61% measures were "trade facilitating"
(39% " " trade Restrictive).

By October 2022, 77% of export restrictions has been repealed
खत्म कर दी

x ———— x ———— x ———— x ———— x

CH 9
Unit 4

Exchange Rates and its Economic effects

① INTRODUCTION

→ A foreign currency transaction that is denominated in or requires settlement in foreign exchange

→ Exchange Rate is the rate at which the currency of one country is exchanged for the currency of another country.

eg. $\boxed{1\$ = ₹ 80}$

1 pen = ₹10
1 pizza = ₹100

→ A direct quote (European Currency Quotation) is the number of units of local currency exchangeable for one unit of foreign currency

$\boxed{₹ 80 / \$}$ ☞ 1 \$ = ₹ 80

→ An indirect quote (American Currency Quotation) is the number of units of foreign currency exchangeable for one unit of local currency

$\boxed{\$ 0.0125 / ₹}$ ☞ 1₹ = 0.0125 \$

② Exchange Rate Regimes (3 Regimes)

(i) $\boxed{\text{Free - Floating exchange Rate System}}$

→ Rate determined by market forces of

- Rate determined by market forces of demand & supply
- NO Government intervention
- Self Regulating ☺
- No need to maintain foreign currency Reserves ☺
- Less stability ☹
- Speculation can be there ☹
- International trades are riskier

(ii) Managed Floating System

- Government & Central Banks often seek to increase or decrease their exchange rates by buying or selling their own currencies.
- Such intervention is likely to have only a small impact.

(iii) Fixed Exchange Rate system

- Set by Government
- Stability ☺
- Less speculation ☺
- Avoids currency fluctuation ☺
- Government has to keep huge foreign currency reserves ☹
- It enhances international trade & Investment ☺

* Basically, free floating exchange rate system is efficient and transparent. It allows Central Bank to pursue its own independent monetary policy ☺

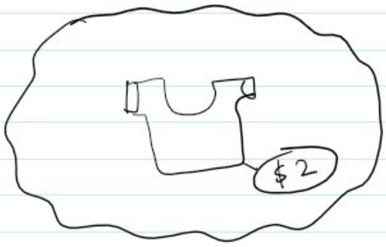
③ Nominal and "Real" exchange Rates

- Nominal exchange rate is expressed in units of

→ Nominal exchange rate is expressed in units of one currency per unit of other currency. A real exchange rate adjusts this for changes in price levels.

→ A real exchange rate is the rate at which a person can trade the goods or services one country for the goods or services of another.

→ $$\boxed{\text{Real exchange Rate} = \frac{\text{Nominal exchange Rate} \times \text{Domestic prices}}{\text{Foreign Prices}}}$$



Nominal exchange Rate

1\$ = ₹1

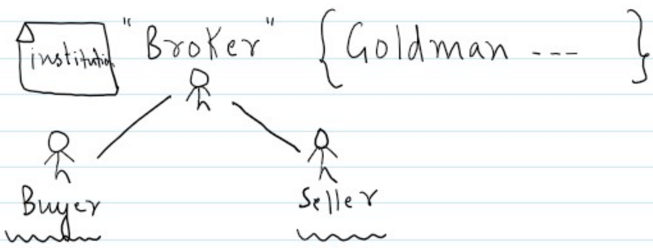
$$\text{Real exchange Rate} = ₹1 \times \frac{5}{2}$$

$$= 2.5$$

$$\boxed{* \ \text{Real effective exchange Rate (REER)} = \frac{\text{Nominal exchange Rate}}{\text{Price deflator}}}$$

(4) Foreign Exchange Market

→ Forex market mainly consists of commercial banks & brokerage houses. (Known as market makers)

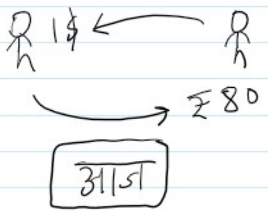


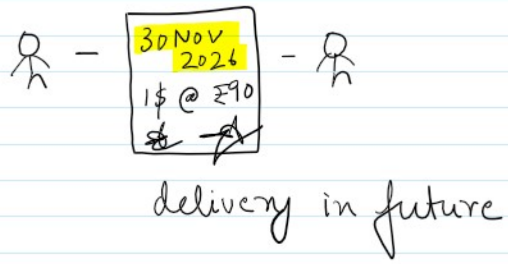
→ In foreign exchange market, there are two types of

