

Real Exchange Rates Over the Past Two Centuries: How Important is the Harrod-Balassa-Samuelson Effect?

Abstract

Using long-span data on the dollar-sterling and dollar-franc real exchange rates over the past two centuries, we apply the findings of various strands of the recent literature in order to examine the statistical and economic significance of the Harrod-Balassa-Samuelson effect (the effect of productivity differentials on real exchange rates) in a nonlinear context while allowing for shifts in volatility across nominal exchange rate regimes, and the implications for the speed of adjustment. The results indicate significant nonlinearity and volatility shifts corresponding broadly to the classical Gold Standard and Bretton Woods periods, as well as a statistically significant Harrod-Balassa-Samuelson effect, although the dominant influence on real exchange rate movements over the past two centuries nevertheless appears to have been purchasing power parity.

JEL classification: F31, F41, C1.

Keywords: purchasing power parity; real exchange rate; nonlinear dynamics; Harrod-Balassa-Samuelson effect; productivity differentials.

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