

Exchange rate in Brazil: a macroeconomic assessment on the first ten years of free floating policy during the Plano Real

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Just to remember I:

- Plano Real was a set of measures to stabilize the Brazilian economy in 1994.
- Between 1994-1998 we had a quasi-fixed exchange rate.
- From 1999 on, we have a floating exchange rate.

Just to remember II:

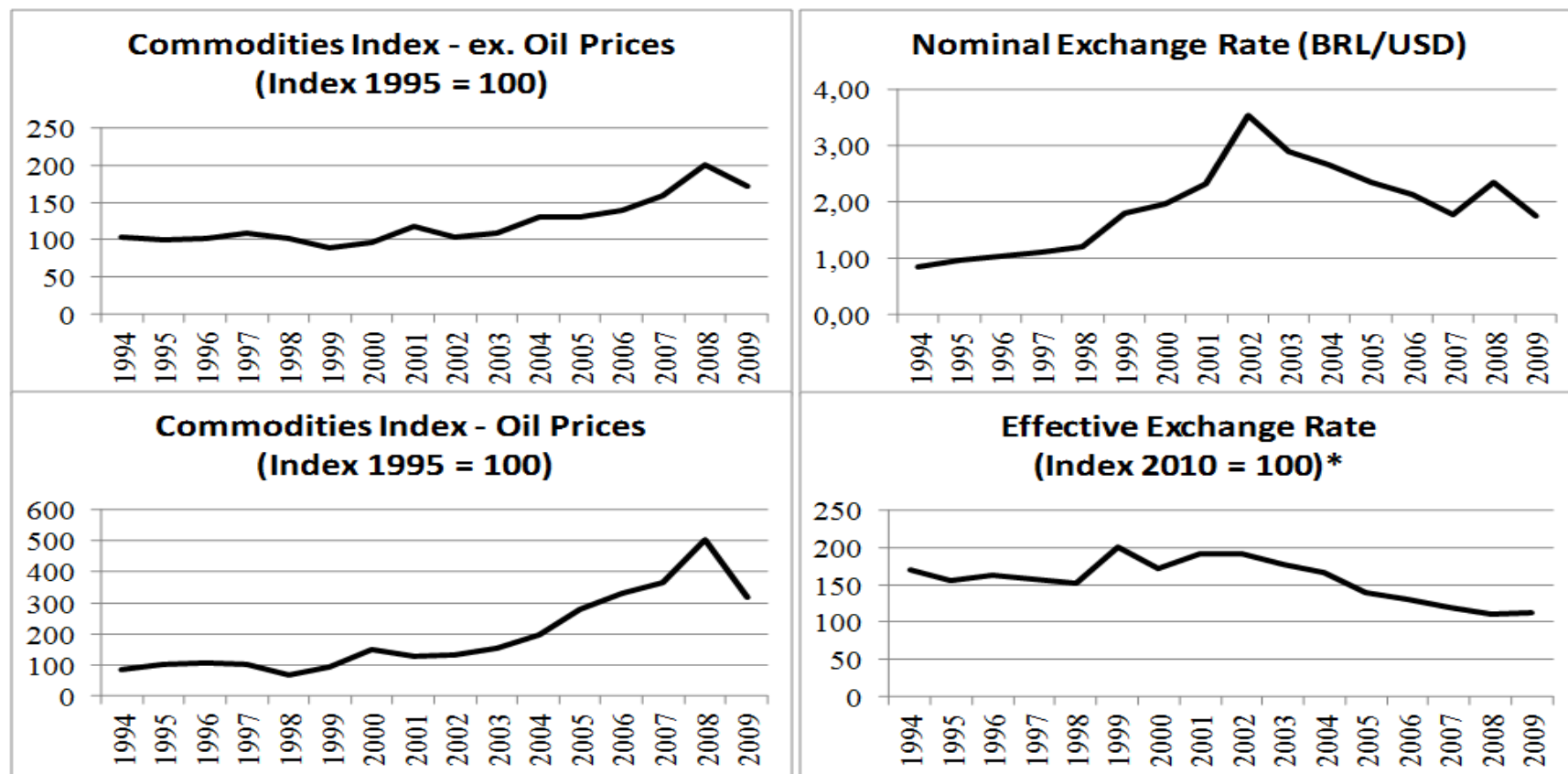
- **Main purpose of New Developmentalism concerning Exchange Rate:**
- “Competitive exchange rate is a condition to promote profits, capital accumulation of potential firms and the economic growth!”

