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Title: Exchange Rates and Asset Prices in a Global Demand System

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Abstract

Using international holdings data, we estimate a demand system for financial assets across 36 countries. The demand system provides a unified framework for decomposing variation in exchange rates, long-term yields, and stock prices; interpreting major economic events such as the European sovereign debt crisis; and estimating the convenience yield on US assets. Macro variables and policy variables (i.e., short-term rates, debt quantities, and foreign exchange reserves) account for 55 percent of the variation in exchange rates, 57 percent of long-term yields, and 69 percent of stock prices. The average convenience yield is 2.15 percent on US long-term debt and 1.70 percent on US equity.

Keywords: Asset demand system, Asset pricing, Foreign exchange reserves, Monetary policy, Portfolio choice