Account of elasticities of demand for the devaluing

Account must also be taken of the elasticities of demand and supply of the goods entering into external trade of the devaluing country, and elasticities of even those goods which have the potential of entering the trade subsequent to devaluation. 3. Composition of Trade: Success of devaluation is closely related to the nature of imports and exports of a country. A country may not be able to produce substitutes of some of its imports. Similarly, devaluation is not likely to result in a substantial reduction in the import of essential consumption goods like food, medicines and energy inputs. In their case, devaluation may only add to the difficulties faced by domestic producers and consumers. Besides, devaluation may fail to bring about a sufficient increase in the exports earnings of the devaluing country.

4. Elasticities: According to Marshall-Lerner condition, devaluation can succeed in improving the BOT only if the sum of elasticities of demand for the devaluing country's exports and imports exceeds unity. 5. Non-Selective: Devaluation has the immediate impact of changing the prices of all traded items by a given proportion. As a result, the devaluing country may incur unnecessary losses of export earnings in respect of commodities or products which have an inelastic demand. 6. Reaction of Trading Partners: There is the risk of competitive or retaliatory devaluation or price cuts by other countries.

To the extent that happens, the gains of devaluation are lost. 7. Supporting Measures: Devaluation brings about a sudden and arbitrary revision in export and import prices, and this, in turn, necessitates several compensatory (corrective) or supportive measures in the areas of taxation, subsidies, regulatory procedures relating to external trade, and so on. 8. Speculative

Activities: Impact of devaluation also depends upon the expectation regarding subsequent measures by the authorities. For example, if the market expects that the current devaluation will be followed by another, it may generate speculative flows of capital and/or trade transactions.

9. Non-repetitive: Devaluation is a measure which cannot be used repeatedly. In case of a repeated use, it can generate counter-productive expectations. 10. Self-defeating: Depending upon the flexibility and other characteristics of the devaluing economy, devaluation may lead to an inflationary price rise in the country. In case that happens, devaluation can be self-defeating and result in a further deterioration of BOP.

11. External Indebtedness: To the extent a country’s external debt is denominated in foreign currencies, cost of debt servicing (measured in home currency) goes up.