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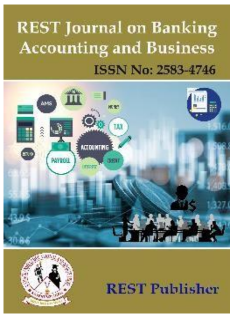

An Evaluation of Currency Deprecation and its impact on Economy- A Conceptual Study

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Abstract: *For any country, value of its currency is considered as one of the major indicators of its economy. In the current global economic scenario where presence of several events plays vital roles in changing the value of any nation's currency, many governments, corporate houses are concerned about the volatility of the value of their currency. The Currency depreciates when the worth of a country's currency drops significantly compared to other currency. There are various impact of currency depreciation ranging from micro level such as inflation, Low performance of Industry/Sector, to macro level such as negative growth rate of GDP, economic instability, Even impacting Global economy by disrupting interrupting international trade. The approach involves gathering insights from previously published research papers and articles as well as from watching recorded interviews from professionals in the field of the topic. Also, data from the government websites are being used to get comprehensive answer. As all the data have been taken from secondary sources so there is no requirement for conducting survey. The main agenda of this research paper is to study different factors that causes the volatility of the currency and analyze the impact of the currency depreciation on the economy and different variables that contribute in currency losing its value. The paper provides brief insight on depreciation of currency and its causes. The research also explains different factors (monetary and non-monetary) such as inflation, interest rates, government policies and how those variables affect the value of the currency. Also, with the causes this paper sheds light on the consequences (monetary and non-monetary) such as rise in cost of imported good, Negative balance of trade, Impact in balance of payment, reduced foreign investment, reduced tourism and how various sector of economy acts simultaneously with decrease in value of the currency. Also, with changing landscape of the economy, the policymakers and investors must be alert and be prompt with their decision making in order to make their companies and country stay afloat. The paper helps various investors and policymakers with insights and recommendation on how policy makers and investors should manage the risk and opportunities that comes with the depreciating currency.*

Key words: *Currency; Inflation; Balance of trade; Foreign Investment; Economic Growth*

