_{d \in T_t} \left[\sum_{k \in K_d} \frac{BAS_d^k}{K_d} \right]$$

where $|\Delta s_d|$ (BAS_d^k) denotes the absolute value of the change in the log spot exchange rate (bid-ask spreads in percentage points) of currency k on day d. T_t represents the total number of days in month t and K_d is the size of the cross-section on day d. Thus, an increase of the variables would indicate and increase in global volatility or illiquidity. The measures are replaced by innovation from an AR(1) model so as to guard against their persistence and we denote them as VOL and ILLIQ respectively.

Global Risk Aversion. We follow Mueller et al. (2017) who show that global FX correlation (γ_t^{FX}) is able to capture the cross-section of currency returns and it can serve as a good proxy for global risk aversion.

$$\gamma_t^{FX} = \frac{1}{N_t^{Comb}} \sum_{i=1}^{n_t} \left[\sum_{j>1} RC_t^{ij} \right],$$

where RC_t^{ij} represents the realised correlation between currencies i and j at time t. N_t^{Comb} is the total number of combinations of currencies (i, j) at time t and n_t is the total number of currencies in our sample at time t. In order to control for the persistence of variable we replace the measure with the innovations from an autoregressive model with one lag and denote it as CORR.

Global Political Risk. We follow Filippou et al. (2018) who show that global FX correlation (γ_t^{FX}) is able to capture the cross-section of currency momentum returns.

$$PR_t = \frac{1}{n_t} \sum_{i=1}^{n_t} \frac{pr_{i,t} - pr_{US,t}}{\sigma_{i,t}^{PR}}$$

where n_t denotes the total number of available currencies at time t and $pr_{i,t}$ ($pr_{US,t}$) is the time t foreign (U.S.) measure of political risk. $\sigma_{i,t}^{PR}$ represents the cross-sectional average of the time t absolute deviation of the foreign (*i*) political risk from the U.S. counterpart. The dataset is obtained from ICRG and span the period of 1999:01 to 2014:01. As before, we replace the measure with its AR(1) innovations so as to control for its high persistence and denote it as GPRUS. We also consider a similar measure that does not include the U.S. political risk and we denote it as GPR.

A.3. Robustness and Other Specification Tests

A.3.1. Portfolio Holdings

Figure A8 shows the constituents of our policy rule portfolios and the frequency of their appearance in the low and high implied interest rate portfolios. More precisely, we consider Taylor rule specifications with vintages of unemployment gap (graph a) and detrended industrial production (graph b). The top graphs show results for the low interest rate Taylor rule signals while the bottom graphs display results for high interest signals. We find that portfolios with relatively lower values of the signal comprise countries such as Japan, Czech Republic, Switzerland, Sweden and Norway. In Portfolio 5 we observe that currencies with relatively high interest rates tend to appear more often than other currencies and, in particular, Mexico, Australia, the United Kingdom, Switzerland, New Zealand and Hungary exhibit frequencies that range from 20% to more than 40%. Interestingly, the dominant currency in Portfolio 1 is Japan, which appears in the portfolios with low interest rate currencies while we find that in Portfolio 5 the United Kingdom, Australia and Mexico tend to appear more often as they demonstrate higher implied interest rates.

Our policy signals are constructed in such a way that they control for the information embedded in interest rates. This is verified by the low correlations of the Taylor rule portfolios with carry trade portfolios reported in Table 2. Another way to examine the connection between the carry trade activity and our forward-looking Taylor portfolios is to investigate the frequency of currencies in portfolios of funding and investment currencies and associate them with the set of currencies that appear in the policy rule portfolios. Graph c of Figure A8 shows the frequency of portfolios of currencies with low and high interest rate differentials (e.g., carry trade portfolios). We find that the constituents of carry trade portfolios are very different to those appear in policy portfolios. Specifically, we find that Japan and Switzerland are the dominant low interest rate countries but the low policy signals exhibit more dispersion across countries and currencies such as the Swiss Franc tend to be silent. On the other hand, Australia and New Zealand as well as a few emerging economies are the major high interest rate currencies while high policy rule signals tend to load also on emerging economies that are more prone to inflation surprises.

A.3.2. Post-Publication Performance

Regarding the role of mispricing, investors could have biased expectations about the true value of the exchange rate and the Taylor rule variable could be correlated with these errors. Under this notion, when investors update their beliefs based on the arrival of new information, there is a correction in prices which leads to currency return predictability. To examine this issue, we adapted the approach of McLean and Pontiff's (2016) novel equity market analysis.[1] In this paper, the authors investigate whether investors in the equity market learn about mispricing from academic publications on equity pricing. Specifically, they synthesize information for characteristics shown to predict cross-sectional stock returns in peer-reviewed finance, accounting,

[1] In the foreign exchange literature, Bartram, Djuranovik and Garratt (2021) has a similar methodology for many anomalies in the foreign exchange market.

and economics academic journals and test whether there is a shift in equity return predictability after the publication of the articles in question, and do indeed show that the returns to a large number of strategies decline after publication, providing evidence of mispricing prior to publication. To examine whether there was a similar effect of learning about mispricing in the foreign exchange market in terms of Taylor rules, we checked for a decline in profitability of our Taylor rule strategy following the publication of the seminal articles of Taylor (1993) and Henderson and McKibbin (1993) in December 1993, using both revised data and real-time data. Our results are very strong for both datasets. Specifically, we see in Table 1, Table 3, Table 4 and Figure 1 that the returns of our portfolios do not decrease significantly post publication using either revised or real-time data. This suggests that the returns are due to a required compensation for risk rather than mispricing.

We also verify these results in Table A15 where we run a contemporaneous regression of the spread portfolio of the Taylor rule strategy on a dummy variable (I_{Post}) that takes a value of 1 after the publication of the Taylor and Henderson-McKibbin papers in December 1993 and zero otherwise. We also control for the dollar factor. Specifically, the model takes the form:

$$HML_{TR,t} = \alpha + \beta_{Post-Publication} I_{Post,t} + DOL_t + \epsilon_t, \text{ where } TR = FTRu, FTRy.$$

Table A15 shows the coefficients and *t*-statistics of the model for a model that includes only the dummy variable as well as a model that includes the dollar factor. We find a positive coefficient that is significant for the Taylor rule that includes unemployment gap and inisgnificant for the coefficient for industrial production. In any case, we find that there is an increase or no significant change in the returns after publication. These results are also robust when we control for the dollar factor. Our results indicate that investors require a compensation for the risk that they are taking on when investing in this strategy.

One could argue that other academic papers that were published after 1993 might have had have a stronger impact in terms of bringing attention to the seminal contributions of Taylor (1993) and Henderson and McKibbin (1993), and thus that investors realized the importance of Taylor rules for the cross-section of currency returns at a later date.[2] For this reason, in Figure A4 we estimate the above equation in a dynamic setting in order to consider future publications that may be equally important in shaping the expectations of the investors. Specifically, we report *t*-statistics of regressions every month starting from December 1993 of spread portfolios on a dummy variable that takes a value of one the month after the current month until the end of the sample, and zero otherwise. For example, the first *t*-statistic in December 1993 corresponds to a regression of a Taylor rule strategy on a dummy that takes a value of 1 in January 1994 until the end of the sample and zero otherwise. In this way, we consider subsequent publications such as the work of Clarida et al. (1999). We also report the annualized volatility of the Taylor rule strategy for the post-publication period in Figure A4 and find that the *t*-statistics follow the volatility of the measure which reinforces the argument that risk is a key driver of the payoffs of Taylor rule strategy.[3]

A.3.3. Data-Snooping Tests

One concern regarding our trading strategy could be that the reported returns are subject to data snooping (i.e. the documented returns are an artefact of chance error) and so they are spurious. In

[2] Figure A3 shows the citations of each paper over time.
[3] We find a similar pattern in alphas and returns of the strategy in Figure A6 and Figure A7. Figure A5 shows similar results for a model that includes the dollar factor.

other words, the performance of the Taylor rule strategy could be sample-specific and might behave differently in periods that predate or follow our sample-period. Our study considers both revised and vintage data so as to ensure data availability at the time of rebalancing but it ignores potential changes in the performance of the strategy for larger samples. To this end, we perform White's (2000) reality check using a stationary bootstrap of Politis and Romano (1994) so as to guard against this issue.

