
 ELSEVIER	Available online at <a href="http://www.sciencedirect.com">www.sciencedirect.com</a>	<b>Journal of International Money and Finance</b>
		<a href="http://www.elsevier.com/locate/jimf">www.elsevier.com/locate/jimf</a>
Journal of International Money and Finance xx (2006) 1--16		
<h2>Interest rate linkages in the Eurocurrency market: Contemporaneous and out-of-sample Granger causality tests</h2>		
Zijun Wang <sup>a</sup> Jian Yang <sup>bc*</sup>		
E-mail address: <a href="mailto:jiyang@pvamu.edu">jiyang@pvamu.edu</a> Qi Li <sup>de</sup>		
<sup>a</sup> Private Enterprise Research Center, Texas A& M University, College Station, TX 77843, USA		
<sup>b</sup> Department of Accounting, Finance and MIS, Prairie View A& M University, Prairie View, TX 77446, USA		
<sup>c</sup> Lingnan College, Sun Yat-Sen University, Guangzhou, Guangdong 510275, PR China		
<sup>d</sup> Department of Economics, Texas A& M University, College Station, TX 77843, USA		
<sup>e</sup> Department of Economics, Tsinghua University, Beijing 100084, PR China		
<b>Abstract</b>		
<p>This paper examines linkages among major Eurocurrency interest rates during 1994–2002. Eurocurrency interest rate causal linkages are found to be much stronger with additional allowance for contemporaneous causality test results than the inference based solely on Granger causality tests. The impact of U.S. interest rates is clearly not dominant in the Eurocurrency markets, while the Japanese interest rates are found to be quite influential. German interest rates both cause, and are caused by, several other Eurocurrency interest rates. By contrast, interest rates on the new currency, the Euro, do not have a substantial influence on other Eurocurrency interest rates, which underscores its emerging status.</p>		
©2006 Elsevier Ltd. All rights reserved.		
<b>JEL classification</b> F36, F21		
<b>Keywords</b> Interest rate linkages, Granger causality, Forecasting evaluation, Contemporaneous correlation, Directed acyclic graphs		
<b>1. Introduction</b>		
<p>In the past two decades, linkages among international capital and money markets have been perceived to increase dramatically, while government-imposed barriers to international capital flows</p>		
*Corresponding author. Department of Accounting, Finance and MIS, Prairie View A& M University, Prairie View, TX 77446, USA. Tel.: +1 936 857 4014; fax: +1 936 857 2797.		
0261-5606/\$ - see front matter ©2006 Elsevier Ltd. All rights reserved.		
doi:10.1016/j.jimonfin.2006.10.005		

have fallen. The extent of interest rate linkages in these markets carries important policy implications for the independence of monetary policies by nations' central banks (Kirchgassner and Wolters, 1987, 1993). If a country is sufficiently large or is isolated from other countries due to idiosyncratic domestic conditions, the country may not be responsive to foreign interest rate changes. This would, in turn, permit the country to pursue an independent monetary policy. Furthermore, enhanced understanding of transmission of (short-term) interest rates across countries can also help to more accurately forecast interest rates in a country, itself a key input to strategic business decisions (Lo et al., 1995). However, the extent of such international interest rate linkages remains an unsettled empirical matter.