

## **Non-Technical Summary**

6th Global Development Network Regional Research Competition (RRC VI)

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**Title of the Project: “Price Convergence in New Member States of the European Union: the Case of Hungary and the Slovak Republic”**

**Full title of the Paper: The Border Effect in Small Open Economies: Hungary and the Slovak Republic**

Authors of the Paper: Julius Horvath, Attila Ratfai and Botond Dome

This paper examines the importance of the national border in relative price variability in two neighboring, small open economies. Using monthly frequency price data of narrowly defined, homogenous consumer products, it finds that the time-series variation in within-country relative prices is about the same in the two countries. After controlling for distance, relative price variation is significantly higher across than within countries. The border is the dominant determinant of relative prices, even after accounting for nominal exchange rate variability and local culture as represented by language spoken. Our estimates of the border effect are largely immune to the bias identified in Gorodnichenko and Tesar (2006).

Keywords: price convergence, border effect, transition economies