We evaluate the performance of the strategies based on their mean excess returns of the spread portfolio (e.g., HML_{FTRuv} and HML_{FTRyv}), the corresponding Sharpe ratios (e.g., SR) and Jensen's alpha. The Jensen's alpha is obtained from the projection of the currency excess return of each strategy (e.g., HML_{FTRuv} and HML_{FTRyv}) on the U.S. stock market excess return (i.e. CAPM) which is defined as the stock market return (i.e. r_m) reduced by the risk-free rate (i.e. r_f).[4] Our goal is to examine whether the Taylor rule strategies outperform a benchmark model after accounting for data-snooping. To this end, our null hypotheses to be tested is that the best performing strategy does not perform better than the benchmark.[5] Our bootstrap procedure follows Politis and Romano (1994). Table A7 displays average excess returns, Sharpe ratio and Jensen's alpha for the best performing strategy. We also report nominal *p-values* for mean currency excess returns, Sharpe ratio and Jensen's alpha as well as *p-values* that guard against data-snooping (e.g., Sullivan, Timmermann and White, 1999; White, 2000), which are estimated based on 10,000 bootstrap iterations. We find that the Taylor rule which includes detrended industrial production is the best performing strategy. In addition, we show that none of the White *p-values* exceed the significance level of 5%, indicating that there is evidence of profitability

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[4] The dataset is obtained from Kenneth French's webpage.

[5] i.e. $H_0: \max_{k=FTRuv,FTRip} M_k \leq 0, where\ M = HML, SR, alpha$. Table A7 evaluates the behaviour of each strategy separately.

even after controlling for data snooping as the null hypothesis of no outperformance is always rejected for all performance measures at standard significance levels. The results are also robust to the consideration of transaction costs.

A.3.4. Alternative Measures of Output Gap

HP filter. In our main analysis we estimate the cyclical component of output gap following the approach of Hodrick and Prescott (1980, 1997). Specifically, the filter is obtained by solving the minimization problem below:

$$\min_{\tau} \sum_{t=1}^{T} (y_{i,t} - \tau_{i,t})^2 + \lambda \sum_{t=2}^{T-1} [(\tau_{i,t+1} - \tau_{i,t}) - (\tau_{i,t} - \tau_{i,t-1})]^2$$

where $y_{i,t}$ is the logarithm of the industrial production and $\tau_{i,t}$ is the trend component for country *i* at time *t*. The smoothing parameter λ reflects the association of the trend component with the raw series. For example, a value of zero of the smoothing parameter would imply that $y_{i,t} = \tau_{i,t}$ for every value *t*. We set the smoothing parameter equal to 1600 for quarterly data and 14400 for monthly data (e.g., Hodrick and Prescott, 1980, 1997; Kydland and Prescott, 1990). Thus, the cyclical component is defined as $c_{i,t} = y_{i,t} - \tau_{i,t}$.

Baxter-King Filter. Specifically, we employ the Baxter-King filter which is a more band-pass filter that eliminates low and high frequency components from time-series by applying a finite moving average to the time-series of the output measure as follows: $\hat{y}_{i,t} = \sum_{h=-K}^{K} B_{i,h} y_{i,t-h}$, where the weights $B_{i,h}$ can be obtained from the inverse Fourier transformation of the frequency response function and the number of nodes (K) take the value of 12 for quarterly data and 36 for monthly data. Baxter and King (1999) propose a band-pass filter with cut-off points at 1/32 and 1/6 for quarterly as well as 8 and 96 for monthly series.

Linear Projection. Following the approach of Hamilton (2018), who argues that the HP filter could generate spurious dynamics, we regress the logarithm of industrial production on at time *t* on 12 (4) lags of monthly (quarterly) log output of the measure with an horizon of 2 years. For example, for monthly data the model is as follows: $y_{i,t} = \alpha_i + \sum_{j=0}^{11} \beta_{i,j} y_{i,t-24-j} + \varepsilon_{i,t}$. Thus, the cyclical component of country *i* at time *t* is measured as $c_{i,t} = y_{i,t} - \hat{y}_{i,t}$.

Quadratic Deterministic Trend. We also consider a quadratic time trend as an alternative way of obtaining the output gap. Specifically, we regress the log of industrial production on a time trend and its squared form: $y_{i,t} = \alpha_i + \gamma_i t + \delta_i t^2 + \epsilon_t$. Thus, the cyclical component of country *i* at time *t* is measured as $c_{i,t} = y_{i,t} - \hat{y}_{i,t}$.

Table A1. Inflation Targets

This table reports inflation Targets of each country in our sample. We consider the targets for the whole data period. The data span the period of 1990.01-2017.03.

Inflation Targets	
	Targets
Australia	2.00
Brazil	3.25
Canada	2.00
Czech Republic	3.50
Europe	2.00
Germany	2.00
Hungary	3.50
Indonesia	4.00
Japan	2.00
Korea, South	3.00
Mexico	3.00
New Zealand	1.50 from 1990.01-2002.09 2.00 from 2002.10-2017.03
Norway	2.50
Philippines	5.00
Poland	3.00
Spain	2.00
Sweden	2.00
Switzerland	1.00
Thailand	1.75
United Kingdom	2.50 from 1990.01-2003.12 2.00 from 2004.01-2017.03
United States	2.00

Table A2. Descriptive Statistics of Taylor Rule Portfolios: *Sub-Samples*

This table reports descriptive statistics of payoffs to Taylor rule strategy using vintage data before and after the recent Financial Crisis. *Panel A (Panel B)* reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal that incorporates the unemployment rate (industrial production) as a proxy of output gap. In particular, HML_{TR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal for HML_{TRu} considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5u_t^{gap} - \lambda r_t$, where $(\pi_t^f - \pi_t^*)$ denotes the difference between the inflation forecast and the corresponding target and r_t represents the interest rate at time *t*. The signal for HML_{TRy} considers the detrended industrial production (e.g., Hodrick and Prescott, 1980, 1997) as a proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5y_t^{gap} - \lambda r_t$, at time *t*. We also report payoffs that are estimated in the presence of transaction costs (e.g., HML_{TR}^{TC}) and the portfolios are rebalanced on a monthly basis. Finally, the mean, standard deviation and Sharpe Ratio are annualized (the means are multiplied by 12 and the standard deviation by $\sqrt{12}$) and expressed in percentage points. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1999:02-2017:03.

	Panel A: Unemployment			
	$HML_{FTRuv}^{before\ 2007}$	$HML_{FTRuv}^{after\ 2007}$	$HML_{DFTRuv}^{before\ 2007}$	$HML_{DFTRuv}^{after\ 2007}$
Mean	10.39***	2.24	4.29	7.16***
Std. Dev.	7.37	7.70	7.77	7.92
SR	1.41	0.29	0.55	0.90
Skew	0.15	0.65	-0.14	0.81
Kurt	3.71	3.47	2.39	4.34
AC(1)	0.01	0.03	0.18	0.07
p-value	0.89	0.73	0.00	0.47
	Panel B: Industrial Production			
	$HML_{FTRyv}^{before\ 2007}$	$HML_{FTRyv}^{after\ 2007}$	$HML_{DFTRyv}^{before\ 2007}$	$HML_{DFTRyv}^{after\ 2007}$
Mean	10.26***	5.60**	5.50**	7.50***
Std. Dev.	6.39	8.96	7.21	8.86
SR	1.61	0.63	0.76	0.85
Skew	0.65	0.32	0.24	0.53
Kurt	5.42	5.93	2.77	4.06
AC(1)	0.06	-0.08	-0.07	0.03
p-value	0.56	0.40	0.00	0.77

Table A3. Dynamic Taylor Rule Models: *Transaction Costs*

This table reports descriptive statistics of payoffs to Taylor rule strategy. *Panel A* reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal for the full sample and *Panel B* report the corresponding summary statistics for the period 1990:01-2007:12. In particular, HML_{DFTR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.50u_t^{gap} - \lambda r_t$, where $(\pi_t^f - \pi_t^*)$ denotes the difference between the inflation forecast and the corresponding target and r_t represents the interest rate at time *t*. The portfolios are rebalanced on a monthly basis. All portfolios take into consideration the implementation cost of the strategy. Finally, the mean, standard deviation and Sharpe Ratio are annualized (the means are multiplied by 12 and the standard deviation by $\sqrt{12}$) and expressed in percentage points. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1990:01-2017:03 for revised data and the period 1999:02-2017:03.

