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The saving–investment correlation in Greece, 1960–1997: implications for capital mobility

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Abstract

In this note, the national saving–domestic investment correlation is examined in terms of an error correction model to gain some insight into the degree of capital mobility, using Greek data for the period 1960–1997. In particular, we employ cointegration analysis with an emphasis on the error correction process of the time series on annual data for Greece. Our work follows the study of Bajo-Rubio [Appl. Econ. Lett. 5 (1998) 769] that deals with the case of Spain. However, we use a longer time period, which enable us to examine with more preciseness the saving–investment relationship in Greece and its implications for capital mobility. The results show that Greek domestic investments and national savings during 1960–1997 are to a great extent cointegrated and that a significant long-run relationship exists.

JEL classification: F41; Macro focus

Keywords: Saving; Investment; Globalization

1. Introduction

There is a consensus among professional economists that full capital mobility increases welfare by allowing efficient allocation of factors of production. Welfare results are indeed optimized in case allocation is taking place at a global level. The argument is, beyond any doubt, sound and true. However, perceptions in the

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literature about the extent and importance of global capital integration in the last 20 years vary, depending on how global capital mobility is measured. The established academic consensus about the degree of global capital markets integration has been even more destabilized since the appearance of the seminal paper by Feldstein and Horioka (1980) on the *S*–*I* correlation.

The Feldstein–Horioka (F–H) puzzle, that a close relationship between national savings and domestic investments constitutes a stable regularity in the OECD countries, continues to challenge economic orthodoxy as the majority of related tests continue showing a saving–investment retention coefficient that lies quite far from zero.[1] Despite objections concerning F–H tests robustness, the puzzle still remains a stylized fact as related studies and tests confirm more or less a strong "home bias" in capital markets and, so, research efforts to solve the puzzle are still of high priority (Rodrik, 2000).[2] Such efforts have been recently focused on indirect ways to explain the puzzle by introducing imperfect goods market integration (Obstfeld & Rogoff, 2000).

We believe that imperfections even if they could be found in goods market, should be less globally homogeneous and so have to be investigated at a national level. Applying various tests country by country could help not only to examine whether — and how much — a single country is financially integrated into the global economy. It could also help us to find out whether F–H tests continue to be valid. It is reminded that the overestimation and sometimes the misunderstanding of the extent of financial globalization could lead individual countries to unsuitable policy responses with catastrophic results. Thus, to measure capital mobility and a country's integration to global capital markets is of cardinal importance for policy prescriptions as well.

In this context, the very first issue needs clarification is whether financial globalization has really gone far for each country. In this note we reassess the relative importance of national economic ties in the case of Greece. The note measures the evolution of the financial integration of the Greek economy during the period 1960–1997. We employ cointegration analysis with an emphasis on the error correction process of the time series on annual data for Greece for the period 1960–1997. Our work follows the study of Bajo-Rubio (1998) that deals with the case of Spain. However, we use a longer time period, which enable us to examine with more preciseness the saving–investment relationship in Greece.

In the last section we focus on the policy implications of the findings. We give emphasis to policy guidelines especially in the context of Greece's efforts to keep up with the EMU requirements.

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[1] See Coakley, Kulasi, and Smith (1998) for an excellent survey.

[2] Such as "endogeneity" or efforts to prove that even a high retention coefficient does not necessarily mean that world capital mobility is imperfect. Also, Alexakis and Apergis (1994), using the methodology of cointegration — in the context of a general equilibrium optimization model capable of generating artificial model data of savings and investment — find no link between savings and investment, supporting the case of highly integrated capital markets.