Response to Referee 1

1. The group of OECD countries considered in the paper is composed of 16 high income economies. In fact, our purpose is to compare BS effects in two areas with noticeable different levels of economic development. For this reason, Mexico – ranked as an upper-middle income economy - is included in the LA area and not in our – purposely - restricted OECD group of countries selected for this empirical research, which are high-income members..

2. Effectively, the period sample is a bit short because we cannot estimate sectoral labour productivities for all countries of our samples with the data available prior to 1991. In fact, empirical analysis of the BS hypothesis in emerging market economies unavoidably face a trade-off between a) making rough and imperfect calculations of labour productivities for the whole economy, which forces us to not differentiate between sectors, and b) computing labour productivities *for each of the two broad sectors* on which the BS hypothesis crucially relies: tradables and non tradables. The first method allows the researcher to obtain data for longer periods, but at the cost of ignoring the differences in labour productivity between sectors. This is the option followed by Drine and Rault (2003) and Lane and Milesi-Ferretti (2004), who used simple GDP per capita of the incumbent countries as a proxy of *global* productivity. We prefer method b) because, apart from being more precise and reliable for sectoral analysis than method a), it also matches better with the spirit of the BS theorem. In any case, we are aware of the difficulties created by the short time period, and try to overcome them by using panel observations and applying recent and consistent bootstrapping methodologies to our panel data.

3. The BS theoretical body deals with **real** exchange rates. Correspondingly, it can be submitted to empirical testing under *any nominal* exchange rate arrangement. However, the distinction between exchange rate regimes does matter for the analysis of PPP(T) as a pillar of the BS theorem. In fact, whilst floating regimes compel us to use the nominal exchange rate as the dependent variable in the PPP(T) relationship, fixed regimes require us to assign this role to the price differential. Since the bulk of countries of our samples exhibited flexibility in their exchange rate regimes during most of the period analysis, we decided to test PPP(T) with the nominal exchange rate as the explained variable, while excluding the countries – not only Argentina, but also Panama, El Salvador and Ecuador - that adopted very rigid exchange rate regimes during the sample period.

4. Testing the reasons why BS results differ between developed and developing countries is a very crucial issue. However, it would require us to write another paper. We leave this interesting topic for a future research. In any case, in the new version of the paper we take into account this worry - raised also by other referees - and we support our reasoning with empirical findings of several recent papers.

Thank you very much for your instructive and interesting comments.