According to the official data, we can see, at the same time:

...the rise of commodities prices

...and the overvaluation of Brazilian currency

Chart 1. Brazilian Exchange Rate (Nominal¹ and Effective) and Commodities Prices



Source: Brazilian Central Bank (BCB), IPEADATA and Commodities Research Bureau (CRB).

¹National currency against US Dollar (end of period).

* Effective Exchange Rate: Prepared by IPEA. Weighted arithmetic average of the bilateral effective exchange rates in the country compared to 24 selected trading partners. The bilateral effective exchange rate is defined by the ratio between the nominal exchange rate (BRL / unit of foreign currency) and the ratio between the price index Wholesale Prices (IPA-EP-DI / FGV) of Brazil and the Producer Price Index (PPI) of the country in the event. The weights used vary each year, and obtained by the participation of each partner in the total Brazilian exports to the countries considered in the two years immediately preceding. For details of the methodology: Effective Exchange Rate. Obs.: The methodology was updated and revised in October 2015, involving the recalculation of the entire series.

According to the Global Competitiveness Report, from World Economic Forum (WEF) ...

- The main reasons to rise of commodities prices were:
 - World's economic growth* around 5% p.y. (until 2008).
 - High Chinese and Indian demand of Oil, Metal & Mining, Food, Raw Materials, among others.
- The main reasons to Brazilian Competitiveness weaknesses were:
 - High real interest rate, tax burden and labor costs.
 - Lack of infrastructure (Logistics, Energy, Telecom., etc.)
 - Exchange rate overvalued, that harms the exports.

Concerning the Brazilian Industry and Imports:

Regarding the **industry**, there was an increase of 5% between 1994-1998, followed by an increase of 29% between 1999-2009.

Industry General Index*	1994	1998	% Var. (1998/1994)	1999	2009	% Var. (2009/1999)
Quantum**	86.0	90.0	5%	90.0	116.0	29%

The domestic demand was supported by **imports**, that had an increase of 89% between 1994-1998, followed by an increase of 70% between 1999-2009. However, the share of Manufactured goods in imports had grew up.

