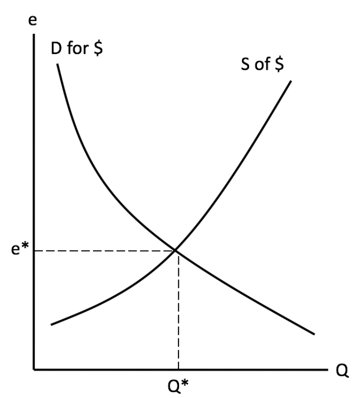
EE312 Macroeconomics, 2/2019 (Sec. 046402/ Sicha)
Chapter 5. Balance of Payments and Foreign Exchange Rate Market

1. Balance of Payments :
   - BP account [Current Account (CA), Capital Account (KA), International Reserve Account (IR)]
   - Balance of Payments = CA + KA
2. Real Exchange Rate VS. Nominal Exchange Rate : Real Exchange Rate $=\dfrac{eP^*}{P}$
3. Long Run Theory : no arbitrage condition
   - Purchasing Power Parity : $P = P^* \times e$, $e = \dfrac{P}{P^*}$
4. **Short-Run Theory : Demand and Supply**

	Demand for FX	Supply of FX
Source	$(1+r)\ldots\ldots\dfrac{(1+r^*)e_{t+1}}{e_t}$	$(1+r)\ldots\ldots\dfrac{(1+r^*)e_{t+1}}{e_t}$
FX Intervention		
e		

5. Exchange Rate Market Equilibrium



   - Flexible Exchange rate regime
     - At Equilibrium, BP = 0
     - Above E. BP 0
     - Below E. BP 0
   - Fixed Exchange rate regime
     - Central Bank intervention

6. Intervention Fixed Exchange Rate Regime
   - $e^f < e^*$ ⇒ Central Bank ....\$(⇒ .... \$ ↑)
     ⇒ Baht flow .... the market ⇒ Money Supply .... ⇒ LM shifts to the ....
   - $e^f > e^*$ ⇒ Central Bank ....\$(⇒ .... \$ ↑)
     ⇒Baht flow .... the market ⇒ Money Supply ....
7. Evaluation : (CH6)

Fixed Exchange Rate Regime	**Flexible Exchange Rate Regime**
* No exchange rate risk, no FX hedging in trade. * No currency speculation.	* Policy independence * The FX market clears and BP = 0 * Insulation from real foreign shocks
* Potential conflict between internal and external balances. * No insulation from external shocks ⇒ required policy response to shocks ⇒ loss of foreign exchange reserve ⇒ cost of devaluation	* Exchange rate risk and uncertainty in trade * FX Hedging is costly. * FX speculation exists. * Exchange rate fluctuations : Resources move in/out export sectors constantly. // Rising exchange rate means higher domestic inflation (rising import prices)// Falling exchange rate reduces competitive exports.