→ In foreign exchange market, there are two types of transactions :-

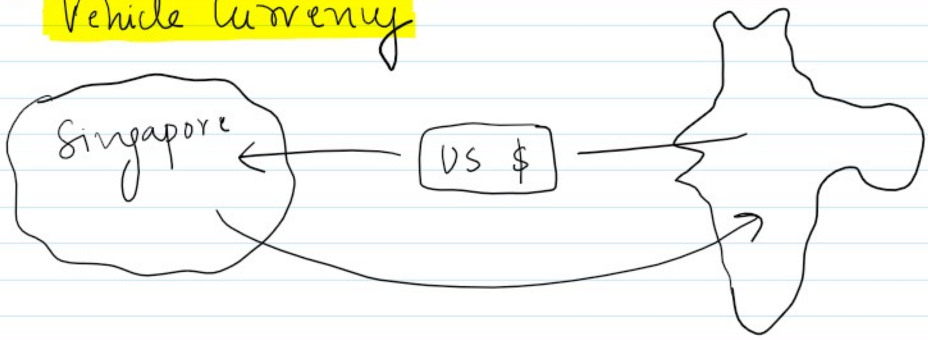
a) currency transactions which are carried out in the spot market and exchange involves immediate delivery

b) future transactions wherein contracts are agreed upon to buy or sell currencies for future delivery which are carried out in forward / future market



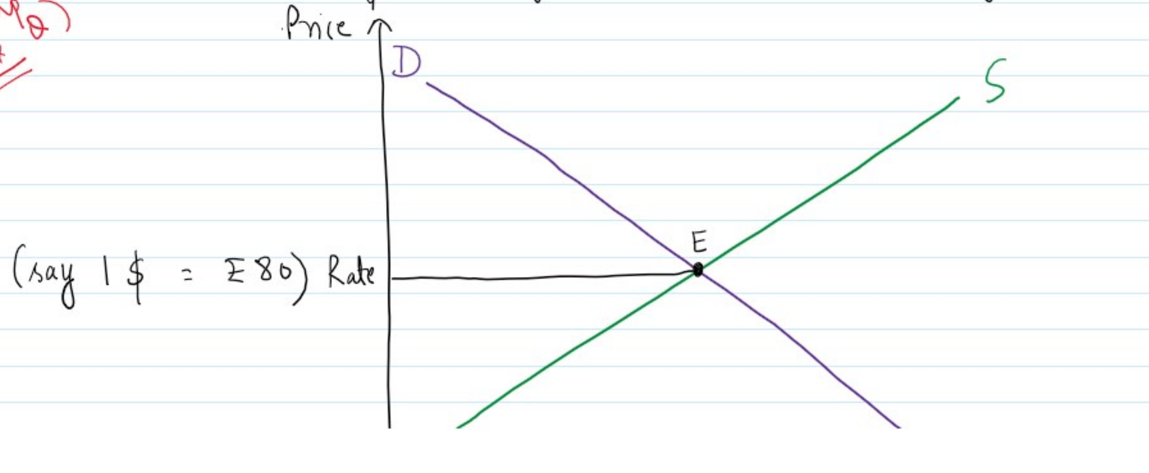


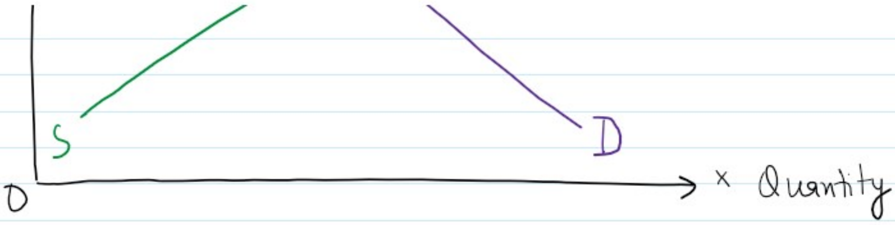
* A foreign exchange transaction can involve any two currencies, but mostly US $ is involved (even though it is not the national currency of either of the countries). Thus, US $ is called "**Vehicle Currency**"



