

On the Dynamics of the Greek Twin Deficits: Empirical evidence over the period 1960 – 2007

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Abstract

One of the most important open macroeconomic issues, during the current global economic recession, concerns the sustainability of persistent budget and trade deficits as well as possible interactions between them. These deficits are most crucial due to severe debt servicing costs, faced by today's economies despite their development level. This paper presents time series evidence over the period 1960 up to 2007, using data of the Greek Economy. Our results confirm 'weak' sustainability of both deficits and evidence in favor of the Keynesian rationale regarding the 'twin deficits hypothesis'.

Keywords: Budget and Trade Deficits, Sustainability, Twin Deficits Hypothesis, Cointegration, Greek Economy (1960-2007).

JEL classification: C22, F32, F41, H62.

1. Introduction

One of the hottest macroeconomic issues during the current economic turmoil concerns the sustainability of persistent current account deficits, due to severe debt servicing costs, faced by both advanced and developing economies. These threatening economic characteristics of today's global recession reinforce the question on the ability of a country to service and repay its debt by avoiding default (Wickens and Uctum, 1993).

Public deficits have created increased borrowing requirements for governments worldwide. In particular, developed economies turn, basically, to domestic borrowing, whereas developing ones turn to both domestic and foreign capital. In any case, though, high deficit levels eventually lead to an accumulation of debt, which forces an inexorable necessity for financial discipline and control over the public deficit (e.g. Hakkio and Rush, 1991; Haug, 1991).

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