

6.5 Policies to correct imbalances in the current account

Name: _____ Class: _____ Date: _____

Total: 23 marks

KEY WORDS expenditure-switching • expenditure-reducing
 • supply-side • competitiveness • current account

Objective

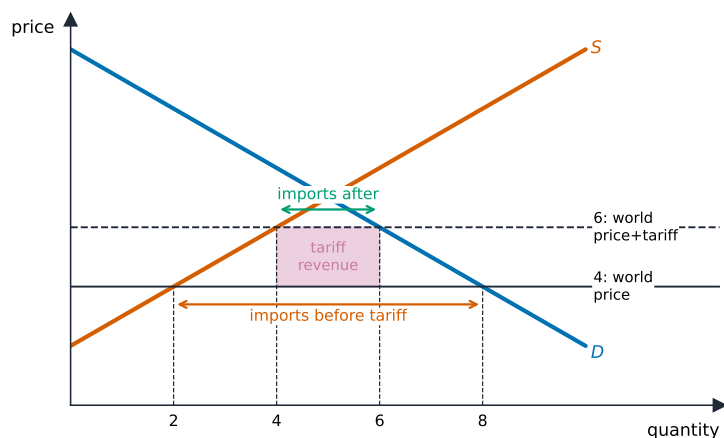
Build the skills to answer exam questions on **policies to correct a current account imbalance** – expenditure-reducing, expenditure-switching and supply-side , , policies.

You must be able to:

- describe the three types of policy to correct a deficit
- explain how each one works and its side effects
- analyse and evaluate the best policy for a deficit

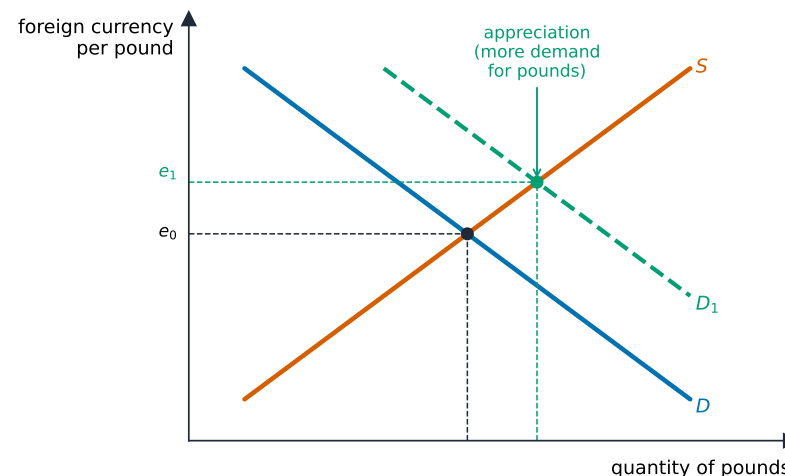
1 Key knowledge and worked examples

■ Correcting a deficit



Three routes to a smaller deficit, each with side effects

- **Expenditure-reducing** : higher taxes/interest rates lower demand → fewer imports – **but** slows growth, raises unemployment.
- **Expenditure-switching** : a tariff or lower exchange rate moves spending to home goods – **but** risks retaliation or inflation.



A lower exchange rate is the main expenditure-switching policy for a deficit

- **Supply-side** : raise **competitiveness** (skills, technology) so exports rise – best long-run, but slow.

Answer shapes: AO1 + AO2 + AO3 (analysis) + AO4 (a supported judgement *in context*).

2 Practice

2.1 Define the term *expenditure-switching policy*. [2]

2.2 State one expenditure-reducing policy. [1]

2.3 State one drawback of using expenditure-reducing policy to cut a deficit. [1]

3 Exam-style questions

3.1 A depreciation of the currency to reduce a current account deficit is an example of: [1]

☐ A an expenditure-reducing policy
☐ B an expenditure-switching policy
☐ C a supply-side policy
☐ D a contractionary monetary policy

3.2 Explain how an expenditure-switching policy could reduce a current account deficit. [6]

3.3 Discuss the best way for a government to reduce a large current account deficit. [12]