Panel A: Unemployment							
	P_1	P_2	P_3	P_4	P_5	HML_{DFTRu}	HML_{DFTRuv}
Mean	-1.58	0.88	-0.34	-0.30	6.55	8.13***	4.35**
Std. Dev.	9.09	8.69	8.69	9.17	9.60	8.80	7.86
SR	-0.17	0.10	-0.04	-0.03	0.68	0.92	0.55
Skew	-1.13	-0.68	-0.30	-0.30	-0.22	0.30	0.45
Kurt	6.58	6.01	4.51	4.48	3.39	3.57	3.66
AC(1)	0.12	0.09	-0.04	0.02	0.35	0.34	0.13
p-value	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Panel B: Industrial Production							
	P_1	P_2	P_3	P_4	P_5	HML_{DFTRy}	HML_{DFTRyv}
Mean	-0.84	0.73	-0.61	0.13	6.13	6.97**	4.95**
Std. Dev.	8.93	8.75	8.75	8.89	9.64	8.62	8.21
SR	-0.09	0.08	-0.07	0.01	0.64	0.81	0.60
Skew	-0.92	-0.59	-0.48	-0.29	-0.15	0.32	0.48
Kurt	5.62	5.52	4.42	4.55	3.38	3.29	3.91
AC(1)	0.13	0.05	0.00	0.04	0.36	0.35	0.01
p-value	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Table A4. Asset Pricing Tests: Taylor Rule and Combo

This table reports asset pricing results for three-factor models that comprise the DOL and forward-looking Taylor rule factors as well as a combo risk factor. We define the combo portfolios as a spread portfolio of currencies that are sorted based on the sum of the signals of inflation and output gap. We use as test assets six currency portfolios sorted based on past forward-looking Taylor rule signals. Particularly, we consider the specification of the Taylor rule signal which includes unemployment gap or detrended output gap. We rebalance our portfolios on a monthly basis. We report Fama and MacBeth (1973) estimates factor prices of risk (λ). We also display Newey and West (1987) *t*-statistics (in squared brackets) or *p-values* (in parenthesis) corrected for autocorrelation and heteroskedasticity with optimal lag selection and SH are the corresponding values of Shanken (1992). The table also shows χ^2, cross-sectional R^2, HJ distance following Hansen and Jagannathan (1997). We do not control for transaction costs and excess returns are expressed in percentage points. The data are collected from Datastream via Barclays and Reuters. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level based on Shanken (1992) standard errors. The data contain monthly series for the period 1999:02-2017:03.

Factor Prices							
	λ_{DOL}	λ_{COMBO}	$\lambda_{HML_{FTRy}}$	χ^2_{NW}	χ^2_{SH}	R^2	HJ
				Unemployment			
$COMBO_u$	0.00	0.00	0.00**	7.64	7.27	0.91	0.05
NW	[0.40]	[0.03]	[2.53]	(0.18)	(0.20)		(0.66)
SH	[0.40]	[0.03]	[2.51]				
				Industrial Production			
$COMBO_y$	0.00	0.02	0.01**	9.52	8.68	0.96	0.11
NW	[0.51]	[1.91]	[3.61]	(0.09)	(0.12)		(0.10)
SH	[0.51]	[1.58]	[3.56]				

Table A5. Robustness: Asset Pricing Tests

This table reports asset pricing results for a two-factor model that comprises that DOL and the Taylor rule risk factors and other risk factors (e.g., carry trade, momentum and value strategies). We use as test assets 36 test assets (TA) that include carry trade, momentum, value, output gap, inflation portfolios and Taylor rule portfolios. Our set of test assets also includes risk factors (e.g., carry trade, momentum, value and Taylor rule portfolios). Particularly, we consider the specification of the Taylor rule signal which includes unemployment (HML_{FTRuv}) and industrial production (HML_{FTRuv}) as a proxy for output gap. We rebalance our portfolios on a monthly basis. This table reports asset pricing results for a number of FX asset pricing models when considering a large number of test assets comprising carry, momentum and value strategies at the same time. We report Gibbons et al. (1989) (GRS) test statistics and the corresponding *p-values*. We also offer GLS R^2 We display *p-values* in parenthesis. The data contain monthly series for the period 1999:02-2017:03.

	GRS Statistic	
	TA = $[PORT_{FTR},\ PORT_{CAR}, PORT_{MOM},\ PORT_{VAL}, PORT_{GAP}, PORT_{INF}\ ]$	GLS R^2
F = [DOL HML_{FTRuv}]	5.45	0.13
	0.00	
F = [DOL HML_{FTRyv}]	5.23	0.15
	0.00	
F = [DOL CAR]	5.30	0.14
	0.00	
F = [DOL MOM]	5.94	0.00
	0.00	
F = [DOL VAL]	6.04	0.04
	0.00	
F = [DOL GAP]	5.85	0.02
	0.00	
F = [DOL INF]	5.97	0.00
	0.00	

Table A6. Backward-looking and Forward-looking Taylor Rules

This table reports contemporaneous regressions of forward-looking on backward-looking Taylor rules as well as carry trade portfolios. We show contemporaneous regressions of forward-looking Taylor rules or backward-looking Taylor rule spread portfolios on combo portfolios. The alphas are annualized and expressed in percentage points. We report *t*-statistics in squared brackets and adjusted R-squares ($\bar{R}^2$) The alphas are annualized. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1999:02-2017:03.

Taylor Rules and Combo Portfolios				
	HML_{FTRuv}	HML_{FTRyv}	HML_{BTRuv}	HML_{BTRyv}
α_{COMBO}	5.38***	6.24***	4.21***	4.35***
	[3.31]	[3.48]	[2.91]	[2.59]
β_{COMBO}	0.27***	0.40***	0.37***	0.50***
	[2.89]	[4.77]	[4.23]	[9.53]
$\bar{R}^2$ $(in\,\%)$	11.10%	20.43%	23.14%	32.19%

Table A7. Reality Check

This table displays performance measures of forward-looking Taylor rule strategy using vintage data. We report mean excess returns, Sharpe ratios and Jensen's alpha with nominal *p-values* and *p-values* of White (2000) that control for data snooping. The portfolios are sorted based on the Taylor rule signal that incorporates vintages of the unemployment rate (industrial production) as a proxy of output gap. In particular, HML_{FTR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal for HML_{FTRu} considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5u_t^{gap} - \lambda r_t$, where $(\pi_t^f - \pi_t^*)$ denotes the difference between the inflation forecast and the corresponding target and r_t represents the interest rate at time *t*. The signal for HML_{FTRip} considers the detrended industrial production (e.g., Hodrick and Prescott, 1980, 1997) as a proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5y_t^{gap} - \lambda r_t$, at time *t*. We also report payoffs that are estimated in the presence of transaction costs (e.g., HML_{FTR}^{TC}) and the portfolios are rebalanced on a monthly basis. Finally, the mean, Sharpe Ratio and Jensen's alpha are annualized and expressed in percentage points. The data span the period 1999:02-2017:03.

