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COINTEGRATION BETWEEN ECONOMIC ACTIVITY AND OIL PRICES IN THE OPEC COUNTRIES: A TIME SERIES APPROACH

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Abstract

The aim of this paper is to study the long-term relationship between oil prices and economic activity, proxied by GDP. To account for the long accepted evidence of a non-existing long run relationship between oil prices and economic activity, we carry out unit root and cointegration tests in presence of deterministic structural breaks. Our empirical analysis concerns the OPEC group, and generally extends from 1960 to 2012. This study contributes to the extensive literature on oil prices by adding a proper supply side analysis of a possible long run equilibrium between GDP and oil prices in a group of oil exporting and producing countries, and effectively manages to find an equilibrium relationship in Saudi Arabia by taking into account possible structural breaks. Setting up a Granger causality test in presence of deterministic structural breaks, the papers concludes that, even though no short run causality linkage could be found between oil prices and GDP, the existence of such relationship holds in the long run and appears to show some degree of predictive ability on GDP growth in Saudi Arabia.

Keywords: OPEC Countries, GDP growth, Oil prices, Cointegration Analysis.

JEL Classification: C32, F43, O47.

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