

Reviews of ECONJOURNAL-D-24-00056R3

The roles of the terms of trade and the real exchange rate in the current account balance

Round 1

Reviewer 1

The Review

The paper "The roles of the terms of trade and the real exchange rate in the current account balance Economics" presents the results of an investigation with SVAR on the determinants of the current account balance. The Authors build up on the existing literature and their results they get are not extreme and follow from the analysis. In general, the paper is really well written and interesting. I found some minor "language mistakes", but all of them can be easily corrected with one more proofread. Consequently, I can recommend publication of the paper.

Reviewer 2

N/A

Editor

ECONJOURNAL-D-24-00056

Dear Dr. Unal :

Many thanks for your submission. Our editorial staff, aided by referees, has had a chance to review the material.

The referees are very split in their assessment : one recommends rejection and the other acceptance, without much explanation in either report (see their brief comments, below). This puts the main weight of the decision onto the editor.

As a result, we have solicited a second editor's opinion so that we can base the decision on several views along with the split referee views. We also wanted to give you some direction about the way the article would need to evolve in order to satisfy future referees.

The editorial view is that the paper needs to be revised before it could be considered for acceptance. Indeed, we would recommend revision at this point but cannot guarantee that acceptance will follow. Still, the paper's topic holds some interest and the required changes seem doable, so we would be happy to entertain a revised version of the paper.

The editorial manager will issue you “default” due dates, but if you need more time to conduct the work, please contact the editorial office, Assistantmanagingeditor@degruyter.com with your required timeframe.

In terms of the changes that would need to be made,

(1) Importantly, the paper does not give any information about its sample, how it was collected, or its nature. That needs to be included so that future authors could potentially replicate the work. You would need to explain your data sources in full, provide summary statistics, and possibly do an informal graphical analysis to set the scene before launching into the econometric work.

(2) The work includes the 2020-2022 time period in the analysis. This will include Covid effects, which need to be controlled for in the robustness section if nothing else. What happens to the results if 2020-2022 is not included? Do they change? If so, how much? A second concern about timeframe is that this includes the post-2016 time when trade between the US and Turkey was affected by trade restrictions (from the Trump administration). Both the terms of trade and exports to the US likely were affected at this point. What is the effect of this on the analysis? Again, some robustness analysis would be a good idea here. Your model contains the Global Financial Crisis period as well. This might also have had particular effects. Is there, then, a shorter time period within your data where there is less disruption and where you could perhaps isolate the effects without those disruptions, and then expand to other portions of your data to see how the various disruptions affected the results? This could help to determine whether the distinction compared to earlier work is the time period you study or whether it is the Turkish economy’s distinct features. It could also help you to dig into what the effects of various different types of crises are on the Turkish economy, which could have interest for readers as a secondary contribution.

(3) For someone who is not using time series analysis, the reason why the SVAR model is superior to the other techniques you mention in the review of the literature (ARDL, for example), is not clear. You say what is good about SVAR, but not why it would be better than the other techniques: when would you want to use ARDL, for example, and when SVAR? It would be useful to make the paper a bit more “teachy” in the sense of explaining your methodology to people who do not use this type of model normally. Remember that we are a general interest economics journal, after all. This also applies to your explanation of the SVAR itself, the 12 period lags, and that entire section of the paper. This part needs to be explained to people who don’t know the time series models well, so that they can understand, too. This needn’t take up a lot of space, but you do need to include some brief explanations to justify what you are doing more clearly.

(4) The material next to the tick marks and following the initial results is interesting but is not related clearly to the modelling. Can you translate these conditions into formal restrictions on your model that identify the effects? This would help to link these paragraphs to the modelling.

(5) You refer to short term and long term effects in your literature review, but your own work occurs over a one year period, it seems. Is this short or long term? Can you link your own work to what others have defined as the short or the long term so that we can make the link? You seem to indicate that 12 months is the long term, but for people who are not in the field, the definition of short term and long term may not be obvious. Again, a brief explanation would be in order here.

(6) Please include full legends along with the figures (and tables) so that readers know what the axes represent, what the units are, and for the tables that they get a reminder of what the different variables mean.