Taylor Rule Strategies with and without Transaction Costs				
	HML_{FTRuv}	HML_{FTRyv}	HML_{FTRuv}^{TC}	HML_{FTRyv}^{TC}
Mean	6.16	7.87	4.39	5.78
Nominal p-value	0.00	0.00	0.01	0.00
White's p-value	0.00	0.00	0.01	0.01
SR	0.81	1.01	0.58	0.74
Nominal p-value	0.00	0.00	0.01	0.00
White's p-value	0.00	0.00	0.01	0.01
Jensen's Alpha	6.26	8.08	4.48	6.00
Nominal p-value	0.00	0.00	0.01	0.00
White's p-value	0.00	0.00	0.00	0.00

Table A8. Asset Pricing Tests: Taylor Rule Portfolios

This table reports asset pricing results for a two-factor model that comprises the DOL and volatility, illiquidity, correlation, global political risk, U.S. political risk and Taylor rule (denoted by FM) risk factors. We use as test assets six currency portfolios sorted based on past forward-looking Taylor rule signals. Particularly, we consider the specification of the Taylor rule signal which includes unemployment gap (*Panel A*) or detrended output gap (*Panel B*). We rebalance our portfolios on a monthly basis. We report Fama and MacBeth (1973) estimates of factor prices of risk (λ). We also display Newey and West (1987) *t*-statistics (in squared brackets) or *p-values* (in parenthesis) corrected for autocorrelation and heteroskedasticity with optimal lag selection and SH are the corresponding values of Shanken (1992). The table also shows χ^2, cross-sectional R^2, HJ distance following Hansen and Jagannathan (1997). We do not control for transaction costs and excess returns are expressed in percentage points. The data are collected from Datastream via Barclays and Reuters. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level based on Shanken (192) standard errors.   The data contain monthly series for the period 1999:02-2017:03.

Factor Prices													
	$\lambda_{HML_{FTR}}$	λ_{FM}	χ^2_{NW}	χ^2_{SH}	R^2	HJ		$\lambda_{HML_{FTR}}$	λ_{FM}	χ^2_{NW}	χ^2_{SH}	R^2	HJ
	Unemployment							*Industrial Production*					
FM=FVOL	0.01***	0.00	8.72	8.19	0.79	0.16	FM=FVOL	0.01***	0.00	10.79	9.83	0.97	0.21
NW	[3.22]	[-0.52]	(0.12)	(0.15)		(0.03)	NW	[4.25]	[0.74]	(0.06)	(0.08)		(0.00)
SH	[3.21]	[-0.51]					SH	[4.23]	[0.73]				
FM=FILLIQ	0.01***	0.00	10.41	9.47	0.70	0.35	FM=FILLIQ	0.01***	0.00	10.41	9.47	0.74	0.35
NW	[4.05]	[-1.29]	(0.06)	(0.09)		(0.00)	NW	[4.05]	[-1.29]	(0.06)	(0.09)		(0.00)
SH	[4.02]	[-1.26]					SH	[4.02]	[-1.26]				
FM=FCORR	0.01***	0.00	8.76	8.13	0.83	0.21	FM=FCORR	0.01***	0.00	10.75	9.88	0.74	0.39
NW	[3.11]	[0.79]	(0.12)	(0.15)		(0.21)	NW	[3.20]	[0.56]	(0.06)	(0.08)		(0.00)
SH	[3.09]	[0.77]					SH	[3.15]	[0.54]				
FM=FGPR	0.00*	-0.06	7.35	2.88	0.70	0.36	FM=FGPR	0.00	-0.01**	5.08	4.83	0.95	0.38
NW	[2.27]	[-2.01]	(0.20)	(0.72)		(0.00)	NW	[0.91]	[-2.23]	(0.41)	(0.44)		(0.00)
SH	[1.81]	[-1.26]					SH	[0.90]	[-2.21]				
FM= FGPRUS	0.00	-0.07	11.33	2.06	0.60	0.36	FM= FGPRUS	0.00	0.00	11.76	0.99	0.84	0.40
NW	[0.50]	[-1.64]	(0.05)	(0.84)		(0.09)	NW	[0.99]	[-0.35]	(0.04)	(-0.35)		(0.00)
SH	[0.25]	[-0.70]					SH	[0.99]	[-0.35]				

Table A9. Taylor Rule Models: *Tradability*

This table reports descriptive statistics of payoffs to a forward-looking Taylor rule strategy. *Panel A* reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal for the full sample and *Panel B* report the corresponding summary statistics for the period 1990:01-2007:12. In particular, HML_{FTR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.50u_t^{gap} - \lambda r_t$, where $(\pi_t^f - \pi_t^*)$ denotes the difference between the inflation forecast and the corresponding target and r_t represents the interest rate at time *t*. We also report payoffs are estimated in the presence of transaction costs (e.g., HML_{FTR}^{TC}) and the portfolios are rebalanced on a monthly basis. All portfolios take into consideration the implementation cost of the strategy. Finally, the mean, standard deviation and Sharpe Ratio are annualized (the means are multiplied by 12 and the standard deviation by $\sqrt{12}$) and expressed in percentage points. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1990:01-2017:03 for revised data and the period 1999:02-2017:03.

Panel A: Unemployment							
	P_1	P_2	P_3	P_4	P_5	HML_{FTRu}	HML_{FTRu}^{TC}
Mean	-0.60	-0.43	1.82	0.29	6.80	7.40***	5.70**
Std. Dev.	9.83	9.91	9.49	9.32	8.71	9.52	9.52
SR	-0.06	-0.04	0.19	0.03	0.78	0.78	0.60
Skew	-0.90	-0.87	-0.50	-0.93	0.13	0.57	0.55
Kurt	6.28	6.15	5.64	6.80	3.30	4.39	4.35
AC(1)	0.12	0.03	-0.11	0.14	0.00	0.02	0.02
p-value	0.10	0.71	0.11	0.04	0.98	0.76	0.77

Panel B: Industrial Production							
	P_1	P_2	P_3	P_4	P_5	HML_{FTRy}	HML_{FTRyv}^{TC}
Mean	-0.48	0.17	0.30	1.34	7.57	8.06***	6.08**
Std. Dev.	9.55	10.26	9.56	10.09	8.44	10.12	10.08
SR	-0.05	0.02	0.03	0.13	0.90	0.80	0.60
Skew	-0.69	-0.83	-0.41	-0.89	-0.33	0.04	0.02
Kurt	5.73	5.78	3.86	8.14	5.78	4.74	4.74
AC(1)	0.13	-0.02	0.00	0.11	0.02	0.03	0.02
p-value	0.06	0.74	0.00	0.12	0.77	0.72	0.81

Table A10. Descriptive Statistics of Taylor Rule Portfolios: *Foreign Investors*

This table reports descriptive statistics of payoffs to Taylor rule strategy using vintage data and taking the perspective of foreign investors. The table reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal that incorporates the unemployment rate (industrial production) as a proxy of output gap. In particular, HML_{TR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). We take the perspective of the British (*Panel A*), Japanese (*Panel B*), Swiss (*Panel C*), Canadian (*Panel D*) and Australian (*Panel E*) investor. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1999:02-2017:03.

Panel A: British Investor

	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}		P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}
Mean	-1.63	-0.81	1.44	1.49	7.14	8.76***	*Mean*	-1.09	-1.39	0.15	1.50	7.07	8.15***
Std. Dev.	8.62	8.63	8.60	8.35	10.59	9.68	*Std. Dev.*	8.45	9.09	8.95	8.80	10.57	9.85
SR	-0.19	-0.09	0.17	0.18	0.67	0.91	*SR*	-0.13	-0.15	0.02	0.17	0.67	0.83
Skew	-0.07	0.80	0.56	0.40	0.12	0.35	*Skew*	0.02	0.28	0.08	0.45	0.35	0.29
Kurt	4.51	6.84	4.97	5.27	5.38	5.71	*Kurt*	4.44	7.50	5.09	4.45	5.95	5.17
AC(1)	-0.08	0.01	-0.01	0.07	0.13	0.26	*AC(1)*	-0.07	-0.05	-0.05	-0.02	0.18	0.24
p-value	0.13	0.80	0.85	0.23	0.02	0.00	*p-value*	0.22	0.36	0.35	0.73	0.00	0.00

