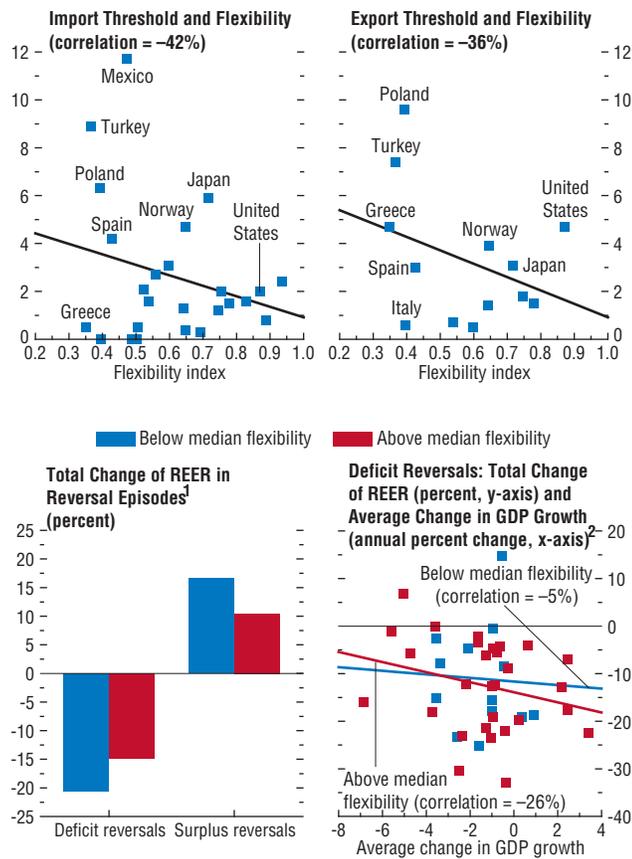


Figure 3.9. Thresholds in Relative Trade Prices, Real Effective Exchange Rate, and Flexibility of Markets

Countries with higher values of the flexibility index tend to have lower thresholds in the growth rate of relative prices of imports and exports. More flexible economies have experienced smaller movements in real effective exchange rate (REER) during reversal episodes. Only for these economies does there appear to be a trade-off between REER depreciation and GDP growth during deficit reversals.



Sources: IMF, *International Financial Statistics*; OECD, *Economic Outlook* (2006); World Bank, *World Development Indicators* (2006); World Bank, *Cost of Doing Business* database; and IMF staff calculations.

¹ Maximum change in REER within the period surrounding the reversal ($-T \dots T$), median across episodes. An increase represents a real appreciation while a decrease represents a real depreciation of a country's currency relative to its trading partners.

² Advanced economies only. Average real GDP growth after the reversal ($1 \dots T$) less average real GDP growth before the reversal ($-T \dots -1$) on the x-axis. Maximum change in REER within the period surrounding the reversal ($-T \dots T$) on the y-axis. Median across episodes.