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ISSUES OF MANAGEMENT AND ENHANCEMENT OF EFFICIENCY OF ECONOMIC PROCESSES AFFECTING THE BALANCE OF PAYMENTS

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Abstract

It can be concluded that the analysis of the balance of payments allows to draw conclusions on overall economic situation of the country (including the exchange rate stability), assess the existing external and internal economic risks, and forecast future developments. Dynamic review of movements in the balance of payments allows assessing changes in the poverty level in the country as well.

Keywords: Economic relations, balance of payments, economic transaction, income, transfer.

Economic relations of a country with other countries are reflected in the balance of payments. The balance of payments is an important source of information about the country's engagement in international economic relations. It makes possible to identify the extent and quality of the country's engagement in the system of foreign economic relations. The balance of payments shows financial position of each country in the system of international economic relations. The balance of payments is a document where for a certain period of time (year, quarter, month) all the payments (expenses) and receipts (income) associated with foreign economic activities of the given country are accounted for.

The balance of payments is a document where for a certain period of time (year, quarter, month) all the payments (expenses) and receipts (income) associated with foreign economic activities of the given country are accounted for [2]. It shows financial position of each country in the system of international

economic relations. As it can be seen from the definition, the balance of payments reflects external economic transactions with goods, services, income, transfers and finance, which are performed between the residents of the given country and residents of other countries within certain period of time [1]. If a country has closed economy, that is, it does not have relations with any other country, it means it does not have the balance of payments. However, in modern conditions, the existence of such a country is expressly excluded. Whenever a country begins to operate in an open regime, meaning it sells something (exports), buys something (imports), borrows or lends, uses or provides information, energy, transport, tourism and other services, that is, enters into international economic relations with other countries, it must have the balance of payments [4]. This evidences that the balance of payments is an economic category that shows the entirety of international economic relations established between the country and the world community.

The balance of payments reflects aggregate transactions between the given country and other countries, rather than individual transactions. Since the balance of payments characterizes financial position of the given country in the system of international economic relations, it becomes an important orienting point for development of macroeconomic policy. This refers especially to fiscal, monetary, foreign trade, currency and other policies. In addition, the balance of payments is basically one of the tools of macroeconomic analysis and forecasting. It helps to find out how foreign trade has been developed over a certain period of time. The balance of payments has a direct impact on production, employment, consumption and exchange rates. The balance of payments allows following the forms of attraction of foreign investments, investments made aboard, timely repayment of foreign debt of the country, etc. At the same time, it shows how the country's central bank has changed the level of its international reserves, the imbalance of payments [6].

The balance of payments is always in accounting equilibrium, but it is not in the state of balance at all times. The balance of payments is equilibrated. Otherwise, when the balance of payments is imbalanced, the economy should be subject to changes in price levels, income, foreign currency exchange rates and other economic variables in order to recover stable relations with the rest of the world. The idea of equilibrium of the balance of payments is an idea of market self-regulation. Therefore, official measures undertaken to control international transactions do not eliminate the deficit of the balance of payments, but simply put pressure on it.

The most helpful balances used for the analysis of the balance of payments are the following three ones:

- current account balance;

- main transactions balance;
- official reserves transactions balance.

In general, over a short period of time the volumes of exports and imports slightly respond to changes in national currency exchange rate. Therefore, during devaluation of national currency, the balance of foreign trade balance deteriorates in the months following the devaluation, and only after a certain period of time an inverse trend emerges, that is, improvement is observed. As a result of changes in the exchange rate, the accounts of the balance of services and balance of transactions with capital will be changed in the same direction and proportion as the volumes of exports and imports, which are served by these services. For example, payments associated with tourism are quite sensitive to changes in domestic prices and depend also on changes in national currency exchange rate. It is quite difficult to assess the impact of changes in exchange rates on capital flows since some forms of international lending are associated with financing of foreign trade operations, therefore, flows of these capital flows will be changed along and in compliance with exports and imports. These forms of capital flows are associated with changes in exchange rates indirectly. At the same time, due to significant depreciation in the exchange rate, the increase of FDI flow can be expected, since appropriate resources necessary for organization of production or economic activity become more accessible to the foreign investor. Moreover, devaluation of national currency restricts import, and the FDI allow foreign firms to bypass foreign trade, economic and currency restrictions of the given country and more easily take on its domestic market.

Now let us explain in more detail how the exchange rate affects the balance of payments [5].

Suppose the USA GDP grows and as a result, the demand for import at this exchange rate is increasing. The balance of payments is not equal to zero only in case the central bank makes interventions by selling foreign currency at the amount equal to total deficit of current account balance and capital flow balance. However, if the central bank does not intervene, foreign currency exchange rate changes in a way to ensure the equilibrium of the balance of payments.

Increase in import expenses against export income ensures new equilibrium of the trademark price denominated in US dollar. Growing import expenses lead to depreciation of US dollar, which in its turn recovers the balance of payments in two ways. On the one hand, it reduces import expenses by making foreign goods more expensive as compared to ours. On the other hand, it also ensures growth of our export competitiveness. By this depreciation of US dollar increases export income and, consequently, helps to finance the

increased import expenses.

Thus, with the help of the absolute flexible exchange rate the balance of payments is mechanically regulated by making the demand for foreign currency conditioned by import expenses equal to foreign currency supply conditioned by export income.