Panel B: Japanese Investor

	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}		P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}
Mean	0.11	2.28	2.31	3.61	5.84	5.73***	*Mean*	0.85	2.47	1.46	2.55	8.82	7.97***
Std. Dev.	12.98	13.13	12.37	13.26	12.34	7.47	*Std. Dev.*	12.53	13.19	12.71	12.92	12.44	7.42
SR	0.01	0.17	0.19	0.27	0.47	0.77	*SR*	0.07	0.19	0.12	0.20	0.71	1.07
Skew	-1.43	-1.22	-0.74	-1.26	-0.68	0.43	*Skew*	-1.13	-1.63	-1.46	-0.90	-0.43	0.08
Kurt	8.18	8.76	4.52	7.60	4.65	3.61	*Kurt*	7.68	10.10	8.39	5.95	3.64	6.64
AC(1)	0.12	0.09	0.07	0.12	0.06	0.10	*AC(1)*	0.11	0.04	0.09	0.14	0.10	-0.04
p-value	0.08	0.20	0.29	0.07	0.34	0.14	*p-value*	0.11	0.58	0.21	0.04	0.12	0.60

Panel C: Swiss Investor

	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}		P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}
Mean	-2.70	0.51	0.50	0.87	3.30	5.99***	*Mean*	-1.61	0.06	-0.99	0.89	6.29	7.90***
Std. Dev.	8.59	8.53	8.27	8.24	9.70	7.68	*Std. Dev.*	9.21	8.64	7.59	8.89	9.32	7.62
SR	-0.31	0.06	0.06	0.11	0.34	0.78	*SR*	-0.17	0.01	-0.13	0.10	0.67	1.04
Skew	-1.24	-1.61	-0.87	-1.23	-1.21	0.30	*Skew*	-1.39	-1.25	-1.42	-1.52	-0.83	0.63
Kurt	6.90	9.23	5.50	6.46	9.42	3.67	*Kurt*	8.88	7.19	8.75	7.54	5.05	6.05
AC(1)	-0.09	-0.04	-0.11	-0.01	-0.05	0.06	*AC(1)*	-0.17	-0.06	-0.05	-0.06	0.06	0.07
p-value	0.21	0.51	0.11	0.84	0.45	0.36	*p-value*	0.01	0.34	0.42	0.37	0.35	0.31

Panel D: Canadian Investor

	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}		P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}
Mean	-3.18	0.26	-0.20	0.69	3.47	6.65***	*Mean*	-1.49	-1.41	-0.68	0.50	6.06	7.55***
Std. Dev.	8.68	8.08	8.85	8.07	8.13	7.57	*Std. Dev.*	8.14	9.00	7.95	8.49	8.39	7.72
SR	-0.37	0.03	-0.02	0.09	0.43	0.88	*SR*	-0.18	-0.16	-0.09	0.06	0.72	0.98
Skew	-0.65	0.17	0.57	-0.03	0.42	0.34	*Skew*	-0.40	-0.72	0.30	0.18	0.28	0.24
Kurt	4.99	3.20	5.26	3.56	3.70	3.37	*Kurt*	4.97	6.18	3.11	3.53	4.08	5.82
AC(1)	-0.01	-0.12	-0.17	-0.07	-0.11	0.05	*AC(1)*	-0.12	-0.10	-0.08	-0.11	-0.08	-0.03
p-value	0.83	0.07	0.01	0.31	0.12	0.46	*p-value*	0.09	0.13	0.26	0.10	0.25	0.69

Panel E: Australian Investor

	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}		P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}
Mean	-5.41	-2.51	-3.87	-2.33	1.01	6.41***	*Mean*	-4.31	-2.66	-3.81	-2.71	2.98	7.29***
Std. Dev.	8.24	8.19	9.21	8.38	8.80	7.53	*Std. Dev.*	9.06	8.57	7.98	8.24	8.99	7.66
SR	-0.66	-0.31	-0.42	-0.28	0.11	0.85	*SR*	-0.48	-0.31	-0.48	-0.33	0.33	0.95
Skew	0.06	0.50	0.66	-0.12	0.38	0.19	*Skew*	0.10	0.31	0.26	0.21	0.57	0.32
Kurt	2.93	3.61	4.64	2.73	3.33	3.33	*Kurt*	3.93	3.13	2.98	3.94	5.61	5.43
AC(1)	0.09	-0.04	0.03	0.00	-0.02	0.02	*AC(1)*	-0.12	0.08	-0.07	0.02	0.05	-0.03
p-value	0.20	0.57	0.67	0.98	0.74	0.82	*p-value*	0.08	0.24	0.31	0.79	0.45	0.69

Table A11. Asset Pricing Tests: Taylor Rule and Term Structure Portfolios

This table reports asset pricing results for two-factor models that comprise the DOL and forward-looking Taylor rule factors as well as a combo risk factor. We use as test assets five currency portfolios sorted based on past yield curve slopes which are measured by the difference between the 10-year yield and one-month interest rate. Particularly, we consider the specification of the Taylor rule signal which includes unemployment gap or detrended output gap. We rebalance our portfolios on a monthly basis. We report Fama and MacBeth (1973) estimates factor prices of risk (λ). We also display Newey and West (1987) *t*-statistics (in squared brackets) or *p-values* (in parenthesis) corrected for autocorrelation and heteroskedasticity with optimal lag selection and SH are the corresponding values of Shanken (1992). The table also shows χ^2, cross-sectional R^2, HJ distance following Hansen and Jagannathan (1997). We do not control for transaction costs and excess returns are expressed in percentage points. The data are collected from Datastream via Barclays and Reuters. We include G10 countries. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level based on Shanken (1992) standard errors. The data contain monthly series for the period 1999:02-2015:12.

	λ_{DOL}	$\lambda_{HML_{FTRv}}$	χ^2_{NW}	χ^2_{SH}	R^2	HJ
			Unemployment			
TA= $PORT_{TERM}$	0.18	0.01	8.60	7.53	0.28	0.08
NW	[0.95]	[1.36]	(0.07)	(0.11)		(0.52)
SH	[0.94]	[1.27]				
			Industrial Production			
TA= $PORT_{TERM}$	0.15	0.01**	3.04	2.50	0.90	0.06
NW	[0.80]	[2.19]	(0.55)	(0.64)		(0.68)
SH	[0.79]	[2.00]				

Table A12. Descriptive Statistics of Taylor Rule Portfolios: *Next Year Inflation Forecasts*

This table reports descriptive statistics of payoffs to Taylor rule strategy using vintage data. *Panel A (Panel B)* reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal that incorporates the unemployment rate (industrial production) as a proxy of output gap. In particular, HML_{FTR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal for HML_{FTRu} considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5u_t^{gap} - \lambda r_t$, where $(\pi_t^f - \pi_t^*)$ denotes the difference between the inflation forecast for the following year and the corresponding target and r_t represents the interest rate at time *t*. The signal for HML_{FTRy} considers the detrended industrial production (e.g., Hodrick and Prescott, 1980, 1997) as a proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5y_t^{gap} - \lambda r_t$, at time *t*. We also report payoffs that are estimated in the presence of transaction costs (e.g., HML_{FTR}^{TC}) and the portfolios are rebalanced on a monthly basis. Finally, the mean, standard deviation and Sharpe Ratio are annualized (the means are multiplied by 12 and the standard deviation by $\sqrt{12}$) and expressed in percentage points. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1999:02-2017:03.

