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CONFIDENTIAL

October 10, 1984

To: Members of the Executive Board
From: The Secretary
Subject: Uruguay - Real Effective Exchange Rate - Information Notice

The attached information notice on the real effective exchange rate of the Uruguayan peso is circulated for the information of the Executive Directors.

If Executive Directors have technical or factual questions relating to this paper, they should contact Mr. G. G. Johnson (ext. (5)8671).

Att: (1)



INTERNATIONAL MONETARY FUND

URUGUAY

Real Effective Exchange Rate--Information Notice

Prepared by the Western Hemisphere Department and
the Exchange and Trade Relations Department

(In consultation with the Legal Department
and the Research Department)

Approved by E. Wiesner and Manuel Guitián

October 9, 1984

The recent evolution of Uruguay's real effective exchange rate, as measured by the standard index developed in connection with the information notice system, is set out in the attached table and chart. Based on this index, as of August 1984 the new Uruguayan peso has appreciated in real effective terms by more than 10 percent since the last occasion on which the Executive Board had an opportunity to discuss the country's exchange rate policy--the Article IV Consultation in May 1984. The appreciation since May 1984 is estimated to have amounted to 15.3 percent.

Developments in exchange rate policy over the past two years were set out in detail in the last Recent Economic Developments report (SM/84/78, 4/13/84) and the paper presenting Uruguay's program for the second year of the stand-by arrangement (EBS/84/160, 7/30/84).^{1/} As noted in those documents, following the abandonment in November 1982 of the preannounced schedule of daily exchange rate adjustments, there was a sharp depreciation of the exchange rate. Thus, between the third quarter of 1982 and the first quarter of 1983 the real effective exchange rate depreciated by 43 percent (Table 1 and Chart 1). The real exchange rate appreciated moderately in the remainder of 1983. During this period the authorities intervened in the exchange market to support the exchange rate.

Since December 1983, the peso has been allowed to float freely, with intervention limited to smoothing out seasonal fluctuations in foreign exchange receipts and outlays. During the first three months of floating, the peso depreciated sharply against the U.S. dollar, and in real effective terms by 18 percent. In April and May 1984 there

^{1/} Consideration of this paper by the Executive Board has been postponed because of certain issues regarding performance in the second year of the program.

was continuing depreciation against the U.S. dollar, but some appreciation in real effective terms. The real appreciation of 15 percent between May and August reflected a small depreciation against the dollar at a time when the increase in Uruguay's cost of living index rose markedly. (Over this period Uruguay's net official international reserves declined by only US\$16 million.) In August 1984 Uruguay's real effective exchange rate was about the same as the average prevailing in 1978 and 1979, and some 40 percent below the peak recorded in the third quarter of 1982.

The pick up in the rate of inflation during the first eight months of 1984 has tended principally to reflect corrective price adjustments. Wage increases during this period have lagged behind inflation, and unit labor costs adjusted for exchange rate changes have changed relatively little. In September, however, a 15 percent general wage adjustment was granted which could compound the problems of securing a sustained lowering in the rate of inflation.

Staff Appraisal

Since December 1983 the Uruguayan authorities have limited foreign exchange intervention to the smoothing out of seasonal fluctuations in foreign exchange receipts and outlays. The recent appreciation of the Uruguayan real exchange rate has been determined overwhelmingly by the free play of market forces. The staff would note that this appreciation was preceded by a substantial real depreciation of the peso.

The staff supports the Uruguayan authorities' continued commitment to a floating exchange rate and shares their view that exchange rate stability is best attained by measures to reduce inflation. In this context, the staff would note that the recent wage award has made more difficult the task of containing inflation. The staff has been discussing with the authorities the measures that might be taken to redress the situation.

Table. Uruguay: Real Effective Exchange Rate and Related Series

(Indexes: 1980 = 100)

	Real Effective Exchange Rate <u>1/</u> <u>2/</u>	Nominal Effective Exchange Rate <u>1/</u>	Relative Consumer Prices (Local Currencies)	Exchange Rate in terms of U.S. dollars	Consumer Price Index (Seasonally Adjusted)	Consumer Price Index (Not Seasonally Adjusted)
<u>Quarterly</u>						
1979						
I	72.7	92.1	79.0	124.7	48.5	48.3
II	77.3	92.0	84.0	117.6	55.8	55.4
III	80.4	90.6	88.7	112.2	64.6	65.0
IV	89.7	94.2	95.2	108.6	75.8	76.0
1980						
I	99.5	100.3	99.2	106.0	86.5	86.4
II	100.9	101.4	99.4	102.8	94.9	94.3
III	100.7	99.3	101.4	98.4	105.2	105.6
IV	99.0	99.0	100.0	92.8	113.7	113.7
1981						
I	99.3	102.8	96.6	88.5	120.0	120.3
II	110.6	117.5	94.1	85.4	129.0	128.4
III	120.1	129.3	92.9	82.5	139.5	139.7
IV	120.3	132.7	90.6	79.6	148.1	147.8
1982						
I	122.5	146.6	83.6	76.9	149.7	150.6
II	124.1	156.0	79.5	74.1	155.2	154.7
III	130.1	173.8	74.9	70.6	162.9	162.8
IV	107.9	154.1	70.3	54.5	170.8	170.0
1983						
I	74.0	96.6	76.6	29.5	209.8	211.5
II	77.1	106.1	72.7	27.5	226.8	226.5
III	78.3	116.2	67.4	26.0	245.0	244.6
IV	76.5	122.3	62.5	23.1	271.0	269.4
1984						
I	69.3	117.1	59.1	19.0	298.5	301.1
II	69.0	120.9	57.1	17.0	340.9	340.6
<u>Monthly</u>						
1984						
May <u>3/</u>	67.8	119.5	56.7	16.8	339.7	338.3
June	72.4	125.6	57.6	16.8	361.6	359.7
July	76.1	131.1	58.0	16.3	382.4	381.8
August	78.2	137.1	57.1	16.1	398.8	397.1
Percentage change May 1984- August 1984	15.3	14.7	0.1	-4.1	17.4	17.4

