Comments on

IMPACT OF EXCHANGE RATE MOVEMENTS ON EXPORTS: AN ANALYSIS OF INDIAN NON-FINANCIAL SECTOR FIRMS

Yin-Wong Cheung & Rajeswari Sengupta

Joshua Aizenman

USC & the NBER

NIPFP-DEA-JIMF Conference,

12-13th December, 2012

Neemrana Fort Palace
Rajasthan

The agenda and results

- Explore the impact of REER fluctuations on the share of exports of Indian non-financial sector firms for the period of 2000 to 2010.
- Find a strong negative impact of currency appreciation and currency volatility on Indian firms' export shares.
- The effect of REER changes is marginally stronger on services exports compared to goods exports.
- Non-IT services are relatively more affected by REER change, whereas IT services are more impacted by REER volatility.

An appreciation of the REER has a signficant negative effect on exports, the effect of depreciation however is not as clear.

Results

Reducing REER volatility by one standard deviation would increase Indian firms' exports share by 11 %.

The methodology

$$\Delta X_{it} = \beta_0 + \beta_1 \Delta REER_t + \beta_2 (REER\_vol)_t + \beta_3 \Delta I_t^* + \beta_4 Y_{it-1} + \beta_5 Z_t + \chi \mu_i + \phi \eta_t,$$

RHS firm exports to sales ratio of firm *i* at time t;

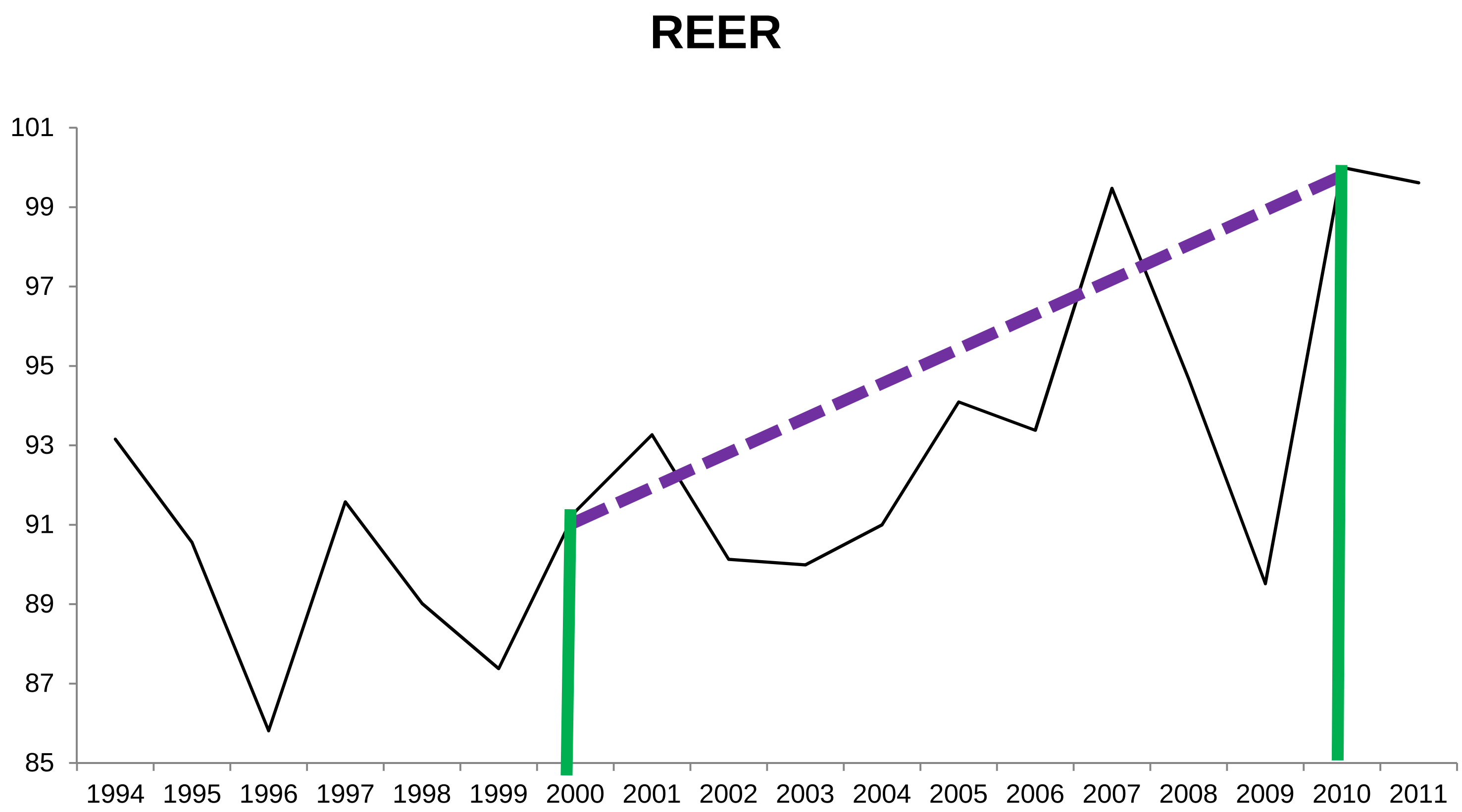
ΔI^* = change in the level of foreign income.