	Panel A: Unemployment						
	P_1	P_2	P_3	P_4	P_5	HML_{FTRuv}	HML_{FTRuv}^{TC}
Mean	-0.36	-0.27	0.61	2.67	3.45	3.81**	2.02
Std. Dev.	10.43	9.53	9.37	9.58	10.07	7.08	7.09
SR	-0.03	-0.03	0.06	0.28	0.34	0.54	0.28
Skew	-0.88	-0.66	-0.41	-0.46	-0.86	0.44	0.42
Kurt	5.72	4.86	4.10	4.86	5.70	4.04	3.99
AC(1)	0.10	0.02	0.02	0.14	0.03	0.04	0.04
p-value	0.15	0.75	0.71	0.05	0.64	0.53	0.57
	Panel B: Industrial Production						
	P_1	P_2	P_3	P_4	P_5	HML_{FTRyv}	HML_{FTRyv}^{TC}
Mean	-0.17	0.52	-0.25	2.16	6.00	6.17***	3.99**
Std. Dev.	10.43	9.71	10.00	9.53	9.04	8.19	8.13
SR	-0.02	0.05	-0.03	0.23	0.66	0.75	0.49
Skew	-0.60	-0.50	-1.24	-0.35	-0.71	-0.13	-0.17
Kurt	5.46	4.75	7.51	4.83	5.02	6.92	7.07
AC(1)	0.04	0.11	0.07	0.05	0.04	-0.08	-0.1
p-value	0.57	0.10	0.28	0.50	0.57	0.23	0.16

Table A13. Taylor Rule Portfolios and Mispricing

This table reports coefficients of predictive panel regressions with country fixed effects of analysts' errors on the Taylor rule measures the month before the forecast. The standard errors are clustered by country. We define analysts' errors as the difference between the spot exchange rate forecast and the realized exchange rate. We show results for Taylor rules spread portfolios that are based on revised data of unemployment ($FTRu$) and industrial production ($FTRy$). The data are collected from Datastream via Barclays and Reuters. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level. The data contain monthly series for the period 1990:02-2017:03.

	Analysts' Forecasts	
	$\hat{S}-S$	$\hat{S}-S$
α	0.30***	0.30***
	[5.39]	[4.76]
β_{FTRu}	-2.49	
	[-0.90]	
β_{FTRy}		-3.12
		[-1.00]
FE	Yes	Yes
$\bar{R}^2$ $(in\ \%)$	1.15	1.28

Table A14. Real-Time Taylor Rule Portfolios and Mispricing

This table reports coefficients of predictive panel regressions with country fixed effects of analysts' errors on the Taylor rule measures the month before the forecast. The standard errors are clustered by country. We define analysts' errors as the difference between the spot exchange rate change forecast and the realized exchange rate change (the exchange rate changes have a negative sign). We show results for Taylor rules spread portfolios that are based on vintage data of unemployment ($FTRu$) and industrial production ($FTRy$). The data are collected from Datastream via Barclays and Reuters. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level. The data contain monthly series for the period 1999:02-2017:03.

	Analysts' Forecasts	
	$\widehat{\Delta S} - \Delta S$	$\widehat{\Delta S} - \Delta S$
α	0.46***	0.28***
	[4.50]	[2.73]
β_{FTRu}	9.79	
	[1.09]	
β_{FTRy}		-8.08
		[-0.89]
FE	Yes	Yes
$\bar{R}^2$ $(in\,\%)$	1.11	0.90

Table A15. Taylor Rule Portfolios and Mispricing

This table reports coefficients of contemporaneous regressions of spread Taylor rule portfolios using revised data. Post-Publication is a dummy variable that takes the value of 1 after the publication of the papers of Taylor and Henderson-McKibbin in December 1993. We also control for the dollar factor. We show results for Taylor rules spread portfolios that are based on revised data of unemployment (HML_{FTRu}) and industrial production (HML_{FTRy}). We display Newey and West (1987) *t*-statistics (in squared brackets). The excess returns are expressed in percentage points. The constant is annualized. The standard errors are clustered by country. We define analysts' errors as the difference between the spot exchange rate change forecast and the realized exchange rate change (the exchange rate changes have a negative sign). The data are collected from Datastream via Barclays and Reuters. The superscripts *, **, *** indicate significance of the loadings at the 10%, 5% and 1% level. The data contain monthly series for the period 1990:02-2017:03.

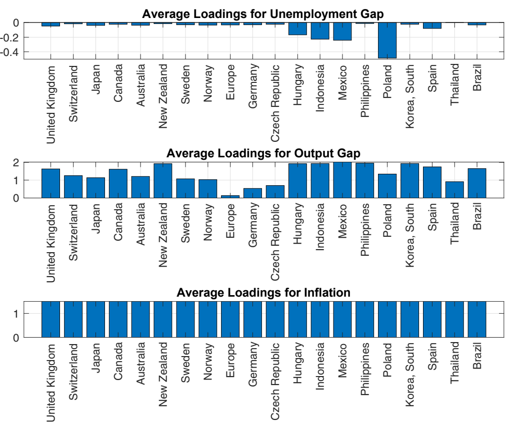
Post-Publication Performance				
	HML_{FTRu}	HML_{FTRu}	HML_{FTRy}	HML_{FTRy}
α	-0.02	-0.02	0.06	0.05
	[-0.34]	[-0.35]	[0.26]	[1.07]
$\beta_{Post-Publication}$	0.01**	0.01**	0.00	0.00
	[2.02]	[1.99]	[0.62]	[0.63]
β_{DOL}		0.12		0.12
		[1.02]		[0.98]
$\bar{R}^2$ $(in\,\%)$	1.26	1.79	-0.17	0.39

Table A16. Backward-looking Taylor Rules

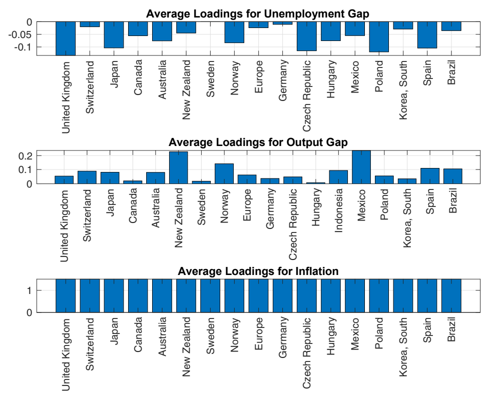
This table reports descriptive statistics of payoffs to backward-looking Taylor rule strategy. *Panel A* reports descriptive statistics for currency excess returns of portfolios sorted based on the Taylor rule signal with unemployment gap and *Panel B* shows the corresponding results for a Taylor rule model with detrended industrial production. In particular, HML_{BTR} denotes the Taylor rule trade strategy that goes long (short) a basket of currencies with highest (lowest) Taylor rule signals (e.g., the surprise element of implied interest rates). The signal considers the unemployment gap (e.g., u_t^{gap}) as proxy of output gap and takes the following form: $\xi_t = 1.5(\pi_t - \pi_t^*) - 0.50u_t^{gap} - \lambda r_t$, where $(\pi_t - \pi_t^*)$ denotes the difference between backward-looking inflation (e.g., the percentage difference of CPI between month t and month t-12) and the corresponding target and r_t represents the interest rate at time *t*. We consider vintage data for inflation, unemployment and industrial production. We also report payoffs are estimated in the presence of transaction costs (e.g., HML_{BTR}^{TC}) and the portfolios are rebalanced on a monthly basis. Finally, the mean, standard deviation and Sharpe Ratio are annualized (the means are multiplied by 12 and the standard deviation by $\sqrt{12}$) and expressed in percentage points. The superscripts *, **, *** indicate significance of the spread portfolios at the 10%, 5% and 1% level that are estimated using Newey and West (1987) standard errors with the optimal number of lags. The data span the period 1999:02-2017:03.