Again, thank you for your submission. We look forward to a revision in due course and will put the modified text back to the referees and editors to evaluate. As I said, if you need more time than is allocated by the system, please do write to ask.

In the meantime, all the best to you.

Round 2

Reviewer 1

Referee comments on "The Roles of the Terms of Trade and the Real Exchange Rate in the Current Account Balance" ECONJOURNAL - D- 24-00056R1

Summary:

This paper postulates an SVAR model of the determinants of the (short term) current account balance in Turkey using a sample that both includes the Covid period and one that excludes this period. The real exchange rate ends up playing an important role in determining the current account balance, although the results for the pre-Covid and Covid inclusive sample differ considerably. Recommendations are made for more integrated fiscal and monetary policy to address current account imbalances.

Comments

As an introduction to the comments, I am a general reader, not a specialist. As a result, my comments are from the perspective of a reader who will need terms defined, and methods explained more than someone who is steeped in the field. As a result, many of my comments are about clarifying your arguments, wording, hypotheses, and conclusions.

1. Please ensure that readers understand your terms at least moderately at the time you first use them:

As this is a general interest journal, please define terms that are specific to your area. You define the HLM effect in section 3, but you mention it very early in the paper without any word telling readers what this is and why it is relevant. A few words would suffice to explain this the first time you mention it. The more detailed explanation can follow later. When you state in the policy section that you find no HLM effect, remind readers about the significance of this finding. Why do you think that this is the case, given that the result contrasts with those of other authors?

Similarly, when you explain your technique in the added section (in blue) at the beginning of section 2.2, you mention several techniques that will not necessarily be familiar to all readers. If you will be explaining these in detail later or at least why you are employing the technique (for example the Cholesky decomposition), say a few words to indicate where it will be explained so that readers don't think that this paragraph is their last chance to see what you are doing and why. When you explain the technique, you don't need to use many words: just say why you're doing it and what it will help you determine.

As an example of a case where readers might pose a question, you indicate later that you use three tests for a unit root for robustness. Simply stating that you do several techniques for robustness at the early stage where you introduce your methodology could help readers understand why you are taking the steps you have taken.

These small changes (I don't think you need to add very many words to clarify any of the concepts) will make the paper more accessible to all.

Finally, please define all acronyms when you mention them (eg, AIC). Please define all your variables in the tables in the legend so that we know which labels refer to which variables. For example, in table 2, what is Inop? Lntt? All the other variable names? When you state the variance decomposition in terms of percentage effect, could you state the percentage effect on what? Presumably you mean the current account balance (heading on the table), but please do just be explicit about this so that it is crystal clear. Readers need to be led by the hand a bit more to get through your analysis easily. If you do not make things very clear, they risk not reading further, and that would be a shame.

2. Please ensure that you are precise in the wording of your sentences, avoiding the passive voice where possible.

Much of the writing is just a bit difficult to interpret and could benefit from being made crystal clear so that readers really understand what you mean.

As an example, though, have a look at the way you phrase the discussion of Uneze et al, 2012. What style of study was Uneze et al? Was it an econometric analysis or did they just present more informal arguments? Was that study about oil importing or exporting nations (the next sentence seems to indicate that it was about oil exporters?) This sort of small added detail will give a sense of the landscape of the literature and how your work fits into it. The next paragraph, second sentence, carries on to say that "It was pointed out that under a system of flexible...". Does this sentence still refer to the work of Uneze et al? Who pointed this out? Later in that paragraph you mention "under a situation of elasticities of demand for imports." What do you mean here? There is always an elasticity of demand, so what is unique about this case?

Do you see the problems I'm trying to get at? Please go back over the writing to make sure that you actually make clear to someone who is not an expert what you mean. That will make the writing clearer to all.

3. Please ensure that your organisation is "linear" so that points are made once and your arguments lead directly to your point.