The base specification is modified by adding various controls.

The contribution of the study is the use of micro-evidence.

Comments

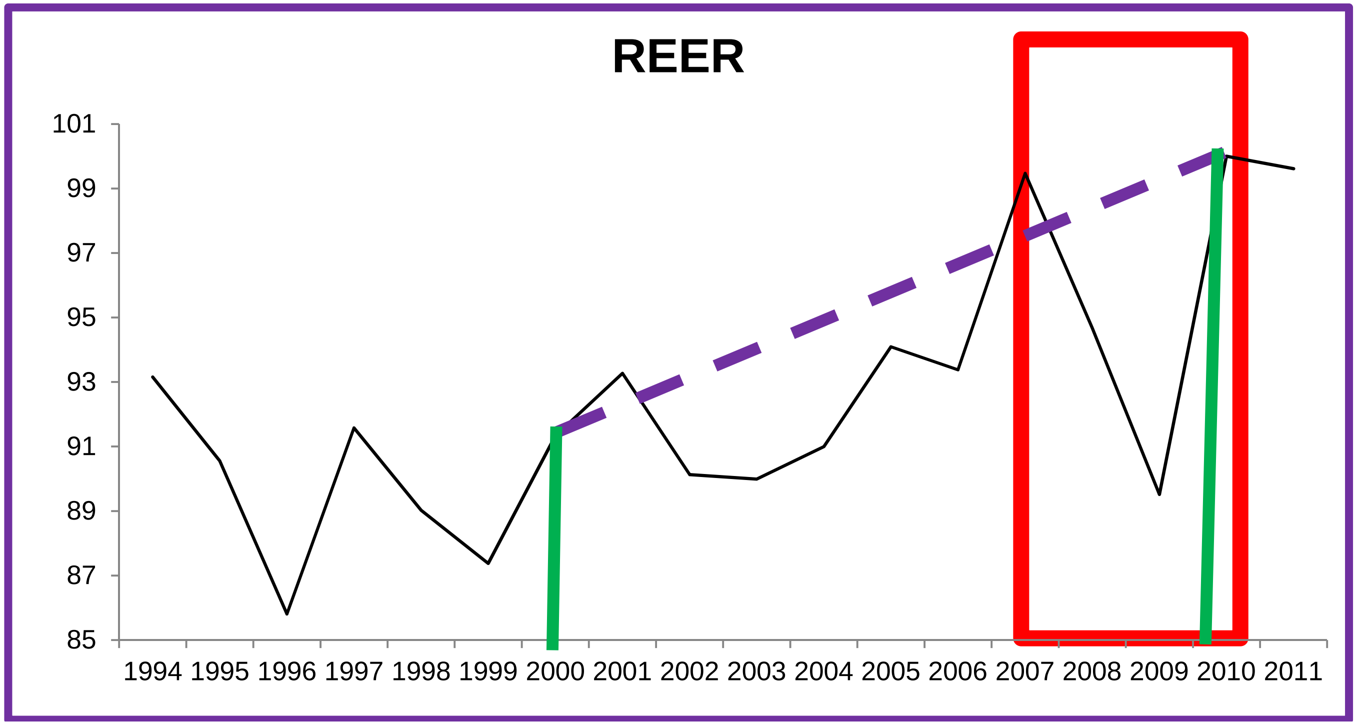
"The main explanatory variable of interest, REER exhibits a steady appreciation from 91 to 100 between 2000 and 2010 registering an appreciation of close to 12% in 2010."