Panel A: Unemployment							
	P_1	P_2	P_3	P_4	P_5	HML_{BTRuv}	HML_{BTRuv}^{TC}
Mean	0.22	0.25	0.98	0.81	3.81	3.59***	1.84
Std. Dev.	10.08	10.71	9.74	9.69	9.72	7.27	7.27
SR	0.02	0.02	0.10	0.08	0.39	0.49	0.25
Skew	-0.71	-1.15	-0.52	-1.13	-0.33	0.12	0.10
Kurt	5.20	7.02	4.89	6.65	3.71	3.49	3.46
AC(1)	0.12	0.04	-0.06	0.09	0.08	-0.01	-0.03
p-value	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Panel B: Industrial Production							
	P_1	P_2	P_3	P_4	P_5	HML_{BTRyv}	HML_{BTRyv}^{TC}
Mean	-0.53	0.26	2.08	1.89	5.38	5.92***	3.77*
Std. Dev.	9.99	10.17	9.38	9.98	10.38	7.72	7.67
SR	-0.05	0.03	0.22	0.19	0.52	0.77	0.49
Skew	-0.50	-1.20	-0.46	-1.05	-0.63	0.11	0.06
Kurt	5.16	7.58	5.00	7.07	4.00	4.26	4.21
AC(1)	0.10	0.08	0.09	-0.02	0.17	0.07	0.02
p-value	0.00	0.00	0.00	0.00	0.00	0.00	0.00



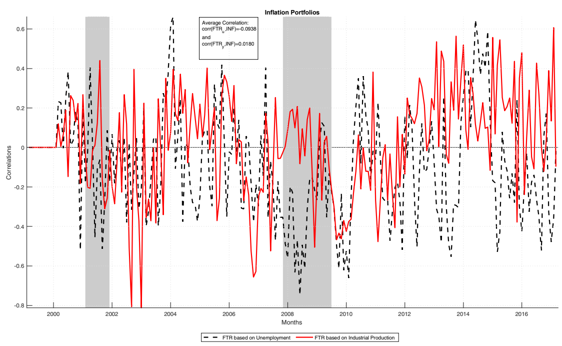
(a.) Revised Data



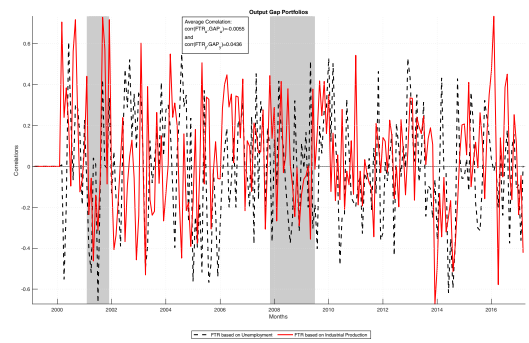
(b.) Vintage Data

Figure A1. Average Loadings of Dynamic Taylor Rules

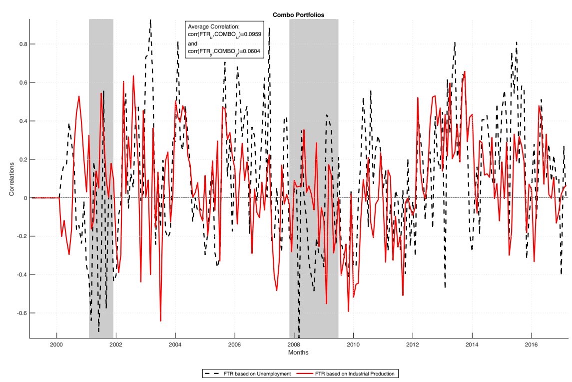
This figure displays average loadings for dynamic Taylor rules. The left graph reports results using revised data for the period 1990:01-2017:03. The bottom graph displays average loadings for real-time data for the period of 1999:02-2017:03. The loadings for inflation are based on a Taylor rule model that includes the unemployment gap and they are comparable to a model that include the detrended industrial production.



(a.) Correlations with Inflation Portfolios



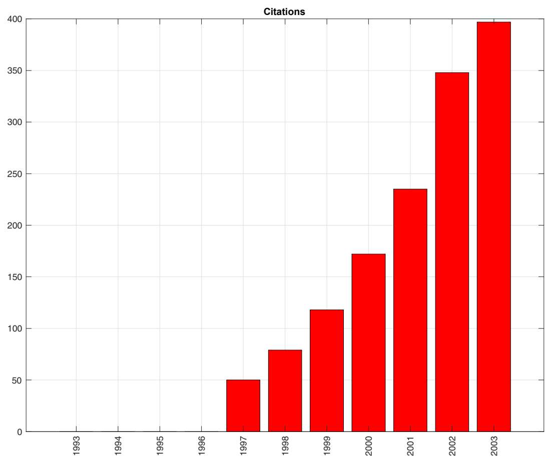
(b.) Correlations with Output Gap Portfolios



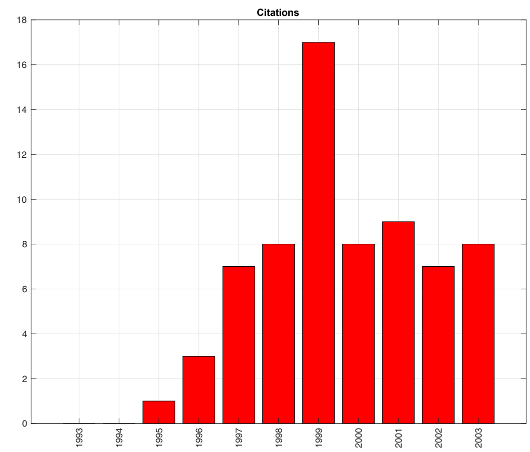
(c.) Correlations with Combo Portfolios

Figure A2. Portfolio Rank Correlations

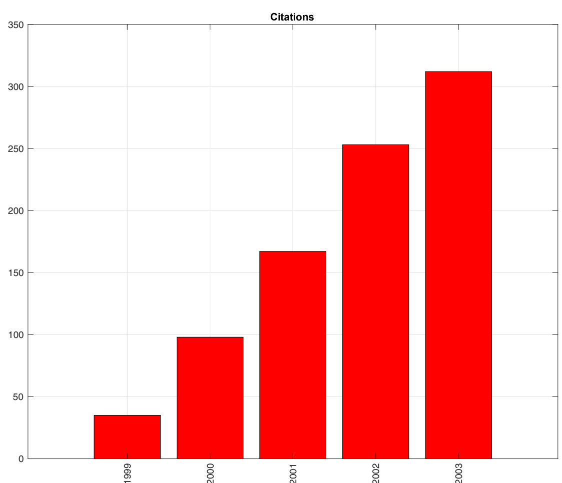
This figure displays the correlations of the portfolio rank for inflation (graph (a.)), output gap production (graph (b.)) and combo portfolios (graph (c.)) with Taylor rule portfolios. We consider Taylor rule specifications with vintages of unemployment gap and detrended Industrial production. The average correlation for all graphs is close to zero and it reported. We employ vintage data that spans the period of 1999.02:2017:03.



(a.) Taylor (1993)



(b.) Henderson and McKibbin (1993)



(c.) Clarida, Gali and Gertler (1999)

Figure A3. Citations of Seminar Papers on Policy Rules

This figure displays the citations of seminal papers on policy rules. Graph (a.) shows the citations of Taylor (1993) and Graph (b.) displays the citations of Henderson and McKibbin (1993). We present in Graph (c.) the citations of Clarida, Gali and Gertler (1999). The data span the period of 1999 to 2003.

Figure A4. Post-Publication Regressions

This figure displays *t*-statistics of contemporaneous regressions of forward-looking Taylor Rule spread portfolios on a dummy that takes the value of 1 the reported month until the end of the sample and zero otherwise. For example, the first *t*-statistic in December 1993 corresponds to a regression of a Taylor rule strategy on a dummy that takes a value of 1 in January 1994 until the end of the sample and zero otherwise. Volatility is the annualized standard deviation of the Taylor rule strategy for the period which corresponds to values of one for the dummy variable. The graph displays results for revised data for the period of 1990:01-2017:03. The black dashed line represents a model that includes a Taylor rule strategy which incorporates unemployment (e.g., HML_{FTRu}) as a proxy for output gap and the red line shows the results for a Taylor rule strategy that considers the detrended industrial production as a proxy for output gap (e.g., HML_{FTRy}). The strategies take into consideration transaction costs. The Taylor rule models consider fixed coefficients.