1. INTRODUCTION

In current situation where there are various economic factors and indicators that constantly changes the shape of the economy. Currency has become one of the major indicators of the economy that is very sensitive in nature i.e., volatile to the factors that influence it. Over the last decades or so currency market and its impact is widely recognized by investors, policy makers as well as normal citizens. Currency is one of the greatest inventions made by human. Currency is a medium of exchange that allows individuals and business houses to carry out transactions and trade goods and services. During early days of human civilization when barter system was the only way of trading goods there were several issues such as lack of common value, transportation and storage. Those issues were eradicated by introduction of currency. Currency, we see today such as paper notes, electronic currency, metal coins were not there from the beginning. As human evolved currency also simultaneously evolved from barter system into what we see now as cryptocurrency. Various factors which include supply and demand, economic fundamentals, market sentiments and government policies plays important role in determining value of currency. Nation's currency value has a significant impact in the country's economy and individuals residing in the country. If a country has strong currency, it impacts the economy by making imports cheaper and making exports more expensive which might reduce economic growth of a country. Simultaneously if a country's currency is weak it can cause in increase in inflation and reduce the purchasing power of consumer. In Economics and Finance currency is considered as a fundamental concept and its value and movement have significant implication for individuals, businesses and economies. Exchange rates refers as the price of one country's currency with respect to another country's currency. As exchange rate compares the value of currency and it has wide ranging implication for international trade, foreign investment and financial flow. Exchange rate also plays an important role in determining the competitiveness of countries' exports and helps attract investment opportunities and skilled labor. There are two types of exchange system. Fixed rate exchange system. Floating rate exchange system. In a fixed exchange rate system, the exchange rate between two currencies is set by government policy. There are several mechanisms through which fixed exchange rates may be maintained. All fixed exchange rate systems share some important features. In a free-floating exchange rate system, governments and central banks do not participate in the market for foreign exchange. The relationship between governments and central banks on the one hand and currency markets on the other is much the same as the typical relationship between these institutions and stock markets. Governments may regulate stock markets to prevent fraud, but stock values themselves are left to float in the market. The U.S. government, for example, does not intervene in the stock market to influence stock prices. In contrast to individual marketplaces or particular enterprises, the study of macroeconomics concentrates on the performance and behavior of an economy as a whole. It focuses on the analysis of economic systems, broad statistics like GDP, inflation, and unemployment, as well as the interactions between various economic entities like governments, enterprises, and people. Macroeconomic theory makes an effort to explain how adjustments to monetary and fiscal policies, global commerce, and other factors affect the economy. Full employment, stable pricing, and long-term economic growth are the aims of macroeconomic policies. Macroeconomics also looks at how various economic agents interact, including how firms and households interact, how the government affects the economy, and the effects of global trade and financial flows. Activities and agreements involving the exchange of commodities and services between nations or regions are referred to as trade affairs. International trade now plays a crucial role in the development of the world economy and has an impact on everyone's social, political, and economic circumstances. While international trade in products and services has existed for millennia, it has undergone tremendous change as a result of globalization and technological improvements. International trade now makes up a sizeable component of the world economy and is a key factor in driving both economic growth and development. The flow of products and services between nations is governed by a complicated network of agreements, policies, and regulations known as trade affairs. These accords aim to encourage free trade, lower trade barriers, and guarantee fair competition between nations. Trade discussions are a crucial component of international trade relations. These discussions take place between nations in order to create trade agreements that will benefit both parties. Both bilateral and multilateral negotiations, including two or more countries, are possible. Trade policy are a crucial component of international trade affairs. To safeguard domestic industries and advance their economic interests, nations employ trade policies. These regulations may include, among other things, tariffs, quotas, and subsidies. Countries may engage in trade disputes, which can have a negative impact on trade ties and have serious economic repercussions. Trade restrictions, intellectual property rights, and tariffs are a few examples of the topics that might lead to disputes. The interrelated economic systems of all nations and places on earth are referred to as the "world economy." It is a dynamic system that includes everything from production and consumption to trade and finance. Changes in technology, politics, and international events all have an impact on the growth and development of the global economy, which is always changing. Over the last few decades, the global economy has expanded quickly as a result of increased trade and investment opportunities brought about by globalization and technological advancements. Millions of people have been lifted out of poverty as a result of increasing affluence and economic progress brought about by the expansion of the global economy. But it has also given rise to fresh difficulties like wealth disparity, environmental deterioration, and social and political instability. Countries rely on one another for commerce and investment, which has resulted in a closely integrated global economy. A sizable component of the global economy is made up of international trade, which has emerged as a crucial engine for economic expansion and advancement. As a result of the sharp increase in international trade in products and services, multinational firms have grown and worldwide supply chains have been established. Finance is another essential component of the global economy. Everything from banking and investments to insurance and capital markets is included in the global financial system. The financial system is essential to the global economy because it makes capital flows and investment possible and supports economic expansion. Significant obstacles to the global economy include political instability, economic inequality, poverty, and climate change. To address these issues, nations and regions must work together and ccollaborate, and creative solutions and policies that support sustainable economic growth and development are also needed.

