Mod 10 Discussion Example 

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**MONETARY ASPECTS OF INTERNATIONAL TRADE by Dr. Pat Bentley,**

**INTRODUCTION**

Module 10 assignment asks us to examine two monetary variables in the global economy which `impact the balance of payment, currency exchange and exchange rate determination. I concluded that the strength and direct of a nation’s currency is significantly influenced by the net of its balance of payments and the level of its interest rates.

**BODY**

The exchange rate is a dynamic calculation published at a point in time. It is a reflection of a nation’s economy in comparison to other countries. Whether one nation’s exchange rate is strong, weak, steady or volatile compared to another country is directly affected by “the generalized balance the real market, the monetary market, the monetary market, and the capital market” (Carmen, p.518). Also affecting the dynamics of a nation’s exchange rate is its economic growth, inflation, competitiveness of the products of the nation, openness of its markets, political stability and effectiveness of the nation’s government. These are measured by a country’s leading economic indicators, many of which are published by a country on at least a monthly basis.

Ghosh and Kallianiotis (2013) analyzed these various leading economic indicators in the US to determine the direct and significance of their influence on the US exchange rate since the recession of 2008. What they found was that the two indicators of the price of oil and the US spot rate had an ***insignificant*** affect on the US exchange rate whereas the increase in the US interest rate and balance of payments (BoP) had a ***significant*** affect on the US exchange rate, with government spending having a positive and significant affect on the BoP. What this means is that when the US interest rates are low and/ or its balance of payments is negative, “international investors are investing in countries with higher return, lower risk, and safety This increase in demand for these (country) assets increases the demand for (that ) currency” (p.7628). To these two economists, the low US interest rates and the increase in US risk, as seen by the deficit in its current account, helps explain the low US foreign exchange since its recovery from the 2008 recession.

Carmen (2008) agreed that the balance of payment is a major determinant of the level and direction of a country’s exchange rate. Studying the exchange rate movements of Romania before and after its entrance into the European Union, he found that “one of the most important factors that influence the foreign exchange rate is the position of the balance of payments” (p.518) Balance of payments (BoP) is also know as ‘net exports’ or the merchandise trade balance. It is calculated as the difference in local currency of merchandise exported from a country, as a positive flow, netted against the merchandise imported into the country, as a negative flow. If the result is positive, that country has more exports than imports and is said to be running a surplus balance of payments. If the result is negative, that country is said to be running a deficit balance of payments.

Besides affecting the exchange rate, as found by Carmen (2008), asked how does the balance of payments effect a domestic economy? Balacescescu and Tomescu- Dumitreascu. (2008), studied the economy of Romania from 1990 to 2000, to find that because that county’s rate of increase in imports were growing faster than the rate of increase in exports, meaning it was carrying a deficit for ten years, Romania had a difficult time securing financing from other countries to support its growth. This period of time studied was significant to Romania because it the time between freeing from the soviet bloc and attempting to become a strong developed county. These researchers found that for Romania from 1990 to 2000, there was a direct relationship between the balance deficit (known to us as the balance of payments) and the absence of foreign investment.

**CONCLUSION**

Ghosh and Kallianiotis (2013) studied the currency in the US since the 2008 recession to find that the economic indices significantly influencing the US exchange rate are the level of its interest rates and the balance of payments. Carmen (2008), studying Romania, seemed to confirm the significance of the balance of payments on exchange rate strength and movement. Balacescescu and Tomescu- Dumitreascu (2008), who also studied the economy of Romania, found a direct relationship between a balance of payment deficit and the inability to secure foreign direct investment, which also seemed to confirm the influence of balance of payments on the demand of a nation’s currency an the level/strength of its currency.

**REFERENCES**

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