

# *brevíssimos cindes* 30

## Exchange Rate, profitability and export performance of the Brazilian industrial sector\*

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July 2011

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The appreciation of the nominal exchange rate, the reduction of the growth rate of exported quantities and the loss in participation of manufactured products in total exports generated the perception among many analysts that the Brazilian industry was suffering from a “Dutch disease” process. This process would result from the effects of exchange appreciation, which reduces stimulus to exports and stimulates imports, reducing global profitability of production and incentives to produce in the industrial sector.

One would expect, therefore, that the process of appreciation of Brazilian currency would be accompanied by a reduction in the profitability of the transformation industry. As a result, one would observe a deceleration and/or drop in industrial production. The data analysis, however, does not corroborate the assumptions and the sequences inherent to that thesis, as we can observe in Picture 1.

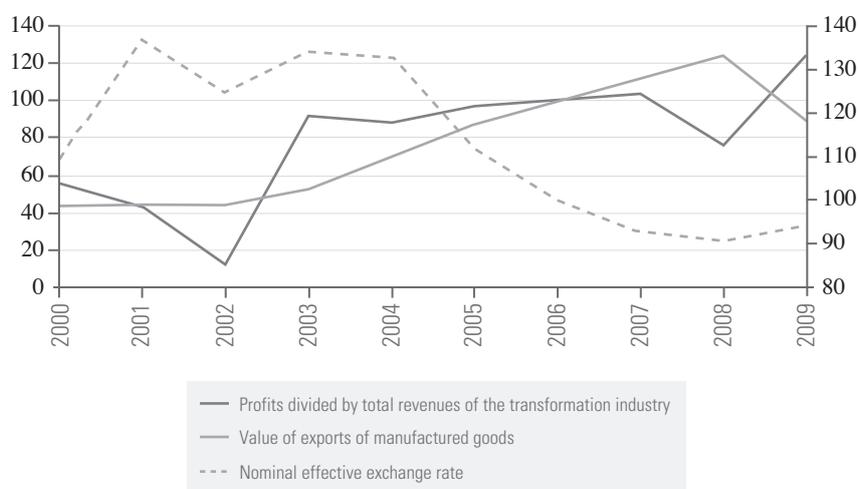
\* This text summarizes the main conclusions of the publication *Breves Cindes 51, Câmbio, rentabilidade e desempenho exportador do setor industrial brasileiro* available at [www.cindesbrasil.org](http://www.cindesbrasil.org)

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**Picture 1**  
**Exchange rate, exporting performance and profitability of the industry**  
**Indexes (2006=100)**



Source: IBGE/PIA, FUNCEX.

The profitability index (profit divided by total revenue) of the transformation industry does not seem affected by the trajectory of the exchange rate: the profitability maintains a slight upward tendency between 2003 and 2007 whereas the nominal effective exchange rate goes through a period of strong appreciation between 2004 and 2008. But, the value of exports of manufactured products presented a sustained trajectory of growth between 2002 and 2008, falling only when the economic crisis is installed at the end of last year. In 2009, at the pinnacle of the crisis, the exchange rate is strongly devalued, but the profitability of the industry increases a lot, while the value of exports drops strongly.

The aggregated performance of the manufacture industry shows that, in average, exporters increased the price of their products in the external markets, maintaining the unit value of exports revenues despite the appreciation of exchange rate. The profitability issues in exports were not the result of revenue problems, but of cost factors – notably of the unit cost of labour – which became more expressive during the last years of the analyzed period. The deceleration of exported quantities did not affect

the rates of production growth nor had significant impacts in profitability.

The study of the behaviour of the exports of manufactured products, of the industrial production and of its profitability for a set of 20 selected groups of industrial activities showed that, in most sectors, exporters managed to compensate revenue losses due to the currency appreciation with the increase of their export prices. Rises in external prices generated negative effects on exported quantities, but similar growth rates of prices had different impacts between capital goods and consumer goods during the period of 2004-2008, suggesting that the consumer goods reduced more rapidly the pace of its sales abroad (or even retracted them) because they were pressured by the growth in domestic demand in the initial phase of the economic expansion. Exporters maintained their unit revenues constant until 2008, increasing them afterwards.

Analysts concerned about the appreciation of the exchange rate understand that the reduction of the growth of external sales after 2004 is a sign of “Dutch disease” in the country. But the reduction of growth

rates of the exported quantum – or even a contraction amidst an international economic crisis – is not a sign of Dutch disease because, for that, one must observe a reduction of profitability and industrial production in the country. One must incorporate other factors into the analysis of that chain, like the relative expansion of aggregate expense vis-à-vis available capacity and the increase in dollars of the prices of exported products. These factors directed the industrial production (which grew after 2004) towards the domestic market and altered exported quantities.

One cannot attribute the reduction in the speed of growth of exported quantities exclusively to the exchange rate. The growth of domestic absorption contributed to that by enabling the redirectioning of a growing part of the production to the internal market. Besides that, the exchange rate was not the only factor to negatively pressure profitability. Domestic demand, when pressuring the labour market, drove workforce costs, reducing profitability of export operations.

In reality, the last decade operated under two different macroeconomic regimens. The second half of the decade watched an expansion of domestic demand,

with the growth of industrial production, slight increase or stability of the unit revenue (effective) of exports and a significant drop in the coefficient of exports of the transformation industry. On the other hand, one also does not observe an explosive growth in the coefficient of penetration of imports which, in the contrary, is still very reduced compared to international standards.

The analysis of the data of industrial production, export performance and profitability of the transformation industry shows that, if there is no evidence of de-industrialization of the Brazilian economy, there are even less evidence that the country is suffering from “Dutch disease”. There are different dynamics being observed in different sectors and one must seek specific explanations to justify such varied behaviours. Anyhow, it seems clear that the expressive growth on domestic absorption produced negative effects on the profitability of exports, both on the side of costs – when putting pressure on the labour market – and on the side of the cost of opportunity, by enabling price increases in the internal market that are above the ones observed for the unit revenue for exports.