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February 16, 1988

To: Members of the Executive Board
From: The Secretary
Subject: Vanuatu - Exchange Arrangements

Attached for the information of the Executive Directors is a paper on a recent change in the exchange arrangements of Vanuatu.

Mr. Singh (ext. 7321) is available to answer technical or factual questions relating to this paper.

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

VANUATU

Exchange Arrangements

Prepared by the Asian and Exchange and Trade Relations Departments

(In consultation with the Legal Department)

Approved by P.R. Narvekar and H.B. Junz

February 12, 1988

In the attached communication dated February 8, 1988, the authorities of Vanuatu have notified the Fund of a change in its exchange arrangements.

Effective from the close of business on February 5, 1988 the link between the vatu and the SDR which had existed since September 10, 1981 was terminated. The vatu is now pegged to an undisclosed basket of currencies.

Vanuatu is heavily dependent on tourism from Australia and, for some time, the authorities have been concerned about increased competition from other countries in the region. The new exchange arrangement would, inter alia, make it easier to maintain competitiveness of the tourist industry.

The staff will discuss the new arrangements with the authorities during the next Article IV consultation discussions, which are scheduled to take place in the latter half of 1988. No action by the Executive Board is required.

Attachment

Port Vila, Vanuatu
February 8, 1988

To: Mr. P.R. Narvekar
Director
Asian Department
International Monetary Fund

With effect from the close of business of February 5, 1988 the Central Bank, with the approval of the Minister of Finance, has delinked the vatu from the SDR and has linked it to another basket of currencies whose composition will be kept secret. In announcing this change, the Minister of Finance made the following statement: -

Quote. "For over six years now, the vatu has been linked to the Special Drawing Right (SDR). The value of vatu in terms of the SDR was fixed on September 10, 1981 at SDR 1 = VT 106.2. With effect from March 12, 1984, the vatu was revalued by 5.57 percent and the new rate fixed at SDR 1 = VT 100.6. For the first time, the vatu was devalued with effect from April 1, 1985, by 8.55 percent and the new rate fixed at SDR 1 = VT 110.0. On February 13, 1986, the vatu was again devalued, this time by 9.84 percent and vatu's parity was thus altered to SDR 1 = VT 122.0. In the same year, one more devaluation was effected - by 14.1 percent, from October 23, 1986, when the parity of vatu to SDR was changed to SDR 1 = VT 142.0.

It would be broadly correct to say that the main policy objective of these exchange rate adjustments was the containment of inflation. While this objective was largely realised, the authorities had often to cope with problems arising from speculative raids in anticipation of exchange rate adjustments by the Central Bank. Such speculative shifts of funds brought in its wake situations of excess vatu liquidity at times and of acute shortages at others. Needless to say that the speculative fervour has, if anything, received further impetus in the wake of the realignment that has been going on in the exchange rates of the major currencies triggered by the traumatic developments in stock and exchange markets the world over in October 1987.

With a view to curbing the speculative tendencies and preventing situations of temporary excesses/shortages of vatu liquidity totally unrelated to the level of economic activity in the country and also taking into account all other relevant factors including the need to bestow on the Central Bank greater measure of freedom in regard to finetuning of exchange rates, the Central Bank has, with my approval, decided to delink the vatu from the SDR with effect from the close of business on February 5, 1988 and to link it to another basket, whose composition has, of necessity, to remain a secret if the speculative elements are to be kept at bay." Unquote.

From: Central Bank of Vanuatu