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# Purchasing Power Parity

Rudiger Dornbusch

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The paper is a survey of PPP theory and evidence prepared for the New Palgrave dictionary of economics. Following a statement of the absolute and relative versions of the theory, there is a brief sketch of the history of thought with emphasis on Cassel and the monetary approach. A theoretical part distinguishes structural and transitory deviations from PPP. The main basis for structural deviations is the Ricardo-Harrod-Balassa-Samuelson model of productivity differentials that affect the real prices of home goods and hence real price levels. Transitory deviations emerge from differential speeds of goods and assets markets. In particular sticky wages combined with imperfect competition or spatial discrimination in pricing give rise to sometimes persistent movements in real exchange rates. After an overview of empirical evidence the paper concludes with a review of implications of PPP disparities. Applications to international real income comparisons, interest rate linkages and exchange rate policy receive attention.

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## Published Versions

Dornbusch, Rudiger. "Purchasing Power Parity," The New Palgrave Dictionary of Economics, Macmillan, 1986.

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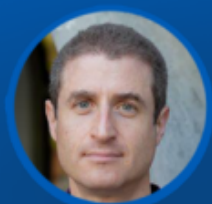
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Contact Us

1050 Massachusetts Avenue

Cambridge, MA 02138

617-868-3900

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