A 1%/year REER appreciation at times of fast growth – not a reason to be concerned.

Yet, there has been a structural change in 2007:

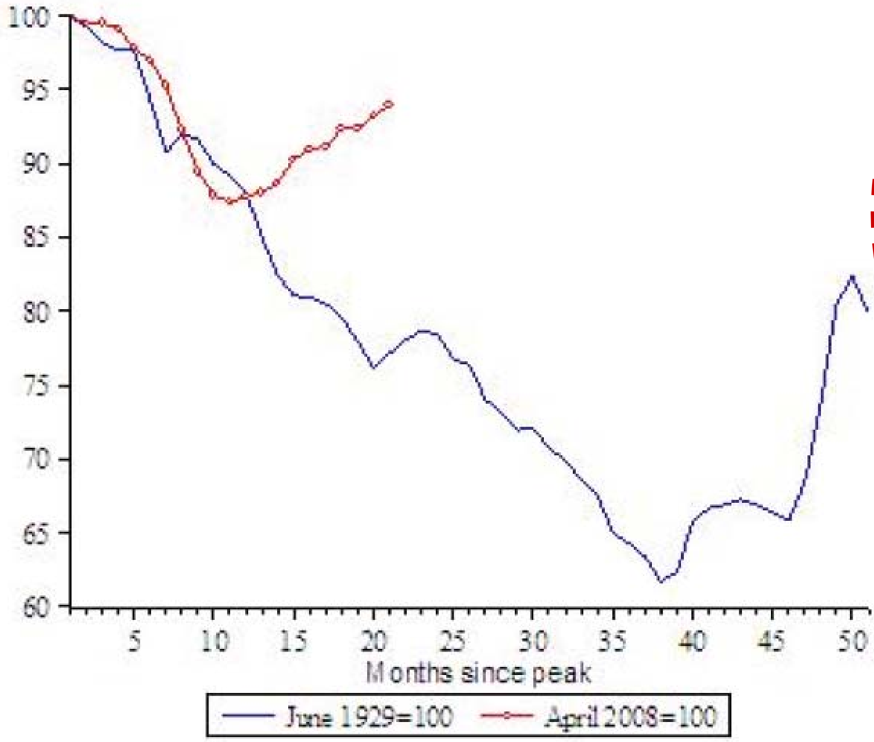
- the end of the great moderation for the OECD countries,
- the global crisis,
- and the following up QE.

