

Banque de France, AFD et Ferdi

**Politique de change et développement durable
dans les pays à faible revenu**

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Session 2

**Politique de change et répartition
des revenus**

Pierre-Richard Agénor

Université de Manchester et Ferdi



Pierre-Richard Agénor and Luiz A Pereira da Silva



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A photograph of several stacks of coins, likely Euro coins, arranged in a row. The coins are stacked in a way that they appear to be rising from left to right. The image has a blue and green color cast and is slightly blurred, giving it a soft, artistic feel. The text "Integrated inflation targeting" is overlaid on the bottom left of this image.

Integrated inflation targeting

Channels through which Devaluations Affect Income Distribution

- Five possible channels.
 - Inflation and real wages.
 - Relative prices and factor intensities.
 - Fiscal channel.
 - Precautionary saving channel.
 - Financial channel.
- Key issue: dynamic adjustment process (wage adjustment, increased factor mobility, changes in distribution of skills).

Empirical Evidence

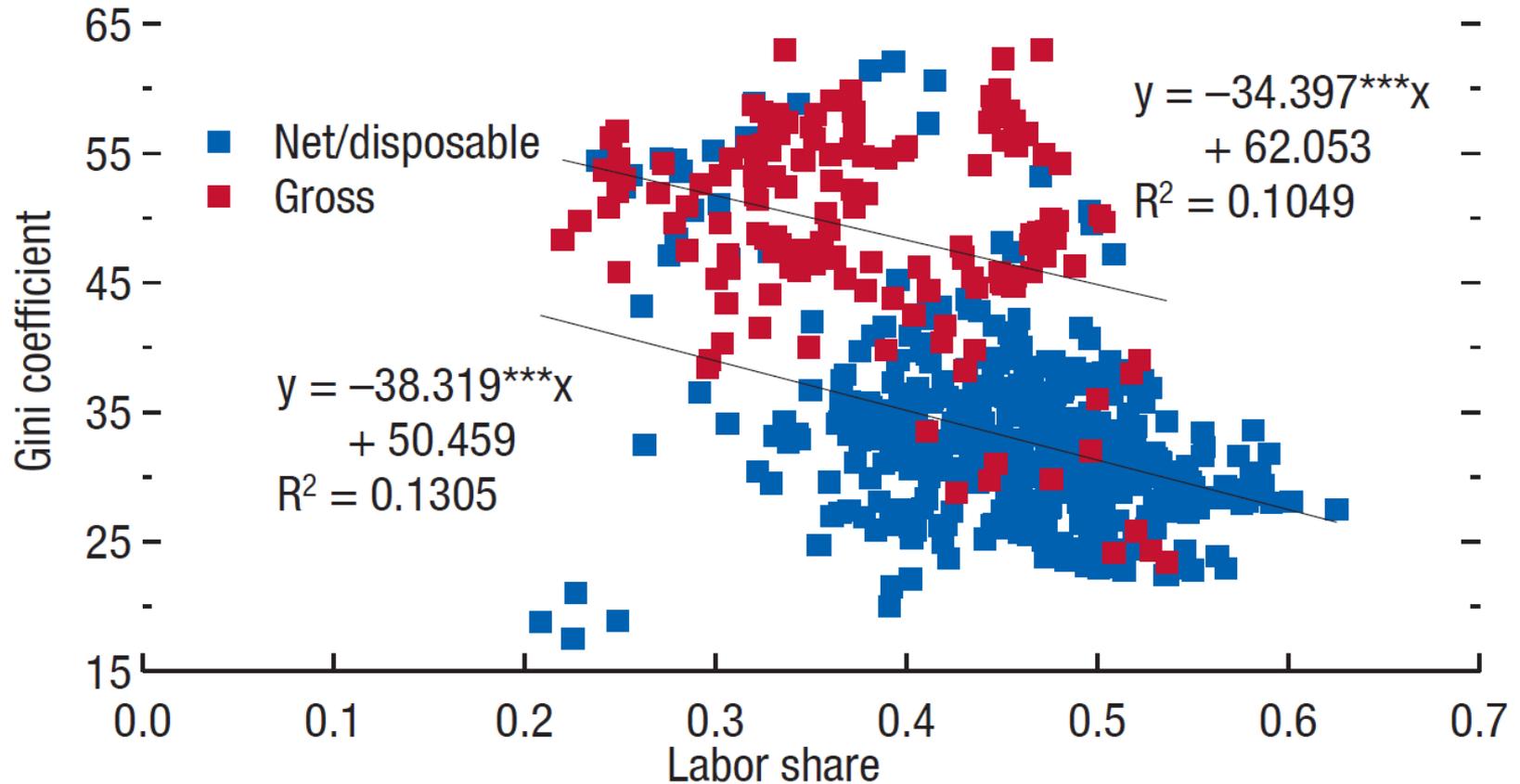
- **Before-after studies** of some major devaluation episodes, using either cross-country time-series data, or country-specific household surveys. Edwards (1989), Azam (2004), Cravino and Levchenko (2017, 2018).
- **Model-based (CGE) studies.** Acharya (2010) for Nepal, Pauw et al. (2013) for Malawi, etc.
- **Time-series econometric studies**, based on “day-to-day” (effective) exchange rate fluctuations.
- Last type is not informative to understand the effects of (large) devaluations.

Before-after studies

Edwards (1989, Chapter 8)

- Data from 31 major devaluation ($> 14\%$) episodes.
- Focus on behavior of the labor share (employee compensation) in GDP.
- In principle, informative about distribution of income between labor and capital.
- Timing of comparison: ± 3 years of event.

Labor Share and Income Inequality across Countries



Source: International Monetary Fund, *World Economic Outlook* (April 2017, p. 122).

- Results: in 15 cases no significant change, in 9 cases significant decline, in 7 significant increase. Difficult to draw general conclusions.

- Changes in the labor share result from changes in the real wage and changes in labor productivity:

$$\text{Labor share} = WL/PY = (W/P)/(Y/L)$$

- W : wages L : employment, Y : GDP, P : GDP deflator.
- Also questionable quality of data; well-known measurement problems (self-employed individuals, depreciation of capital, etc.).

Cravino and Levchenko (2017, 2018)

- Focus: 1994 Mexican peso devaluation.
- Poor households spend relatively more on tradable product categories and consume lower-priced varieties within categories.
- Devaluation raised the prices of consumption baskets of low-income households substantially more than those of high-income households.
- 2-year post-devaluation: sizable effect.

- Problems with B-A studies: difficult to
 - Control for other determinants of inequality (incl. other policy changes).
 - Capture dynamic effects.
 - Problem is magnified for studies based on household surveys (frequency may not match economic time frame).

Final Thoughts

- 1. Empirical literature does provide some support for redistribution against labor (formal and informal sectors) after large devaluations.
- Recent B-A work based on household surveys uses much improved data and techniques.
- However, dynamic effects (highlighted in theoretical literature) are not well accounted for.
- Worth revisiting earlier cross-country B-A studies with larger samples, better data, and more advanced techniques.

- Example: Edwards and Santaella (1993) sample of 48 devaluations.
- Extends Edwards (1989).
- Window of comparison can be varied for sensitivity analysis.
- Cross-country regressions can supplement non-parametric and parametric tests.

- 2. Little focus on impact of devaluations on **gender inequality**. Data issues? Requires disaggregated data on distribution of labor force, factor intensities, wages.
- Some CGE-based simulation studies: devaluation leads to an expansion of activity in agricultural and industrial sectors, and contraction in services.
- If women are over-represented in services, nominal devaluations will not be gender neutral.
- If gender effects are persistent: eventual impact on women's bargaining power in the family.