

Theme:

“On Using Exchange Rate for Promoting Exports”

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Abstract:

In recent years, Pakistani exports suffered large setback and especially textile exports decreased significantly. Some economists are suggesting devaluation of Pakistani Rupee to improve the exports (Javed et al, 2016). Many countries including Pakistan have experimented devaluation in the past to boost exports, but most of these experiment did not bring desired results and a significant change in the balance of trade could not be observed. For example, value of Pakistani rupee declined by 20% during 1981-82 and by 34% during 2007-09. No improvement in trade could be observed after each episode of depreciation, on contrary, the gap between exports and imports widened. There are well known explanations in contemporary economic literature which explain this counterproductive impact of depreciation. However, analyzing the impacts of depreciation and/or devaluation in context of trade only is never justifiable. The depreciation of local currency has serious implications for many other important economic indicators including external debt, tax revenue, budget deficit, current account deficit and domestic inflation. For example, a one percent reduction in value of local currency ‘causes’ an increase in external debt by the same percentage, measured in local currency. Due to this increase in the external debt, the amount needed for debt servicing shall also increase which increases the budget deficit and the current account deficits. The suggestion of depreciation could be supported only if the sum of expected gains from all kinds of its impacts are positive. Given the complexity of all this estimation, one can focus on external debt and balance of trade. The effect of depreciation on external debt can be easily counted, and the improvement in trade must be more than the increase in external debt to justify depreciation. Taking into account all these factors, particularly the debt factor, it could be easily seen that net impacts of devaluation are negative and extremely harmful for the Pakistan Economy.