The University of Nottingham

Leverhulme Centre
for Research on Globalisation and Economic Policy

Research paper media briefing

Exchange rates and Exporting

Evidence from Manufacturing Firms in the UK

by David Greenaway, Richard Kneller and Xufei Zhang

Key Findings:

- Changes in exchange rates have only modest impact on total UK manufacturing exports
- Exchange rates don't affect firms' decisions to enter or exit export market
- Export levels of multi-nationals are not affected by exchange rates at all
- Export levels of domestic firms are affected - by 1.28% for every 1% change in an index

The most comprehensive research of its kind carried out into the relationship between exchange rates and exporting in the UK.

Some of the main findings in detail:

Exchange rates have little impact on UK exports

Changes in exchange rates have only a modest impact on UK manufacturing exports and will do little to reduce the country's record trade deficit.

To export or not to export?

The research showed that changes in exchange rates have no impact on a manufaturer's decision over whether to start - or stop - exporting.

Report co-author, Dr Richard Kneller, said: "Sterling is very strong at the moment and you do hear people arguing that this is why we have such a large trade gap. But our research indicates that a drop in the value of the pound will not suddenly persuade British manufacturers to get out their foreign phrase books and start tyring to sell overseas."

Multi-nationals

The analysis showed that changes in exchange rates make no difference to the level of exports of multi-nationals based in the UK.

Dr Kneller said: "It would appear that multi-nationals are better able to internalise and offset currency risks. In the last few years there has been a huge amount of foreign direct investment in the UK, which means that multi-nationals now account for at least a third of total UK exports."

So who is affected?

The research suggests that domestic, or indigenous, UK firms are affected most by exchange rate movements. For every one-percent increase in an exchange rate index a firm's exports will drop by 1.28 percent. Typically in a year exchange rate indices change between 3 and 10 index points.

Dr Kneller said: "You have to put this into context - on average exports account for just 5.6% of a domestic UK manufacturer's business; so, on average, a 10 point change in the exchange rate index will make about half a percent difference to total sales for a firm. "

Conclusion

In December 2006 the UK imported £6.9 billion worth of goods more than it exported. Last year the UK's deficit on goods and services was £43.3 billion for the year as a whole, compared with a deficit of £29.2 billion in the previous year. The deficit in goods was £83 billion.

Dr Kneller says: "Our findings may surprise many people - intuitively you would expect a strong pound to be bad for exports and a weak pound to lead to much greater exports, but this research shows a different picture. It means those concerned about the size of the trade deficit should not see a devaluation of sterling as a magic bullet solution to closing the gap."

Pre-Doctoral Research Fellow, Xufei Zhang, said: "Nominal and real exchange rates have fluctuated significantly since the early 1970s, following the breakdown of the Bretton Woods System. Greater volatility has led to increased interest in the effects of exchange rate movements on international trade. The UK is the fifth largest exporter of merchandise globally, so this matters."

Process

The GEP team analysed exchange rate movements and export patterns of 23,171 UK manufacturing companies over a 17 year period from 1987 to 2004.

Xufei Zhang said: "Earlier studies in the UK failed to establish a link between exchange rate movements and export levels but our research, by distinguishing between domestic and multinational firms, has identified what impact exchange rate movements have."

GEP - the Globalisation and Economic Policy Centre - is the major centre in Europe studying the impacts of globalisation and economic policy, and one of the biggest of its kind in the world. The centre has an impressive international reputation; its academics have advised the Treasury, the OECD, the World Bank and WTO.

GEP is keen to promote its research work and is committed to communicating its expertise through the media and to assisting journalists whenever able.

GEP is based at the University of Nottingham and is substantially funded by grants from The Leverhulme Trust.

Website: www.gep.org.uk

GEP Academics:

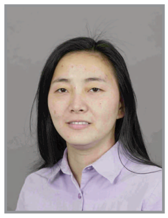
Professor David Greenaway
Professor of Economics and GEP Director

David Greenaway is one of the world's leading experts on globalisation – and has a particular interest in China. His research interests lie primarily in the fields of exporting and productivity, cross-border investment and international trade and economic development. At various times he has been a consultant to the World Bank, UNIDO, UNCTAD, European Commission, GATT, UNECE and HM Treasury.

Dr Richard Kneller
Associate Professor in Economics

Richard Kneller's research interests include cross-country comparisons of productivity and economic growth as well as the impact of globalisation on individual firms. He is currently researching how government and social institutions can encourage firms to adopt new technology and how new technological developments spread across the world.

Xufei Zhang
Pre-Doctoral Research Fellow



Xufei (Florence) Zhang is a research student funded by the Leverhulme Trust and the University whose thesis focuses on firm level responses to globalisation.

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