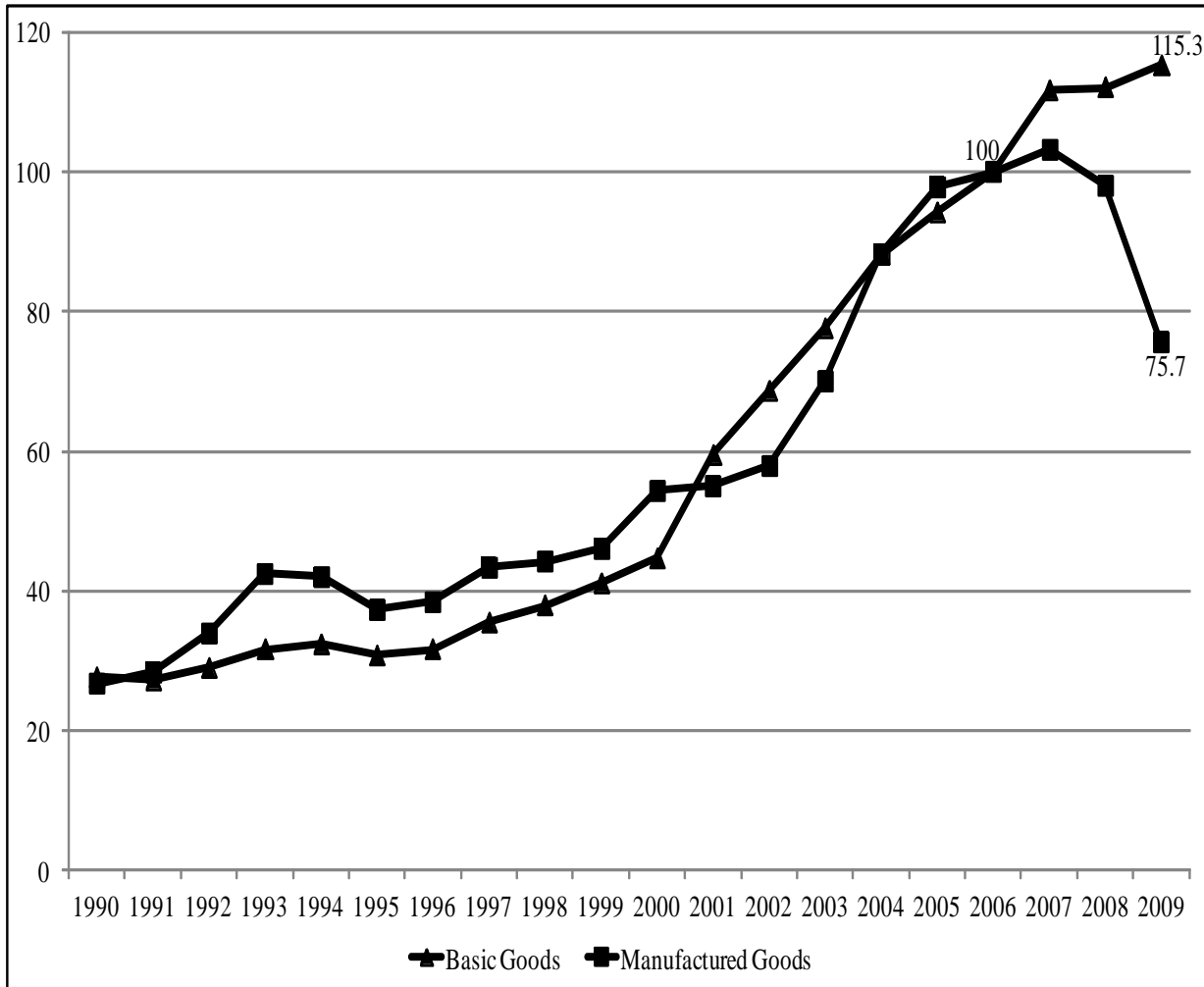
Imports General Index*	1994	1998	% Var. (1998/1994)	1999	2009	% Var. (2009/1999)
Quantum**	43.7	82.5	89%	70.1	119.3	70%

*Index 2006 = 100, Source: – Fundação Centro de Estudos do Comércio Exterior.

** Funcex does not disclosure the data openly of basic and manufactured classes of imports. Funcex only disclosure the subclasses of goods such as capital, intermediate goods, etc, making it impossible to compare with the exports data.

Observing the Brazilian exports performance ...

Chart 2. Brazil: Exports Quantum (average 2006 = 100)



- With **commodity prices** rising and the **overvalued exchange rate** between 2002-2007, we have:
- 15% of **basic goods exports** **increasing** in historical level of external revenues, especially of Oil (Petrobras), Metal & Mining (Vale).
- 24% of **Manufactured exports** **decreasing**, mainly of hi-tech and industrial goods.
- Thus, It is possible to see the **weaknesses in Modern industries!**

According to IMF's data, the main effects of overvalued exchange rate in Brazil were:

- Despite the **inflation** stabilization, we have:
 - The **investment rate** decreasing from 19.7% (1990-98) to 18.4% (1999-2009).
 - With **commodities** exports increasing and **industrial** exports decreasing, the **Brazilian Real GDP** grew up 3.8% p.a. – , against the 10.0% p.y. of **China**, 7.1% p.y. of **India** and 5.6% p.y. of **Russia** in the period 1999-2009.
- In other hand, the **BRICS** countries have used the **exchange rate** to access external demand and promote **economic growth**.

Concluding Remarks

- The **overvalued exchange rate in Brazil in long-run**, including compared to other Developing Countries **has harming the capital accumulation, economic growth and exports in Brazil.**
- In another words, with the rise of commodity prices **between 2002-2007**, Brazilian economy has focusing the basic goods output (Oil, Mining, agricultural goods), instead of manufactured goods.
- Thus, the **weaknesses in Brazilian competitiveness has harmed the industrial output and exports of local value added.**

Thank You!