For example, the added paragraphs at the beginning of 2.2 could be organised better: I was left somewhat confused about the contribution and the state of the previous literature. The first paragraph added to 2.2 does not cite specific work, although it makes the main argument for contributions; the later added paragraphs do mention earlier work but this is not integrated with the earlier contribution statement. This organisation is difficult. Could you boil these paragraphs down to a single statement of contribution, contrasting your work with specific previous papers, so that a single statement of the contribution is possible? As part of these added paragraphs, a reference for readers on the history of Turkish economic development could help readers who are not familiar with the country (supplementing the comments at the end of the first paragraph in blue, section 2.2).

4. Please clarify the model statement and examine robustness as part of defending it.

While the statement of the model is reasonable in section 4.2, it is not clear that this is the only or the best model. Do you have any robustness work that can argue for this as the best model in any sense? Secondly, do you have a null hypothesis that you are testing in the model? Can you state it so that readers can tell what the direction of travel is before they see the results tables?

Finally, your results indicate that the exchange rate is the largest determinant of the current account balance, but is this surprising? Why would this not be the case, and is your study an outlier at all or is this a standard result?

5. Please highlight your contribution as part of stating your results.

In terms of your other results (for example the variance decomposition), you can improve the understanding of your contribution by commenting at the point you present the results on how different these results are from those of other similar studies. Similarly, are your response functions quite unique or is this much in line with other work? Please say it at the point where we have the results in front of us. By doing so, you could underline your contribution.

6. Clarify your conclusions and make your recommendations more precise:

In your conclusions, you reiterate that the real exchange rate plays a determining role in the current account balance, but then you say that the effect of the early 2000's devaluations is assumed to be limited. Who assumes this? Why would this be assumed if the real exchange rate plays an important role in your model? I was unsure how to interpret this comment. If you are saying that the findings in the paper are directly in contradiction to public statements by the government or other studies, maybe put in some quotes at this point so that the importance of your points for policy is clear?

As you point out, the results pre-Covid are quite different from the results including the Covid period. Which should be the basis for decision-making? When you discuss policy in the paper, which results are you pointing to (the pre-Covid results or those including Covid information)? Why?

As a final comment on the policy implications, you could make your argument more forceful by contrasting your argument for integrated fiscal and monetary policy to address current account deficits with the actual policy: is fiscal and monetary policy integrated in the way you suggest? Can you point to examples of where it is not? This could make your recommendations a bit more concrete and impactful, as they would indicate what is going wrong in a more precise way.

Round 3

Editor

Thank you for your follow-up correspondence. As you agree to continue with the revision process, and we support this decision, we will re-issue the previous reports for version R2 of the paper. Please see the report, below, for the comments on which we would appreciate your input.

Should the revision take you beyond the stated due date, please write to me with the time you require to perform the work. We can adjust the parameters so that you have the time you need to address all the editorial concerns.

[illegible]

I appreciate the effort you have invested in enhancing the clarity and depth of your analysis. Upon a thorough review, I believe that additional revisions are necessary to elevate the paper to meet our journal's standards. Another reviewer also has further suggestions and comments for improving the quality of the manuscript, and I agree with all of them, especially regarding enhancing clarity for a general audience. The reviewer emphasizes the need to define technical terms and explain methodologies clearly at the first mention. There are suggestions for improving sentence clarity, organizing content more logically, and making the paper's arguments and conclusions more understandable to non-specialists. Specific feedback includes defining acronyms, clarifying variable names in tables, and elaborating on the significance and novelty of findings. The reviewer also advises on structuring the paper's arguments more effectively. Please note that while addressing these comments thoroughly will significantly improve your submission, it does not guarantee publication. All revisions will undergo further review to ensure they meet the journal's standards of rigor and clarity. We look forward to receiving your revised manuscript. My suggestions and the reviewer's comments are provided below:

Coeditor's Comments and Questions

1) In Section 2.2, the paper discusses the application of an SVAR model to account for the bidirectional instantaneous causal relationships between the current account balance, industrial production, and the real exchange rate. However, the justification for assuming instantaneous relationships between these variables is not fully verified with specific empirical evidence or theoretical backing. Moreover, the section could benefit from a detailed explanation of how the SVAR model's specific constraints are formulated based on these assumed relationships.

