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ASSIGNMENT

1. Foreign exchange management is the core issue in international finance. DISCUSS

FOREIGN EXCHANGE can be defined as the transformation of one currency into another which is acceptable for the settlement of debts in international transactions. The value of a countries currency is based on the demand and supply. For instance, if there is high demand of oil in Nigeria and America wants to import more from Nigeria they will have to change more dollar into Naira to be able to purchases crude oil which is called foreign exchange rate. Therefore, foreign exchange management affects the importation and exportation of goods this is because importers and exporters need foreign currency in other to complete transactions.

A situation where by a country doesn’t engage in foreign exchange is a very big issue this is because it affects the central bank due to the fact that it is the major supplier of funds for the market. Nigeria for example the determination of foreign exchange rate in Nigeria has two mechanisms which are fixed and flexible. The fixed exchange rate was in the 1960 from independence, this means the value of local currency in foreign currencies were fixed by the central bank. importers and exporters of non oil commodities were asked to get license from the ministry of commerce before they could undergo foreign exchange market but in the 20th century the exchange rate in Nigeria is to increase the value of the domestic currency, to ensure macroeconomic stability and a good balance of payment.

1b)

A change in a Nigeria’s exchange rate can affect the balance of payment this is because a weak exchange rate can lead to balance payment deficits. there will be an increases in the demand for foreign exchange which means more importation and less exportation from Nigeria therefore more payment has to be done and this can make the Nigeria debtors because they will have pay for consumption instead of investing in the growth of the country, if this continues the country will have to sell off their assets. For Nigeria to prevent deficits they should increases the rate of exportation by building more factories which leads to employment for citizens, they should be enough savings to lend to countries that by its product, exchange rate policies should be imposed also with fiscal and monetary instruments. When trade is being made it should be recorded in the current account because it measures the country’s trade balance. If Nigeria has a high demand for its goods tends to export more than imports which will lead to an increases in demand for its currency.

1. Explicitly show the issues in FEM using your home country as case study

Nigeria has a complex foreign exchange system, the exchange rate is often unstable, the administration has found it a big challenge to unify foreign exchange market that can gain the confidence of the users. exchange rate is measured by the prices of a foreign exchange changes overtime. When the exchange rate is unstable it causes a nervousness in foreign exchange market because the traders for uncertain of the market state on daily basis. This changes affects the whole country because prices can increase which can lead to inflation, unemployment, lack of savings due to a fall in exchange rate. The central bank controls the exchange rate volatility. Every country has an equilibrium of its exchange rate. Exchange rate is misaligned when it passes its limit. When there is disequilibrium in the foreign exchange market which is caused by in adequate supply of foreign exchange reserves, pressure may be exerted on foreign exchange reserves.  If the reserves are not adequate, it will deteriorate into balance of payments problems, hence the need to manage a nation’s foreign exchange resources so as to reduce the adverse effect of foreign exchange volatility. The management of foreign exchange resources is further informed by the need to set an appropriate cleaning price in the foreign exchange market. Therefore, the act of foreign exchange management in a conscious attempt to harness foreign exchange resources, deploy them to service the economy so as to prevent the economy from experiencing shocks due to foreign exchange volatility. “The practice of managing the foreign exchange resources has therefore evolved broadly in line with the globalization and liberalization of economics and financial markets”.  (Anifowose, 2017)