

## **Capital Account Liberalisation and Flexible Exchange Rate**

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Restoration of market forces in foreign trade has been an important policy decision since the sixties. First it was confined to developed industrial countries only but since the mid seventies developing countries also started moving in the same direction - Chile, Argentina, Uruguay, the 'Southern Cone' countries provide the ready example. It is being said that for proper integration an economy must throw itself open to the rest of the world. Freeing of international trade from all restrictions, promotion of free trade in the movement of goods as well as in assets constitute the care of liberalisation movement, liberalisation as can be seen applies both to trade and capital account. In the present paper, however, we are concerned only with capital account liberalisation. Theoretical as well as practical issues arising out of liberalisation and policy measures, if any, to deal with them will be discussed in the following sections.

### **I. OPEN CAPITAL ACCOUNT : THEORETICAL ISSUES**

Liberalising capital account in the first place will imply withdrawing all restrictions on movement of funds from/to abroad. Some countries have minimised restrictions on movement of long and medium term funds while retaining those on short term ones in the fear that withdrawing restrictions on them might be quite destabilising. Once restrictions on capital flows are withdrawn, private individuals become free to invest in foreign financial assets. Asset portfolio now