2) In Section 3, what is the justification for the selection of the specific period (Jan. 2005 to Oct. 2022) and its relevance to the study objectives, especially considering the significant extreme events during this period that could impact the results (e.g., the 2008 global financial crisis and the COVID-19 pandemic)? The transformation of all data into a logarithmic form is mentioned but not justified. Clarifying why logarithmic transformation is necessary (e.g., to normalize data, handle skewness, etc.) and how it impacts the analysis would provide additional justification for the econometric approach used.

3) What are the potential implications if any of the variables were found to be integrated of order one, especially since such findings can lead to spurious regression issues if not appropriately addressed? Given that the oil price, terms of trade, real exchange rate, and industrial production index are identified with an order of integration of one, it would be beneficial to justify not differencing these series or using a cointegration approach if these variables are used in the same model.

Also, for the SVAR analysis, while you outline the use of the A-B model and its constraints, there is a lack of explicit detail on how the identification restrictions are empirically justified or derived from the theoretical or prior empirical literature. Detailing this could strengthen the credibility of the model specification. The choice of a maximum lag of 12 for the VAR model using AIC could be better substantiated by comparing it against other criteria, such as BIC, which might suggest different lag lengths. A robustness check using different lag selections could reveal the sensitivity of your results to the chosen model specification.

4) I encourage you to conduct robustness checks. This could involve using alternative econometric models or a subset of the data to verify the stability of your results. Please include a new subsection, 4.6, detailing these checks and discussing how they support or challenge the main findings.

5) For policy implications, while the discussion correctly identifies the terms of trade and the real exchange rate as significant factors, the linkage between these empirical findings and the suggested policy actions could be made more explicit. For example, while you suggest policies aimed at reducing export prices to enhance competitiveness, the empirical backing for this recommendation from the SVAR results should be detailed further. Specifically, it would be beneficial to discuss how changes in these variables have historically impacted the current account balance in the models used and how these effects substantiate the recommended policies (Mesagan et al., 2022; Bleaney & Tian, 2014).

Secondly, the recommendation to manage the real exchange rate through monetary policy could benefit from a detailed discussion about the potential side effects of such policies, including impacts on inflation and foreign investment inflows (Bahmani-Oskooee & Aftab, 2017; Edwards & Cabezas, 2022). Including a brief review of the literature on the effectiveness and risks associated with exchange rate manipulation in similar economic contexts could provide a more balanced view.

Furthermore, while the paper discusses the need for productivity improvements in export goods, a detailed strategy on how to achieve these improvements would enhance the practical value of the recommendations. This could include policies aimed at technological adoption, skills development, or sector-specific incentives that have been successful in other emerging economies (Blyde et al., 2018).

6) There are minor editorial issues, such as typos and grammatical errors. For example,

- I would remove C5 from JEL codes since the paper doesn't contribute to econometric modeling techniques per se but rather applies them.
- This sentence on Page 2 needs to be rewritten: ``it became a serious problem around 48.8 billion US dollars in 2022."`
- Please ensure the placement of Figure 3 is correct within the document layout.

There are other grammatical errors, and I suggest carefully proofread the paper.

References

Bahmani-Oskooee, M., & Aftab, M. (2017). On the asymmetric effects of exchange rate volatility on trade flows: New evidence from US-Malaysia trade at the industry level. *Economic Modelling*, 63, 86-103.

Bleaney, M., & Tian, M. (2014). Exchange rates and trade balance adjustment: a multi-country empirical analysis. *Open Economies Review*, 25, 655-675.

Blyde, J., Iberti, G., & Mussini, M. (2018). When does innovation matter for exporting? *Empirical Economics*, 54, 1653-1671.

Edwards, S., & Cabezas, L. (2022). Exchange rate pass-through, monetary policy, and real exchange rates: Iceland and the 2008 crisis. *Open Economies Review*, 33(2), 197-230.

Mesagan, E. P., Alimi, O. Y., & Vo, X. V. (2022). The asymmetric effects of exchange rate on trade balance and output growth. *The Journal of Economic Asymmetries*, 26, e00272.