Analysis of international lending and borrowing (and speculations) is fraught with difficulties. However, as the main principle flexible (floating) exchange rates remain, which are considered to be the mechanical tool of regulation of the balance of payments. In this case, there is no need for the state to interfere to ensure the foreign trade balance. For the balance between import expenses and export income to be regulated, exchange rate is mechanically changed. A completely different, but again mechanical tool functions under the conditions of fixed exchange rate. As a striking example of fixed currency system is the gold standard. The three basic rules of the gold standard are as follows:

- The state fixes the gold price and hence its monetary unit expressed in gold. The parity value of gold is the price set by the state for gold expressed in national currency. For example, from 1933 to 1960s, the parity value of gold or the dollar-denominated price was set at US dollar 30 per one ounce.
- The state assists in converting domestic currency into gold. In other words, the state is obliged to buy or sell domestic currency at parity value.
- The state supports the gold security or 100% compensation policy. That is to say, it maintains gold reserve equal to the value of money in circulation. The state creates money only when it buys gold from population, and destroys it only when sells gold to population.

Since the idea of 100% compensation is considered to be the key element of the monetary system, which is based on the gold standard, it is also worth noticing.

Modern central banks usually do not practice bank deposits. All foreign assets are in gold, rather than in foreign currency. The central bank holds only gold, which it obtains by putting money into circulation.

Let us go back to the gold standard. Suppose the population decides to buy gold from the central bank for US dollar 100. In case of 100% compensation, the state loses US dollar 100 in gold and also reduces its liabilities (quantity of banknotes) by the same amount, since when the state sells gold, it is paid for it in banknotes (and therefore these amounts are stored or destroyed). Thus, the reduction of gold reserve in the central bank leads to decrease of quantity of money in circulation.

As we can see, this mechanism guarantees mechanical regulation of the

balance of payments by the influence of the exchange rate. Now let us see what happens when the initial balance of payments equals to zero. In this case, the adaptation mechanism of the balance of payments is also considered, which guarantees the regulation of the balance of payments [3].

In due course, the deficit of the balance of payments is mechanically regulated. When importers buy gold from the federal reserve system, the USA stock of money decreases. Gold is sent to England and is exchanged for pound sterling. In order to buy gold, the bank of England should print more currency, which leads to increase in stock of money in Britain. Consequently, the deficit of the USA balance of payments mechanically results in reduction of money stock in circulation in the USA and its increase in the Great Britain.

Changes in money supply in their turn affect the spending level. Reduction of money stock in the USA leads to increase of interest rates and decrease of expenses, whereas the decrease of interests rates results in increase of the spending level. These changes in expenses in their turn affect currency market. Under the conditions of the gold standard, the process of mechanical regulation does not happen at once. Certain period of time is required for the loss of gold and decrease of money supply in the countries having deficit to reduce import expenses, and for the increase of money supply and flow of gold in the countries with positive balance to increase import expenses. This process continues until the existing deficit is eliminated. The process is considered to be mechanical since by simply observing three basic rules of the gold standard the balance of payments is finally regulated under the influence of the exchange rate.

Thus, in case of floating exchange rates, the exchange rate changes in a way that it eliminates any deficit or positive balance of current balance of payments and equates the demand for foreign currency conditioned by import to the supply of foreign currency ensured by export.

The process of regulation of the balance of payments by the exchange rate influence takes place without the interference of the state.

The country's balance of payments cannot remain in an imbalanced state for an indefinite period of time. Its regulation can take several forms. In the short run, in case of deficit of official reserves the country can attract short-term capital. However, if the deficit is maintained, the country has to arrange for the regulation in the following three ways:

1) by internal deflation of prices and income against foreign prices and income,

2) by depreciation of foreign currency exchange rate;

3) by establishing foreign currency and trade control.

The first two methods of regulation work through market processes,

including changes in income, prices, foreign currency exchange rates, money supply, interest rates and other economic phenomena. Market self-regulation, however, does not imply a lack of government actions. Successful market self-regulation depends on fiscal and monetary policies aimed at strengthening of balancing market forces. Fiscal and monetary policies of the state can also counteract the balancing effects by introducing misbalancing changes in income, prices, etc., unless they supplement the market self-regulation mechanism.

Non-market regulation is in sharp contradiction with market regulation. State control and supervisory tools replace the market in the pressure of external imbalances. Controlled self-regulation is not a genuine (true) self-regulation. Although imbalance symptoms are eliminated through direct control, the reasons for the imbalance (cyclic, structural, etc.) remain unaffected. The result is a suppressed imbalance. Suppressed imbalance is usually the outcome of application of import quotas and foreign currency restrictions.

Before joining the EAEU, in the relations with the outside world Armenia was considered to be a country with open economy, which meant that economic inflows and outflows were liberalized as far as possible. From 1991, Armenia implemented market reforms by focusing on trade liberalization. In 2003 Armenia joined the WTO. Before becoming a member of the EAEU, a completely free regime was established in Armenia for trade of goods and services, capital and investment flows; commodity markets were accessible both within the country and within the meaning of formal border crossing procedures, there were no legislative restrictions on the inflow of foreign capital, and regimes contributing to the establishment of internal, maximum favorable conditions and return on capital and income for foreign investments were envisaged. However, at present serious restrictions and risks have emerged for continuation of this policy. Being one of the weakest items in the world economy in structural, technological and administrative aspects, Armenia at the same time has appeared in the EAEU zone, which means that Armenia cannot enjoy the advantages of open economy. In fact, by simplifying the movement of goods, services, capital and labor force in its zone, the EAEU set restrictions on them in the relations with the rest of the world. At the same time, being the country with open economy, Armenia's economy responds rapidly to economic developments in the countries on which it is economically dependent.

Thus, it can be concluded that the analysis of the balance of payments allows to draw conclusions on overall economic situation of the country (including the exchange rate stability), assess the existing external and internal economic risks, and forecast future developments. Dynamic review of

movements in the balance of payments allows assessing changes in the poverty level in the country as well.

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