2. REVIEW OF LITERATURE

Mehl, A. & Reitz, S. (2018). The impact of currency undervaluation on economic growth in emerging economies, the relationship between depreciation of currency and economic growth in up-and-coming economies are studied in this article. By using 31 countries and their data from 1995 to 2015 the researcher found that if the currency devaluation is not extreme then it can have positive impact on the growth of the nation. An estimated growth rate up to 1.2 was seen when the currency of that nation depleted by 10%. Simultaneously when the undervaluation of currency was extreme the nation's economy showed a negative growth rate through series of indicators such as inflationary pressure and reduced foreign investment. This study emphasizes that policymaker should analyze the potential risk and opportunities that comes with the undervaluation of currency and maintain a balance between undervaluation and overvaluation of a country's currency while formulating economic policies of a country. Ito, T. (2018). The economic effects of the YEN depreciation: Evidence from Japanese firm-level data, this paper provides insights on how micro economic indicators such as sales profit and investments are impacted with the depreciation of Japanese Yen. In this research there was positive effect seen on exports and sales whereas minute effects were seen on profit and investment of a firm with high export to sales ratio, but a negative effect on the profit and investment of firms with a low export-to-sales ratio. The paper shows that depreciation of yen had a positive impact on the overall economy by increasing aggregate demand and stimulating economic growth. The author found that policymaker need to consider the heterogeneity of firms when the formulate economic policies related to exchange rate and its management. Bhunia & Mukherjee (2019) examine the relationship between currency depreciation and inflation in India, in this study they found a positive relationship between the considered variable. With the help of monthly data, the authors used econometric techniques to study the long-run and short-run relationship between inflation and currency depreciation, where it indicated that currency depreciation can result to inflationary pressure in economy of India. To be specific when the Indian rupee depreciated by 1% the inflation was seen to increase by 0.05%. The research suggests policymakers that the potential inflationary impact of currency depreciation need to be carefully considered while formulating exchange rate policies. The researcher stated that the study is only relevant for Indian economy but there was also seen common pattern for others up-and-coming market economy where currency deprecation is there. Edwards. S (2019), the researcher examines the interrelation between exchange rate policies and economic growth. The study is done by analyzing 117 countries and their data over the time period of 1980 to 2017, emphasizing the role of exchange rate regimes in promoting economic growth. In this study countries with flexible exchange rate seems to have high level of economic growth than those with fixed or non-flexible exchange rate. Moreover, those country whose exchange rate regimes were more stable showed immense growth rate. In order to achieve more sustained economic growth there should be appropriate macroeconomics policies and institutional framework. The paper's finding consists of several implementation that policymakers and politicians can implement in order to achieve flexible and stable exchange rate regime. Hatice & Erol (2019) The impact of exchange rate fluctuations and foreign trade in Turkey. The authors investigate the impact of exchange rate fluctuations on foreign trade in Turkey using ARDL bounds testing methods (ARDL bounds testing approach is a cointegration method developed by Pesaran et al to test presence of the long run relationship between the variables). With the help of monthly data from 2003 to 2017 the author found that exchange rate fluctuations had major effect on foreign trade of turkey. When Turkish Lira lose its value, the exports increased whereas the imports decreased simultaneously the appreciation showed exact opposite effect. Also, the author found a J-curve pattern where the short-term effect of exchange rate fluctuation is negative whereas the long-term effect of exchange rate fluctuation is positive. The research emphasizes on achieving the stable exchange rate in order to promote international trade and while formulating exchange rate policies policymakers should be aware about the impact that exchange rate policies make on the trade competitiveness Huchet-Bourdon, et al. (2018) in their paper examines the effectiveness of fiscal devaluation in emerging economies, using the case of Mauritius as a case study. In the paper discal devaluation was defined as a policy that aims to minimize labor cost and boost export competitiveness by shifting the tax burden from labor to end consumer. Fiscal devaluation results in significant increase in exports and reduction in imports which results in improved trade balance. The author found that fiscal devaluation can lead into short term inflation whereas in long term context there is seen positive impact on investment and employment. Prasad (2018), the author examines the effect of currency intervention by central banks on exchange rates and economic outcomes. This paper provides in depth analysis on the experiences of up-and-coming economies and advanced well-established economies and findings portrayed that depending on circumstances currency intervention can have both positive impact as well as negative impact on economy of a country. Positive impacts can be stable exchange rates, reduced volatility. Whereas negative impacts can be inflationary pressures, distortions in financial sector and increase in government debt. The effectiveness of currency intervention is affected by several variable such as range of factors, exchange rate regime, level of economic development and the institutional framework. Findings also provides important implications for central banks and policymaker as they try to maintain stable exchange rate and promoting economic growth while avoiding potential negative consequences of currency intervention. Sarno, L., et al. (2018), gives in depth report of the economics of exchange rates. In this paper history and evolution of exchange rate regimes, several theories that determine exchange rate and empirical evidence on exchange rate behavior is examines. The paper signifies the challenges of predicting exchanges rates as well as how market sentiment, news events and global economic condition plays an important role in determining exchange rates. The relationship between exchange rates and various macro-economic variables such as trade investments and inflation are studied in the paper. The study is based on the following objectives. To study the history of currency and the factors that contributes in increasing the value of currency. To find out the factors that could result in depreciation of a currency. To study the effect of devaluation of currency on the economy. Currency devaluation has become a major challenge for countries all around the world which cause severe consequences to the country's economy. When a currency starts losing its value it can cause to rising inflation, higher interest rates, reduced trade and other negative effects that can hamper the economic growth and development of nation. There is significance to understand the causes and effect of currency devaluation on the economy and the solution that can help mitigate negative effect and boost positive effect. This research paper aims to study the problem of currency devaluation and its effect on the economy, it provides an in-depth analysis of the problem and offers implications to tackle this critical situation.

3. RESEARCH METHODOLOGY

The descriptive study is based on the secondary data. Thorough literature survey to gather information and insights from previously published research, articles, and publications on the topic. The various published resources such as reports, journal articles, and newspaper articles are considered for the research. We have also acquired and analyzed data on economic variables including exchange rates, inflation, and trade balances with the aim of looking for trends and patterns in the value of the currency and its impact on the economy. We have also observed and examined conversations with experts and stakeholders from academia, finance, and government to obtain understanding of the potential effects of a depreciating currency on multiple areas of the economy. This can offer a deeper understanding of the problem in its context and help discover viable policy solutions and suggestions. There are qualitative and quantitative factors influencing on the currency value.

