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# Purchasing Power Parity in economies in transition: evidence from Central and East European countries

Dimitrios Sideris

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## Abstract

The present study tests for the validity of long-run Purchasing Power Parity (PPP) for 17 European economies in transition. Analysis is performed following the methodological suggestions expressed in recent studies for PPP. Long-run PPP is initially tested for each economy vis-a-vis the USA, using the Johansen cointegration methodology and then for the whole set of countries using the Johansen (2001) model cointegration

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## Notes

- <sup>1</sup> In this, the categorization of Froot and Rogoff ([1995](#)) is followed.
- <sup>2</sup> Dibooglu and Kutan ([2001](#)) identify the impact of nominal shocks on the nominal and real exchange rates in Hungary and Poland; Suppel ([2003](#)) illustrates the important effect of real shocks to the real exchange rates of Poland, the Czech Republic and the Slovak Republic; Borghijs and Kuijs ([2004](#)) show that it is mainly nominal shocks, which have contributed significantly to nominal exchange rate variability in five CEE Countries (the Czech Republic, Hungary, Poland, the Slovak Republic and Slovenia).
- <sup>3</sup> Most of these papers find evidence for relative PPP but fail to support strong PPP.
- <sup>4</sup> See Taylor ([1988](#)), for the derivation of Equation [3](#) in a model allowing for transportation costs and measurement errors.
- <sup>5</sup> The panel cointegration analysis uses a common sample length for all countries.
- <sup>6</sup> Their diagnostic tests do not indicate any serious mis-specification (serial correlation and/or non-normality) problem. They are not reported here for space reasons but are available on request.
- <sup>7</sup> They argue that in panel tests testing for the stationarity of real exchange rates, the non-stationarity hypothesis is rejected as a result of a few stationary real exchange rates in the panels. Still, alternative tests to overcome this problem turn out to be generally
- <sup>8</sup> In any analysis

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