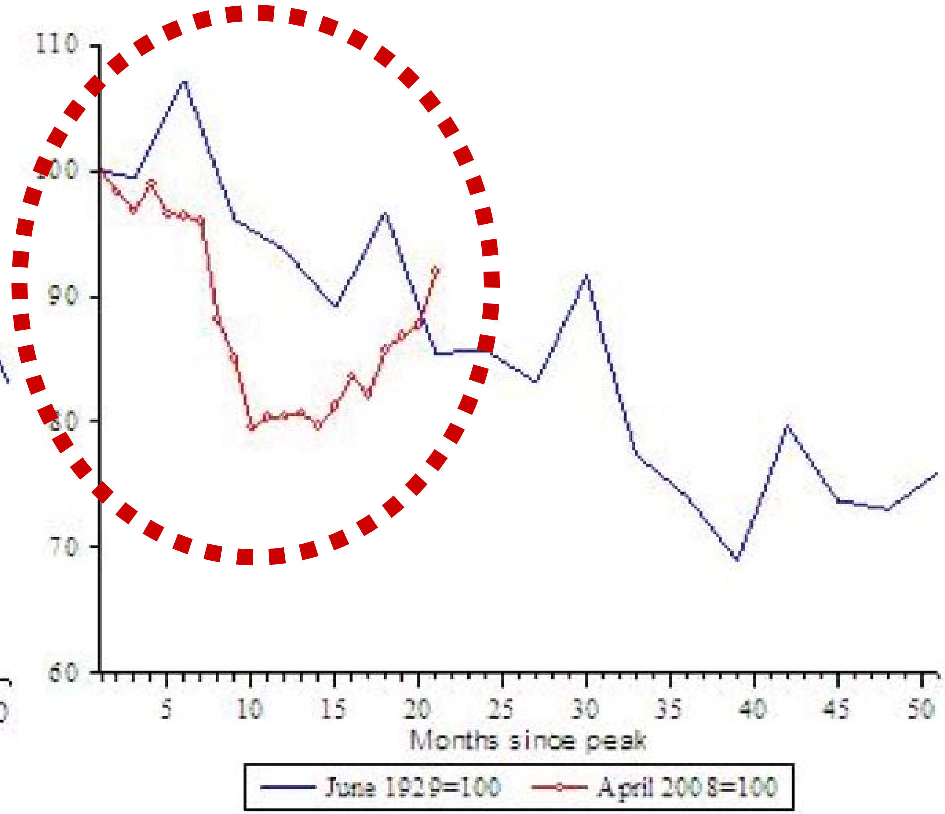


What do the new data tell us?
Eichengreen, O'Rourke, 8 March 2010, Voxeu

World industrial production, Volume of world trade,

now vs. then





Suggestions

- Re-do the regressions, splitting the sample, 2000-2006, and 2007-2010. I expect that most of the quentative results are driven by the global crisis window.
- I am not convinced that the complexity of the crisis is properly controlled.

The authors control the “World Exports/World GDP.”

- I suggest to control for

- Volume of world trade, collapsed by 20% during the crisis.

- VIX [or other measures of crisis driven volatility]

- Oil prices and CTOT of India [IMF data].

Policy conclusions?

"If policy makers wish to promote exports, they ought to focus their efforts on stemming steady appreciation of the exchange rate."

I am skeptical.

- Successful growth may entail REER appreciation due to the B_S effect.

- Reducing REER volatility around the trend is desirable, but killing the REER appreciation trend may be misguided.

- Are the results driven by the global collapse of trade, and by the QE that followed?

Reflections on India

- The bottleneck hindering higher growth of manufacturing exports is the state of Indian’s infrastructure [Rail, ports, etc.], and the challenges facing its education and training systems.
- These factors matter much more than the REER trend with fluctuations in a band of about +/- 10%.

- Better access to bank funding, reducing the financial and labor market frictions will help.

- Attempts to fix the nominal exc. rate at times of growth may kill growth by leading to a crisis [see Argentina in 1990s, small volatility of the REER, ended with a massive volatility of the REER in the early 2000s].

- Using IR to smooth REER fluctuations may help, Aizenman, Edwards and Riera-Crichton, (JIMF, 2012).

An interesting paper, more work is needed.

Sources

- Aizenman, J. Edwards S. and d. Riera-Crichton, 2012,

"Adjustment patterns to commodity terms of trade shocks: the role of exchange rate and international reserves policies." JIMF

- Lewis, L., 2011, "Menu Costs, Trade Flows, and Exchange Rate Volatility."