5 Determination of Nominal exchange Rate

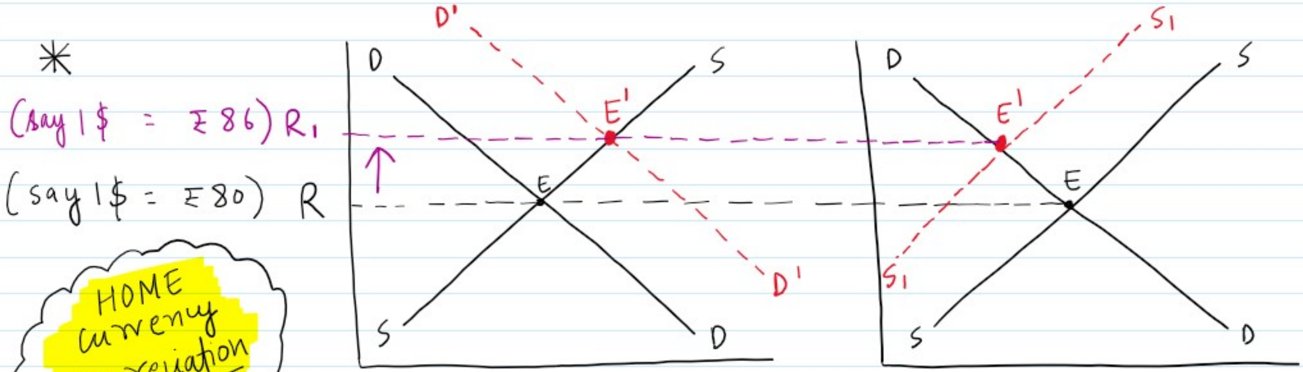
V. Imp. Q
(MAX)





Why demand ? (Why $ is demanded ?)	Why Supply ? (Why inflow of $?)
→ To purchase goods & services from foreign country	→ Exports
→ Foreign Tour	→ Investments by foreigners in our country
→ To send unilateral transfers	→ Unilateral transfer received
→ To make investment in foreign countries	→ Foreigners visiting India
→ To open foreign Bank A/c	→ Speculation
→ For Speculation	etc etc etc
etc etc	

*



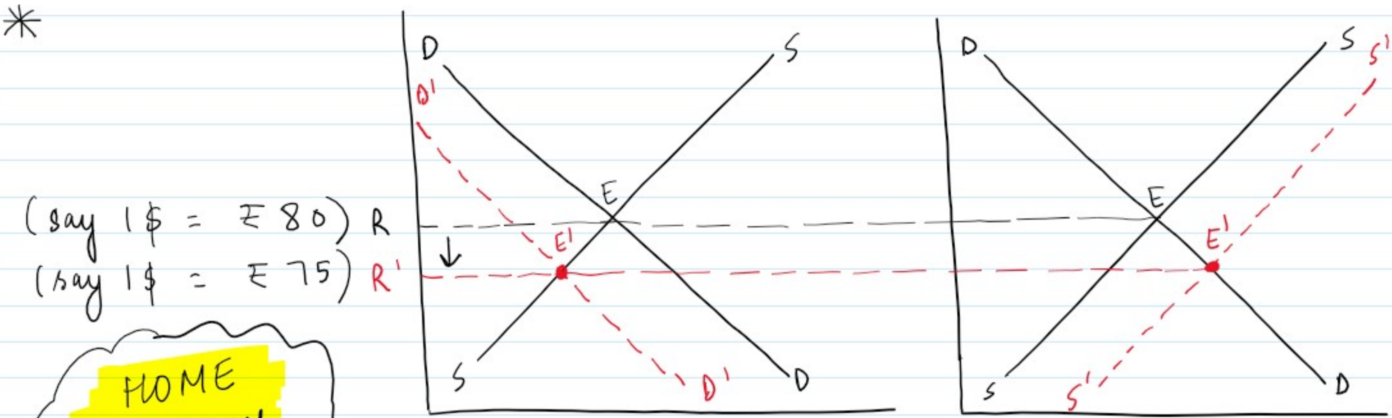
HOME currency Depreciation

" रुपया कमज़ोर "

Increase in Demand*

Decrease in Supply*

*



HOME currency

Home currency Appreciation

(रुपया मजबूत)

Decrease in demand

Increase in Supply

* Effects of Currency Depreciation & Currency Appreciation

Exchange Rate depreciation lowers the relative price of country's exports (export rises), raises the relative price of its imports (import falls), leads to output expansion, encourages economic activity, increases international competitiveness and improves Balance of trade

Currency appreciation raises the price of exports, (decreases export), increases imports, adverse effect on competitiveness, causes larger deficits & worsens the trade balance

(6) Depreciation (Appreciation) VS Devaluation (Revaluation)

Earlier 1 \$ = ₹ 80	Earlier 1\$ = ₹ 80
Now 1 \$ = ₹ 85	Now 1\$ = ₹ 85

Depreciation — रुपया कमज़ोर हो गया — Devaluation

Depreciation: It occurs due to market forces of demand + supply

Devaluation: deliberately done by government

x ——— x ——— x ——— x ——— x

CH 9 Unit 5

International Capital Movements

(1) Foreign Capital

→ Foreign Capital includes any inflow of capital into the home country from abroad