Quantitative Factors

Exchange rate	Exchange rate compares the value of currency it has wide ranging implication for international trade, foreign investment and financial flow. Exchange rate also plays an important role in determining the competitiveness of countries' exports and helps attract investment opportunities and skilled labor.
Inflation	Inflation is a measure of the rate at which the general level of prices for goods and services is rising, and the purchasing power of a currency is decreasing. Inflation can be caused by a variety of factors, including increases in the supply of money, changes in the demand for goods and services, and changes in the supply of goods and services.
Interest Rates	In general, a country with higher interest rates will attract more foreign investment, which can increase demand for its currency, leading to an increase in the currency's value. Conversely, a country with lower interest rates may be less attractive to foreign investors, leading to a decrease in demand for its currency and a decrease in its value.
Trade Data	Trade data such as imports, exports, balance of trade, balance of payments plays vital role in increasing or decreasing the value of any currency, also above factor are also heavily affected when the value of certain currency falls. Hence trade data has been considered in order to analyze the impact in international trade pattern of an economy
Market Data	Devaluation of any currency can have significant impact in stock of that particular county. In order to understand the effect of falling currency several stocks and indexes have been used for interpretation.

Non-Quantitative Factors

Policies and Law	Policies and Law, and value of currency are directly interrelated. The monetary policy and foreign exchange operations of central banks, can have a big impact on the value of the currency and vice versa.
Market Sentiments	Market sentiments refers to the emotions of the investors, consumers and corporate houses towards the economy and market. Positive market sentiments can help currency to flourish whereas negative market sentiments can influence in downfall of the currency
Pandemics	After the impact of COVID-19 in the economy and its indicators. Pandemic has become one of the variables that affects the value of the currency in an economy.
Environmental Factors	The uncertainties that environmental disasters bring onto the economy of the nations should be taken into consideration. Environmental turmoil indirectly affects the currency of the nation. For example: After the earthquake the Turkish Lira has started to depreciate rapidly.

In any country interest rates are facilitated by central bank. Interest rates impacts the cost of borrowing money and the ROI (Return on Investment). If the interest rate which are set by the central bank is low then the cost of borrowing money from the banks becomes relatively cheaper which leads to increased spending and economic growth. Low interest rate generally makes currency less attractive to foreign investors, which results them seeking their returns elsewhere. Conversely when central banks set higher interest rates the cost of borrowing money from bank becomes higher than lower interest rates which results in foreign investors being attracted towards the currency in order to seek better return. It tends to increase the demand for the currency and ultimately results in increasing the value of the currency. Hence, If the interest rates in the country is low then investors are keen to move their money away where they can earn favorable return on investment which leads in decrease in demand for the country's currency and depreciation of its value For example: If central bank of country A raises its interest rates while central bank of country B keeps it interest rates unchanged then investors may shift their investment from country B to country A, increasing the demand for currency of country A whereas decreasing the demand for currency of country B. Which results in currency B to lose its value against currency A. Another factor that can cause volatility in value of currency is inflation. Inflation means the rate at which general level of prices for services and goods rise. During high inflation a country experiences the purchasing power of its currency decreasing which results in their currency becoming less attractive. Adding onto that when inflation rates are high investors can lose confidence in economy of the country's economy leading them to sell the investments in country's currency and invest elsewhere there is low rate of inflation. Hence when investors sell currency it can lead to currency depreciation Another critical factor that can impact the value of a currency is political and economic stability. When there is political instability such as civil war and constant policy changes, it can lead to uncertainty in the country and makes it risky to invest in the economy making it less attractive to foreign investors. Likewise, when there is economic turmoil like high level of debts can undermine investors' confidence and lead investors to sell their investment or not to invest at all. If country A has frequent regime changes and has unreliable policy makers who frequently changes policies, tax rates then it results in difficulty to invest and get return in country A. As a result, investors and corporate houses decides not to invest in that particular country and sell the investment if they had already invested in the country's economy. Exports is one of the major incomes for any economy and similarly imports are its major expenses. If an economy can keep its exports high while minimizing its import then we can assume that the country's economy is flourishing.

