BOP Correcting Methods

Exchange Control

Methods of correcting Adverse Balance of Payments

1. ***Trade Policy Measures***

- *Expanding Exports and Restraining Imports*

2. ***Expenditure Reducing Policies***

- *Tight Monetary Policy*
- *Concretionary Fiscal Policy*

3. ***Expenditure Switching Policies***

- *Devaluation- Marshal- Lerner Condition*
- *Income Absorption Approach to Devaluation*

4. ***Exchange Control***

Exchange Control

- Finally, there is the method of *exchange control*
- As discussed earlier we find that *deflation is dangerous*; devaluation has a temporary effect and may provoke others also to devalue
- *Devaluation* also hits the *prestige of a country*
- These methods are, therefore, *avoided and instead foreign exchange* is controlled by the government

- Under exchange control method, all the exporters are ordered to *surrender* their *foreign exchange* to the central bank of a country and it is then rationed out among the licensed importers

- No one else is allowed to import goods *without a licence*

- The balance of payments is thus rectified by *keeping the imports* within limits

- After the Second War World a *new international institution' International Monetary Fund (IMF)'* was set up for maintaining equilibrium in the balance of payments of member countries for a short term

- IMF also advises member countries how to *correct fundamental disequilibrium* in the balance of Payments when it does arise

- It may, however, be mentioned here that *no country* now needs to be forced into *deflation* (and so depression) to root out the causes underlying disequilibrium as had to be done under the gold standard

- On the contrary, the IMF provides a mechanism by which *changes in the rates of foreign exchange* can be made in an orderly fashion

Conclusion

- In short we can say that no single method will be sufficient for the correction of disequilibrium

- All the following tools and methods should be used judicially

- *Monetary and fiscal changes affecting income and prices in the country;*

- *Exchange rate adjustment, i.e., devaluation or appreciation of the home currency;*

- *Trade restrictions, i.e., tariffs, quotas, etc.;*

- *Exchange control*

- *No reliance* can be placed on *any single tool*
- There is room for *more than one approach* and for more than one device
- But the application of the tools depends on the *nature of the disequilibrium*

Thank You