ESTIMATING THE EFFECT OF THE REAL EXCHANGE RATE ON CHILE'S AGRICULTURAL EXPORTS TO THE UNITED STATES

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ABSTRACT

Chile is a small economy and opened to the international market, which has currently free trade access to 59 countries (equivalent to a market size of 85.7% of the world's GDP). Chile has presented very strong macro-financial and fiscal stability, becoming one of the most important emerging market economies. The country heavily relies on the production of copper, representing more than 50% of the export basket. Since the beginning of this century, a new international macroeconomic environment has been in place, where dramatic rises in copper prices and an unprecedented growth of China economy have occurred. Due to the copper boom, Chilean economy might be affected by the "Dutch Disease", compromising economic and social variables. One of the signs the Dutch disease may be the significant deterioration of the Real Exchange Rate (RER). Agricultural exporters are concerned because there is evidence suggesting that the appreciation of the real exchange rate will tend to diminish agricultural exports and deteriorate the competitive trade position of a particular economy. The present study was undertaken to determine whether the real exchange rate has an effect on Chile's agricultural exports to the United States over the period between 1992 and 2011. The study analyzes through a log-log OLS model using time series data sets from Chilean and United States' sources, on a monthly and quarterly basis.

The research concludes from the econometric analysis that Chile's agricultural exports to the United States are inelastic to changes in the real exchange rate. Even more, the effect of real exchange rate on bilateral exports is not statistically significant in three of the four models under study. No evidence was founded supporting that agricultural exports would be more responsive to changes in the specific sector of the agricultural bilateral real exchange rate than to changes in the general exchange rate, as the first one is more volatile. Furthermore, the analysis suggests that Chile's agricultural exports to the United States seem to have a significant and relatively elastic response to changes in the real GDP of the United States, being an important variable which has been influencing real agricultural

exports. Finally, analyzing the effect of the real exchange rate on aggregate agricultural exports and measuring the differences across the main sub-sectors will be desirable in the future research agenda. Furthermore, it will be worth measuring the indirect effect of the real exchange rate on agricultural exports by analyzing it due to its effect on the price incentive structure rather than as a direct explanatory variable. Thereby more accurate policy could be recommended.