LUKÁŠ FRÝD

University of Economics, Prague , Czech Republic

INSTABILITY IN THE ECONOMETRIC MODELS: AN APPLICATION TO THE FELDSTEIN-HORIOKA PUZZLE

Abstract:

Nowadays we face the big debate about the pros and cons of membership in the European Union. In this paper, we analyze one particular potential benefit of membership for the Czech Republic. This benefit is capital mobility. We show that after joining the CR to the EU the capital mobility significantly increases. Our model is based on the alternative Feldstein-Horioka (FH) model derived from the vector error correction model. This alternative form comes from the intertemporal budget constraint and shows the FH as the inappropriate model for capital mobility measure. We propose an empirical framework to capture two different regimes, regime one and regime two in the vector error correction model. We show the period 1996–2004 is composed of both regime when regime two dominate. The most important conclusion is that the period 2005–2017 is given by the pure regime one which is connected with the higher capital mobility than regime two and so after 2004, the capital mobility in the Czech Republic increases.

Keywords:

Feldstein-Horioka Puzzle, threshold cointegration, switching models

JEL Classification: E22, F41, F40