

Composition of Imports, Expenditure Switching and Trade Policy

M. K. Datar

The open economy framework is increasingly used for theoretical analysis of macro economic problems as also for discussions regarding policy analysis and policy reforms. The policy literature has grown largely in the context of developing countries; their problems and experiences. While the policy literature has been influenced by developments in theoretical literature, the latter largely remains at an abstract level.

The theoretical literature typically considers a small open economy as the subject matter of enquiry. The smallness is defined in terms of price taking behaviour. Small open economy would be a price taker when it sells as well as when it purchases in international markets. Distinction between tradeable/non-tradeable goods is an essential feature of open economy framework. The possibility that producers of specialised primary commodities may not be, at times, price takers in export markets is recognised. In such cases the line of distinction is drawn between national/international goods and the two sector framework is preserved. The framework is used for analysing macro problems like determination of output, wages, price and effects of macro economic shocks ^{1/}. While the 'structuralist' tradition has concentrated for long on the difficulties developing countries would face in the given structure of international transactions, Taylor (1984) has recently presented a macro-economic framework which incorporates some distinguishing features of developing countries. That in an interdependent world an open economy framework is more appropriate to analyse macro economic problems than a closed economy framework can hardly be contested. But it is felt that the approach of incorporating special features of developing countries in the analytical frame would be useful.

This paper highlights some special features of large developing economies that have implications for policy analysis in an open economy framework. It is argued here that the size of an economy would be linked to its degree of openness. For large countries the dependence on trade would be of a different type which would be reflected in commodity composition of tradeables in general and importables in particular. The typical commodity structure of importables has certain implications for use of expenditure switching policies and sequencing of export