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**Lag Length Selection and Tests
of Granger Causality
between the Twin Deficits**

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Lag Length Selection and Tests of Granger Causality between the Twin Deficits

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Abstract:

This paper employs Granger causality tests to investigate the causal relationship between the twin deficits based on arbitrarily chosen lags, lags chosen based on five statistical criteria, and an extensive search of the lag space. The results suggest the absence of causality between the twin deficits for developed countries while results are mixed for developing countries.

The results also suggest that the arbitrarily lag-length specifications fail to ensure that the results are not based on the capricious choice of the lag structure. Furthermore, a frequently suggested rule of thumb does not appear to fare any better. Indeed, if one wishes to be agnostic about the order of the model, it appears that the safest approach is to perform an extensive search of the lag space.

A comparison of the above results with results obtained from robust selection criteria confirms the robustness of the previous findings.