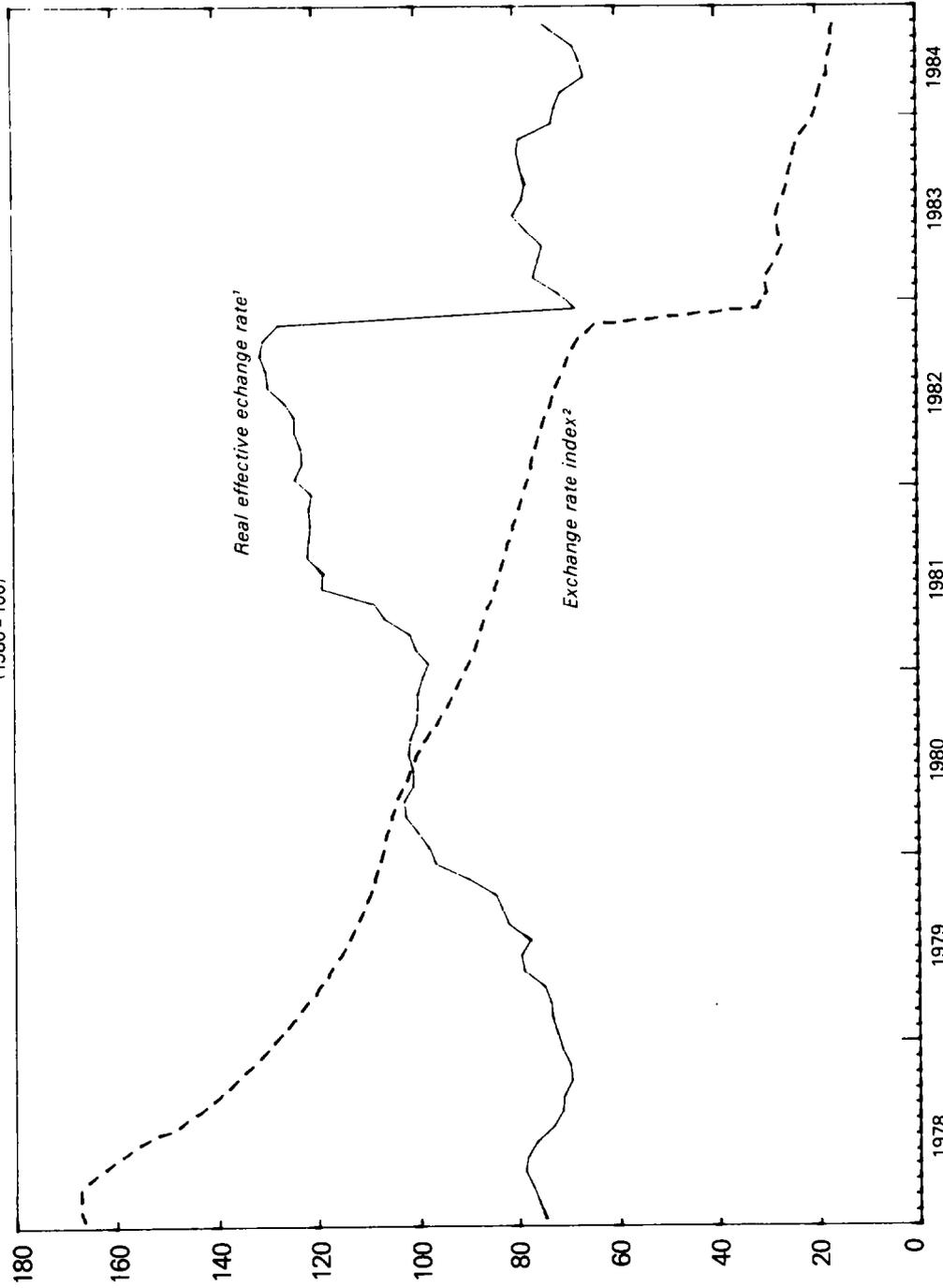
1/ Increases mean appreciation.

2/ Using seasonally adjusted price indexes.

3/ Date of latest consideration by Executive Board.



URUGUAY
INFORMATION NOTICE SYSTEM INDEX OF REAL EFFECTIVE EXCHANGE RATE
(1980=100)



¹Trade-weighted index of nominal exchange rates deflated by seasonally adjusted relative consumer prices. Increases mean appreciation.
²U.S. dollars per Uruguayan peso.

