Credit Constraints, Firm Entry, and Exchange Rate Pass-Through*

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Abstract

This paper builds a two-country heterogeneous firm model with credit constraints and endogenous markups that can account for the exchange rate pass-through behavior. I find different results between the short-run and the long-run exchange rate pass-through. It is shown that the exchange rate pass-through in the short run declines with the level of credit constraints of the exporting country. However, in the long run, where the firm entry occurs, the exchange rate pass-through increases with the level of credit constraints of the exporting country. This difference between the short run and the long run stems from the difference of market structures.

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