Trade balance is the term which is generally used to define the difference between the country's exports and its import. When a country's trade balance has a deficit that indicates that the country is importing more goods than it is exporting and it must pay its imports in foreign currency which decreasing the demand for country's currency in the international market and causing depreciation. Hence trade surplus can lead to increased demand for country's currency resulting in increase in value for the currency whereas trade deficit decrease the demand for country's currency leading to depreciation in currency. As discussed before the causes of currency devaluation, it is seen that most of the factors and currency devaluation are directly related i.e., the factors that affect the value of the currency also are impacted when there is depreciation of currency. There are few benefits that an economy can reap from depreciation of its currency amongst them increase in export is one. When a country's currency is depreciated it makes the product cheaper for other countries to buy and import them into their own country, it results in boost of country's competitiveness in export market of global economy. When the demand for country's export increases the export revenue of the country increases, there is more employment opportunities and eventually boosting the economic growth rate. For example: When the value of Yuan decreases, China becomes cheap for foreign buyers to source their raw materials from which led to an increase in demand for Chinese goods and services in international market. Although currency devaluation helps to increase exports by making it cheaper on the other hand it impacts the import by making it more expensive. When value of currency decreases, one has to pay more money for the same amount of goods or services which used to be cheaper before. When imports are expensive the price for general public consumer also increases. This causes decrease in standard of living especially for those country where citizen mostly rely on imported goods and services resulting in inflation. Currency depreciation affects the psychology of investors where they lose confidence in the economy, making them to leave the economy by selling off their investments. When investors leave the economy starts to decline and crumble. In order to attract the investors back into the economy and stabilize the economy the central banks tend to raise the interest rates. Depreciation of curreny can increase the burden of foreign debt on an economy. When there is depreciation in a currency, it requires more of the depreciated currency to pay off foreign debt which is denominated in other currencies. Which increases the cost of servicing the debt ultimately leading to an increase in the debt burden. For example: when the value of the Indian rupee decreased in 2018, it became more expensive for India to pay off its foreign debt i.e., leading to an increase in the debt burden. When there is currency devaluation can lead to an increase in deficit of currency account. When country's currency depreciates there is increase in the price of goods and services imported into the currency, which leads to increase in the current account deficit. Current account deficit is especially in those countries that rely heavily on the imported goods and services. For example: when the value of the Nigerian currency Naira depreciated in 2016, the cost of importing fuel skyrocketed, which led to an increase in current account deficit. Capital flight refers to the situation in which investors and multinational companies that have invested their money in the economy decides to sell their investment, assets and shift their money elsewhere. Capital flight is caused when investors lose their confidence in economy of the nation which is generally when value of currency depreciates. Capital flight leads to decrease in foreign investment which stops economic growth having negative impact on the economy. For example: When the value of the Argentine peso decreased in 2018, there was a significant amount of capital flight out of the country. Economy consists of several industries, each and every industrial sectors reacts differently with the change in value of the currency. Industries that heavily rely on the export may usually be benefited with depreciation of currency as exports are relatively cheaper when there is devaluation of currency. On the other hand, those industries that heavily rely on the imported inputs are found to experience negative impact as during depreciation cost of imports are high. By now we know that when there is decrease in value of currency then imported goods tend to be more expensive and also export tends to reduce substantially. When the imports are expensive the government are required to pay more of the devaluated currency, which can lead to increased government spending. As we know if there are more expenses than income the revenue eventually decreases. Hence decrease in value of currency indirectly has an impact on government revenue. Currency depreciation can also have impact on investment made by government, corporate houses or individuals. If a currency depreciated then investment denominated in that currency loses its value. This can have negative impact on the investors who hold investment denominated in the devaluated currency. For example: 1 lakh Rs worth of investment made in Indian stock market will not be as valuable when the currency starts losing its value.

4. CONCLUSION

Currency is sensitive and volatile in nature. There are several factors that plays an important role in appreciating or depreciating the value of the currency. Also change in the value of currency can bring impact ranging from micro level to global level of an economy. The presumptions believed that the currency depreciation can only bring negative impact on the economy. But findings from the paper suggests that there are both positive as well as negative impact brought on by depreciating currency. The paper has also identified several factors like inflation, interest rates, exchange rates, trade balances, market sentiments, pandemic, environmental turmoil. By understanding these factors and how they impact the currency policymakers and investors can draft the strategies that can help to minimize the risks that comes with the depreciation of the currencies. Hence this study signifies the importance of understanding the complexities that comes with the value of currency on economical level

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