In this paper Professor Bernholz and Kugler discuss an important topic and their analysis could make a significant contribution to our understanding of the short-run fluctuations of exchange and interest rates. The revised version of the paper states the problem and the methodology of their research much more clearly than before. However, it seems to me that some further work is needed to clearly bring out the importance of the authors' contribution: My suggestions are as follows:

1. In the introduction it might be useful to give a simplified mathematical outline of Dornbush's (or Kouri's) model in order to motivate the paper and inform the readers about the structure of their own empirical model. The short-comings of the basic Dornbush/Kouri model and Niehans's modifications can be discussed formally. Then the Kugler/Bernholz model can be stated clearly in the context of this theoretical literature. Such a discussion will provide the needed theoretical background and framework to motivate the empirical analysis of this paper.

2. Some effort should be made to specify the underlying theoretical model of Bernholz and Kugler's model. The discussion on page 4 of the manuscript is not very clear and illuminating. What is the structure and properties of the model the authors have in mind that would provide them with the results stated on the bottom of page 4 and top of page 5 that they expect? Are these results uniquely deducible from their model or are they ad-hoc expectations?
3. The justification for the form of the basic model (1) is not provided. Why should the model include all the specific variables and why should be distributed lag formulation be the way as stated in equation (1) or (2)? What are the potential specification errors that may arise because of the simultaneity of money, prices and output in these equations?

4. It might be helpful to specify clearly what type of expectations process is embedded in the model. The authors make references (for example on page 6) to this phenomenon but why not formulate the exact expectation formulae?!

5. The feedback system underlying the reduced form equation (2) should be discussed in some detail, again explicitly, to show how the structure of the autoregressive part of the equations can tell us something about the feedback between the interest and exchange rates.

6. The empirical results are interesting but several points need to be made
(i) Why the same length of distributed lag is assumed for each explanatory variable? Is there any theoretical or empirical justification for this?
(ii) Why not drop some of the insignificant coefficients? Using conventional criterion of t statistics: $t > 2.0$, a large number of the coefficients in each regression equation drops out. How would the results be then interpreted?
(iii) Also, many of the distributed lag coefficients for a given variable have positive and negative signs. What sense the authors make out of this?
(iv) The authors might have considered using the Almons approximation method to estimate their distributed lag model. Then they could have appropriately restricted the form and pattern of the lag structure in (2) according to some a-priori formulation and obtained a more reasonable set of results.
7. There is a strong possibility that a high degree of multicollinearity pervails among the independent variables and their lagged values in all the estimated equations. If so the empirical results provided in the paper are highly suspect. The authors should test for presence of multicollinearity and reformulate and estimate their model if necessary.

8. The authors hardly discuss why their model gives contrasting results for Germany and Switzerland: Consider the interest rate equations (5) and (7): In equation (7) the coefficients of money and price variables are hardly significant. While this is not the case for equation (5). What is the economic rationale for this? What is in the two economies that may explain the differences?

9. Finally, it might be desirable for the authors to give more clear interpretation of the economic meaning of whatever empirical results they find. Also it would be good to know whether this empirical analysis leads in any way to modification or confirmation of the Dornbush/Kouri type of theoretical models.