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Importers, exporters, and exchange rate disconnect
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One of the most important aspects of the international macroeconomy is the fact that movements in exchange rates only seem to have a limited impact on observed export prices. In other words, a 10 % appreciation of the euro will result in a rise in prices of exports to non-euro countries of less than 10 %. This is known as *'incomplete pass-through'* of exchange rate changes or *'exchange rate disconnect'*.

In this research paper, we show that in order to gain an understanding of this '*exchange rate disconnect'* phenomenon, it is important to take account of the fact that the biggest exporters are also the biggest importers. This finding is of significance for understanding both the low overall '*exchange rate pass-through'* and the variation in '*pass-through'* between exporters.

Using Belgian firm-level data, we demonstrate that exporters who import a large proportion of their inputs tend to pass on a much smaller part of the exchange rate variations in their export prices. Even though most exporters tend to import as well, it is notable that large exporters have a disproportionately bigger import share. Because of this, import-intensive companies have high export market shares and consequently (thanks to their strong market position) can count on high margins as well, which they also actively adjust in response to changes in marginal costs. This leads to a second channel that limits the impact of exchange rate fluctuations on export prices.

A typical small exporter who does not resort to using imported inputs has an almost complete *pass-through* of more than 90 %, while a major exporter with intensive import business has a *pass-through* of only 56 %. The biggest exporters have a large market share and are also import-intensive, which can help to explain the low total *pass-through* and *exchange rate disconnect*.

Understanding why there is an incomplete *pass-through* is important from the welfare economics perspective since the effects differ depending on whether the incomplete *pass-through* is attributable to differences in the distribution of price margins between firms or to complex global sourcing patterns, which in turn influence marginal costs.

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