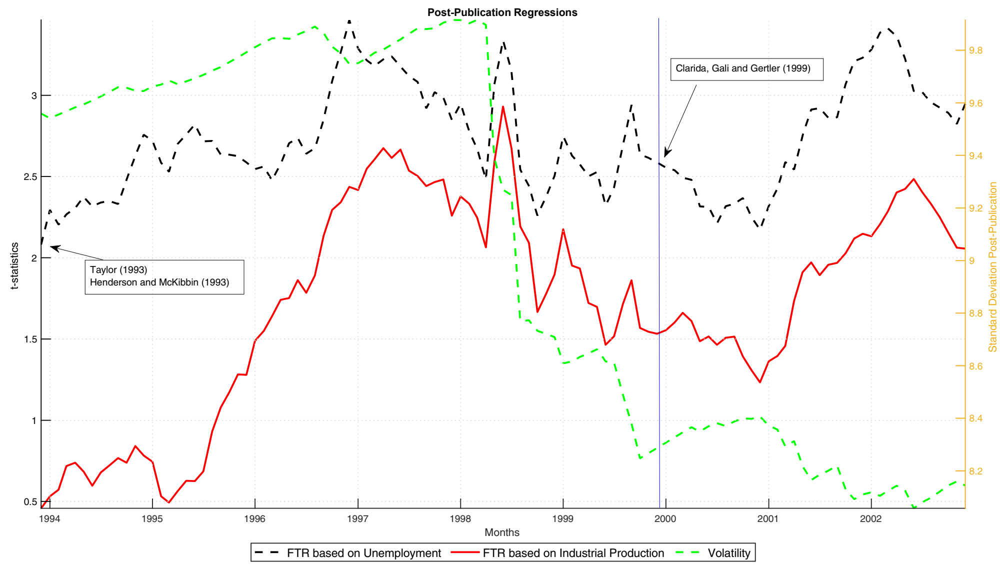


Figure A5. Post-Publication Regressions including the Dollar Factor

This figure displays *t*-statistics of contemporaneous regressions of forward-looking Taylor Rule spread portfolios on a dummy that takes the value of 1 the reported month until the end of the sample and zero otherwise and the dollar factor. For example, the first *t*-statistic in December 2013 corresponds to a regression of a Taylor rule strategy on a dummy that takes a value of 1 in January 2014 until the end of the sample and zero otherwise. The graph displays results for revised data for the period of 1990:01-2017:03. The black dashed line represents a model that includes a Taylor rule strategy which incorporates unemployment (e.g., HML_{FTRu}) as a proxy for output gap and the red line shows the results for a Taylor rule strategy that considers the detrended industrial production as a proxy for output gap (e.g., HML_{FTRy}). The strategies take into consideration transaction costs. The Taylor rule models consider fixed coefficients.

Figure A6. Post-Publication Alphas

This figure displays annualized alphas of the Lustig et al. (2011) model for the post-publication period. The graph displays results for revised data for the period of 1990:01-2017:03. The black dashed line represents a model that includes a Taylor rule strategy which incorporates unemployment (e.g., HML_{FTRu}) as a proxy for output gap and the red line shows the results for a Taylor rule strategy that considers the detrended industrial production as a proxy for output gap (e.g., HML_{FTRy}). The strategies take into consideration transaction costs. The Taylor rule models consider fixed coefficients.

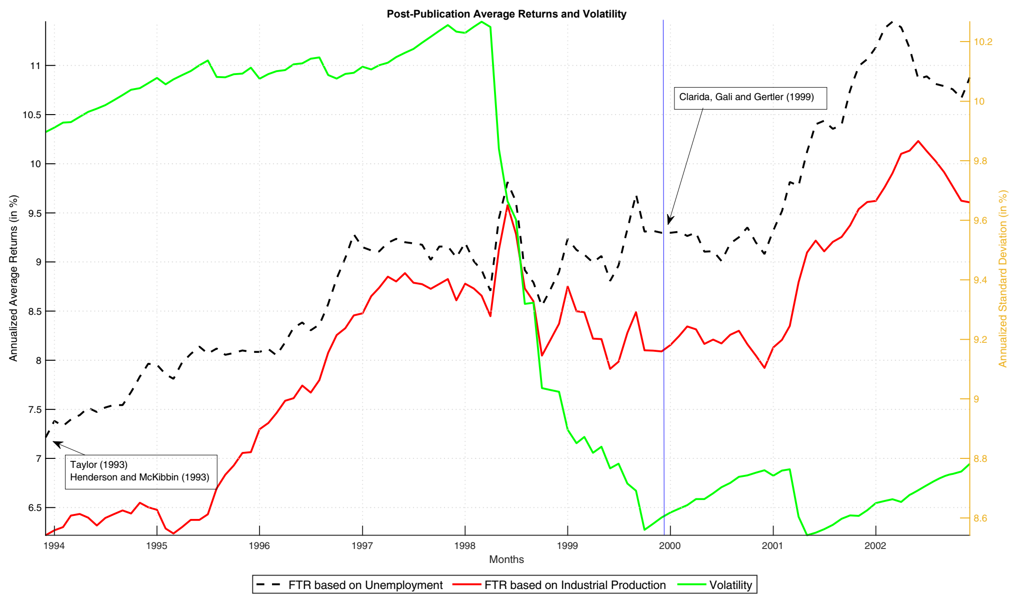
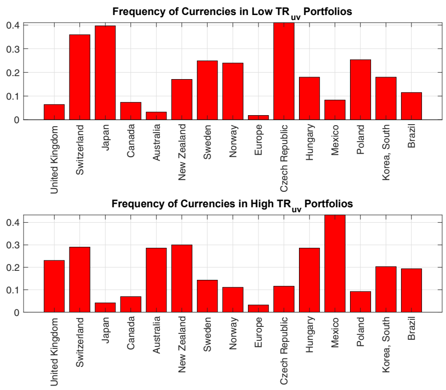
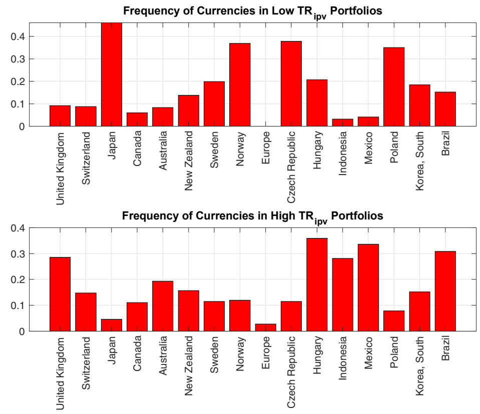


Figure A7. Post-Publication Average Returns

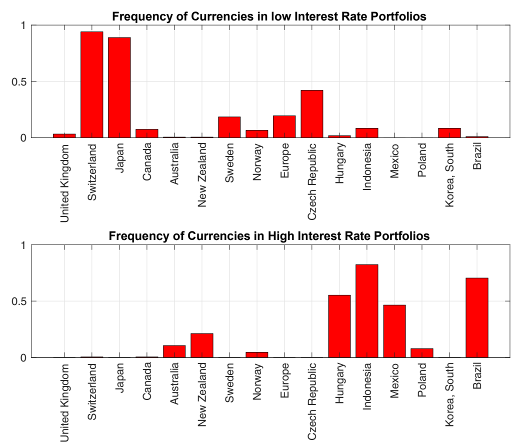
This figure displays annualized average returns for the post-publication period. The graph displays results for revised data for the period of 1990:01-2017:03. The black dashed line represents a model that includes a Taylor rule strategy which incorporates unemployment (e.g., HML_{FTRu}) as a proxy for output gap and the red line shows the results for a Taylor rule strategy that considers the detrended industrial production as a proxy for output gap (e.g., HML_{FTRy}). The strategies take into consideration transaction costs. The Taylor rule models consider fixed coefficients.



(a.) $\xi_t = 1.5(\pi_t^f - \pi_t^*) - 0.5u_t^{gap} - \lambda r_t$



(b.) $\xi_t = 1.5(\pi_t^f - \pi_t^*) + 0.5y_t^{gap} - \lambda r_t$



(c.) Carry Trade Portfolios

Figure A8. Portfolio Holdings

This figure displays the frequency of each currency in low and high Taylor rule portfolio. We consider Taylor rule specifications with vintages of unemployment gap (graph (a.)) and detrended Industrial production (graph (b.)). The top graphs show results for the low Taylor Rule signals while the bottom graphs display results for high signals. Graph (c.) shows the frequency of currencies in carry trade portfolios. We employ vintage data that spans the period of 1999.02:2017:03.