

Exporters' Resilience?

Attention has been focused upon the fall of the US dollar. But on the flip side, interest is now being shown in the economic consequences of a rising Euro. Since 2002, the value of the Euro has risen from \$0.80, to \$1.40, or a rise of 75%. Eurozone exporters and politicians alike are beginning to worry about the impact of this rise on exports.

Such is the concern that the French even went as far as raising the question of whether, or not, an exchange rate target should be set for the Euro. While such a system may help to prevent a rising currency choking off external demand, the real reason behind the French proposal was perhaps a back door means of gaining some power over the interest rate setters within the European Central Bank.

If the rising value of the Euro is a concern for exporters, then with the greatest exposure to exports, Germany might be considered to have the most to lose. However, this does not appear to be the case this time. First, while it remains to be seen whether parts of the world economy are decoupling from the US, it has been clear for sometime that economies in South East Asia and the emerging economies of Europe have been helping to drive the growth in world exports. In fact in Europe, the US has contributed less than half the growth in exports since 1999. Therefore, since many of these fast growing economies are also seeing rises against the dollar, their changes against the Euro have been relatively modest. Plus, since these economies are growing, they often need to invest in capital-intensive production processes – which generally involves capital machinery and control systems – something which the Germans excel in providing.

The resilience of German exporters is not only down to the decoupling of the world economy. Some German companies have adopted their practices in order to hedge exchange rate risks. The main automobile manufacturers, such as BMW and Volkswagen are known to use forward currency contracts. However, this has not prevented Volkswagen from losing in excess of \$1bn per annum due to the rising value of the Euro. In fact each one cent rise in the Euro is thought to cost German auto manufacturers \$50m per annum. To address this problem, car makers are trying to internationalize more. At present BMW sell 200,000 more cars per year in the US, than

they manage to make in the US. Even for those cars that are assembled in the US, up to 40% of the value of the car can still be imported from Germany. Overall, the US accounts for 9% of BMW's purchasing and about 25% of sales, while Europe accounts for 84% of purchasing and only half of sales. Estimates by BMW, suggest that Toyota have a 40% cost advantage over BMW by virtue of concentrating more of their production and purchasing in the US. Therefore, until BMW diversifies its production and purchasing base from within Europe, it will continue to suffer the consequences of floating exchange rates.

Questions

1. Explain whether a rising exchange rate is good or bad news for exporters.
2. Given the growing importance of the Eurozone and the emerging economies of China, India and Russia, should the world remain fixated about the value of the US dollar?
3. Can you think of other industries where international production and purchasing are the norm?