



Panel cointegration results on international capital mobility in Asian economies

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Abstract

This paper investigates the Feldstein–Horioka coefficients for 11 Asian countries using the recently developed ‘between-group’ FMOLS and DOLS panel cointegration techniques. Savings and investment rates are found to be nonstationary and to be cointegrated in panels. The estimated coefficients using FMOLS and DOLS are 0.39 and 0.42, respectively, for the period 1980–1998. These values are much smaller than the estimates of 0.58 and 0.76 for 1960–1979. The small coefficients suggest that capital mobility increased in Asian countries in the 1980s and 1990s.

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1. Introduction

Increasing capital mobility across countries is an important phenomenon for economic policy makers and firms. It has potential beneficial effects on the economy because it enables agents to allocate the resources more efficiently and give more scope for risk management. However, higher international capital mobility may increase the possibility of abrupt reversals of capital flows that destabilize economies and cause financial crises, like the 1997 Asian crisis. The degree of international capital mobility also has an influence on the effects of economic policy and responses to external shocks. Therefore, it is important and worthwhile to investigate the degree of international capital mobility.

Asia is composed of many dynamic emerging economies. Most of the Asian countries restricted capital flows across countries during the 1960s and 1970s. But in the 1980s they introduced relatively floating exchange rate systems and started to take measures for capital account liberalization cautiously and progressively. They accelerated capital market opening in the 1990s. It is expected that the removal of capital controls has increased international capital mobility. These capital account liberalization policies contributed to massive capital inflows to Asian countries in the 1990s prior to the financial crisis in 1997. Here the question arises as to whether international capital mobility actually increased in Asian economies after the 1980s relative to periods of the 1960s and 1970s, and if so, how mobile are capital flows across countries in Asia?

There are several ways to investigate the degree of international capital mobility.¹ One is to investigate the relationship between savings and investment. [Feldstein and Horioka \(1980, hereafter FH\)](#) proposed that the correlation between savings and investment would be zero under perfect international capital mobility, whereas it would be one under no capital mobility. Many economists have studied the savings and investment relation² since the seminal work of FH.

Some of these studies focused on the time series aspects of the data. Savings and investment rates usually turn out to be nonstationary. It is well known that one should avoid a spurious regression problem by checking the cointegration relationship when the time series data are nonstationary. However, the traditional cointegration technique has the problem of low power. In order to improve the power of the test, the number of observations (span of data) should be extended. However, it is not easy to find data for a very long time span except for a few countries.³ Furthermore, expansion of the time horizon might cause the unwanted regime-shift problem for the saving–investment relationship. The panel data enable us to solve the power problem.

¹ These include checking the covered or uncovered interest parity condition and examining the international consumption correlation, international portfolio diversification. [Obstfeld \(1993\)](#) is referred to for more details.

² See [Coakley et al. \(1998\)](#).

³ [Taylor \(1996\)](#) uses the data of savings and investment rate for 12 countries over the period of 1850–1992.

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