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**PURCHASING POWER PARITY IN TRANSITION ECONOMIES:
DOMESTIC CURRENCY AGAINST THE EURO**

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Abstract. The objective of this study is to analyze the validity of the PPP theory, in its strong or weakest forms, for a sample of countries that have recently integrated or are about to integrate in the European Union vis-à-vis the Eurozone countries. We apply three different classical methodologies: graphical analysis, stationarity tests of the real exchange rates and cointegration analysis. The exchange rates display most of the times negative deviations from the PPP exchange rates. For most of the countries (8 out of 10), the unit root tests indicate that the real exchange rate is not level or trend stationary. The cointegration analysis provides support for the existence of a long run relationship between the exchange rate and the price ratio for 5 of 7 transition economies. The results of such an investigation are important for policy makers, as well as for traders.

JEL Classification: E31, F31, P24

Keywords: purchasing power parity, real exchange rate, cointegration, transition

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