Comparative advantage as a source of exporters’ pricing power: Evidence from China and India
by
Sushanata Mallick and Helena Marques

Discussion
by
Rudrani Bhattacharya

National Institute of Public Finance and Policy

March 14, 2014
Part I

Summary of the paper
Objective

- Role of product-level comparative advantage in exchange rate pass through (ERPT) to exporting firms’ prices in China and India

- Comparative advantage associated with lower fixed cost and higher market power

- Higher ERPT to export prices if cost effect dominates

- Lower ERPT to export prices if market power effect dominates
Methodology

- Assumption: Firm-level productivity is a function of product-level Revealed Comparative Advantage (RCA) index and bilateral exchange rate
- Optimal price set by an exporting firm depends on its productivity and hence on product-level comparative advantage and exchange rate
- Panel data set from UN Comtrade consisting of location and product-specific export price data for China and India at 6-digit level
- Product-level RCA index (Hanson, 2012) to proxy comparative advantage
Main findings

In response to a depreciation of NEER

- Chinese firms reduce yuan prices to gain market share: Fixed cost effect

- Indian firms increase rupee prices (pricing-to market, hence incomplete ERPT): Market power effect
Part II

Comments
Implied homogeneity assumption for firm-productivity

Firm productivity: Function of product-level comparative advantage and bilateral exchange rate

- Homogeneous, not heterogeneous productivity across firms exporting a specific product
- Symmetric export price across firms for a specific product
- Product-level ERPT identifiable
Firm productivity in India function of comparative advantage and exchange rate

- Can firm productivity be explained by comparative advantage and exchange rate in India?

- Are estimates of firm-level productivity based on firm level data support this assumption?
Effect on volume of exports?

- Higher the pricing to market, lower response of export volume to exchange rate change

- Exploration of this issue would strengthen the story
Role of imported intermediate inputs (Amiti, Itskhoki, Konings, 2012)

- Large exporters are simultaneously large importers of intermediate inputs
- Depreciation increases variable cost of inputs
- Firms optimally choose to keep mark-up high
- Incomplete ERPT to export prices
- Identification problem of market power channel and imported input cost channel
Are large exporters also large importers of imported input in India?

- Non-financial manufacturing exporting firms in Prowess
- Spearman rank correlation
  - Exports and imports of raw materials (in real terms)
  - Exports (real) and raw material imports as a share of raw material purchase
Findings
Full sample

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<th>Rank correlation coefficient</th>
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<td>Exports &amp; imports in real terms</td>
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<td>Exports (real) &amp; raw material imports/purchase</td>
<td>0.21***</td>
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</table>
**Findings**

Exporters with exports to sales ratio > 30% (value at 75th percentile)

<table>
<thead>
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<th>Rank correlation coefficient</th>
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<tbody>
<tr>
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<td>Exports (real) &amp; raw material imports/purchase</td>
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Alternative possible explanation for low ERPT

- Incomplete ERPT to Indian export prices due to imported input cost effect

- Control for imported input intensity of exporting firms needed
Thank you