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EBS/87/76

CONFIDENTIAL

April 13, 1987

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

Attached for the information of the Executive Directors is an information notice on the real effective exchange rate of the Saudi Arabian riyal.

Mr. Bélanger (ext. 8671) is available to answer technical or factual questions relating to this paper.

Att: (1)

INTERNATIONAL MONETARY FUND

SAUDI ARABIA

Real Effective Exchange Rate--Information Notice

Prepared by the Middle Eastern Department  
and the Exchange and Trade Relations Department

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

Approved by A.S. Shaalan and J.T. Boorman

April 10, 1987

The recent evolution of Saudi Arabia'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 January 1987, the Saudi Arabian riyal has depreciated in real effective terms by 12 percent since the last occasion on which the Executive Board had an opportunity to discuss developments in Saudi Arabia's exchange rate--1986 Article IV consultation in July 1986. 1/

Saudi Arabia's exchange rate policy and exchange system have remained unchanged since the last Board review. 2/ In particular, the need to maintain broadly stable rates vis-a-vis currencies of other members of the Cooperation Council for the Arab States of the Gulf (GCC), and the desire to minimize exchange risks for and to maintain the competitiveness of the private sector have continued to be important determinants of exchange rate policy. The real effective depreciation of the Saudi Arabian riyal during the seven months, July 1986-January 1987, reflects both a weakening of the riyal along with the U.S. dollar as well as a further decline in Saudi Arabia's cost of living. Though formally pegged to the SDR, the Saudi Arabian riyal was, as in the recent past, allowed to depreciate with the U.S. dollar. Over the seven months under review, the U.S. dollar depreciated against the SDR by about 7.6 percent; in the process the riyal registered a nominal effective depreciation of 7.8 percent. Over the same period, consumer prices in Saudi Arabia relative to its major trading partners declined by 4.6 percent.

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1/ The Chairman's Summing Up was circulated as SUR/86/81 (7/3/86).

2/ For a detailed description of the exchange system, see Saudi Arabia, Real Effective Exchange Rate--Information Notice (EBS/86/58, 3/11/86) and Saudi Arabia--Staff Report for the 1986 Article IV Consultation (SM/86/118, 5/29/86).

Saudi Arabia's external accounts continued to be under pressure in 1986. The current account deficit in 1986 is estimated at about US\$9 billion as compared with US\$10 billion in the previous year, or the equivalent of about 12 percent of estimated GDP. However, notwithstanding the weakened external sector situation, official foreign assets stood at US\$99 billion at the end of March 1986 (the latest period for which relevant data are available) or the equivalent of over five years of merchandise imports at the estimated 1986 level. The current account is expected to remain in deficit for the next two to three years and the continuation of the present exchange rate policy should facilitate the adjustment process.

#### Staff Appraisal

The staff believes that the depreciation of the riyal in real effective terms is consistent with the increasing importance that is being attached by the authorities to the diversification of the economy and should facilitate adjustment of the balance of payments. It provides additional opportunities for private sector investment in the traded goods sector without placing reliance on discretionary protection and government incentives, and will thereby promote the more efficient allocation of resources. This general view was endorsed by Executive Directors in concluding the 1986 Article IV consultation with Saudi Arabia.

Recent developments in the effective exchange rate and their implications for the achievement of the authorities' internal and external objectives will be reviewed with the Saudi Arabian authorities during the 1987 Article IV consultation discussions which are scheduled for mid-April 1987.

Table 1. Saudi Arabia: Real Effective Exchange Rate and Related Series

(Indices: 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 <u>1/</u>	Consumer Price Index (Seasonally Adjusted)	Consumer Price Index (Not Seasonally Adjusted)
Quarterly						
1982						
I	100.2	112.5	89.0	97.4	102.2	102.3
II	100.9	115.4	87.5	97.1	101.9	101.8
III	103.0	119.6	86.1	96.8	102.1	101.9
IV	103.2	121.0	85.3	96.8	102.2	102.3
1983						
I	100.3	118.0	85.0	96.8	102.8	102.9
II	100.5	119.9	83.8	96.6	102.5	102.5
III	100.2	123.0	81.5	96.1	100.3	100.1
IV	98.6	122.8	80.3	95.7	100.4	100.5
1984						
I	97.2	122.2	79.5	94.9	100.4	100.5
II	96.6	122.3	78.9	94.7	100.6	100.7
III	100.0	128.0	78.1	94.5	100.6	100.3
IV	99.6	129.9	76.7	93.5	99.7	99.7
1985						
I	100.8	134.6	74.9	92.8	98.3	98.4
II	94.8	129.2	73.3	92.0	97.3	97.4
III	88.6	122.6	72.3	91.3	96.4	96.2
IV	81.7	114.4	71.3	91.3	96.0	96.0
1986						
I	76.1	108.1	70.4	91.3	95.1	95.3
II	71.5	102.8	69.5	90.5	94.3	94.4
III	64.9	96.5	67.3	88.8	91.0	90.8
IV	64.1	96.3	66.6	88.8	90.9	90.9
Monthly						
1986						
June <u>3/</u>	69.1	100.5	68.8	88.8	93.2	91.1
July	66.5	97.8	68.0	88.8	92.1	90.4
Aug.	64.3	95.9	67.0	88.8	91.0	90.5
Sep.	64.0	95.7	66.9	88.8	91.0	90.5
Oct.	63.9	95.6	66.9	88.8	90.9	90.7
Nov.	64.7	97.0	66.7	88.8	90.9	90.5
Dec.	63.7	96.2	66.1	88.8	90.3	91.4
1987						
Jan.	60.8	92.6	65.7	88.8	89.8 <u>4/</u>	
Percentage change						
June 1986- Jan. 1987	-12.0	-7.8	-4.6	0.0	-3.7	

Source: Information Notice System.

1/ Increases mean appreciation.

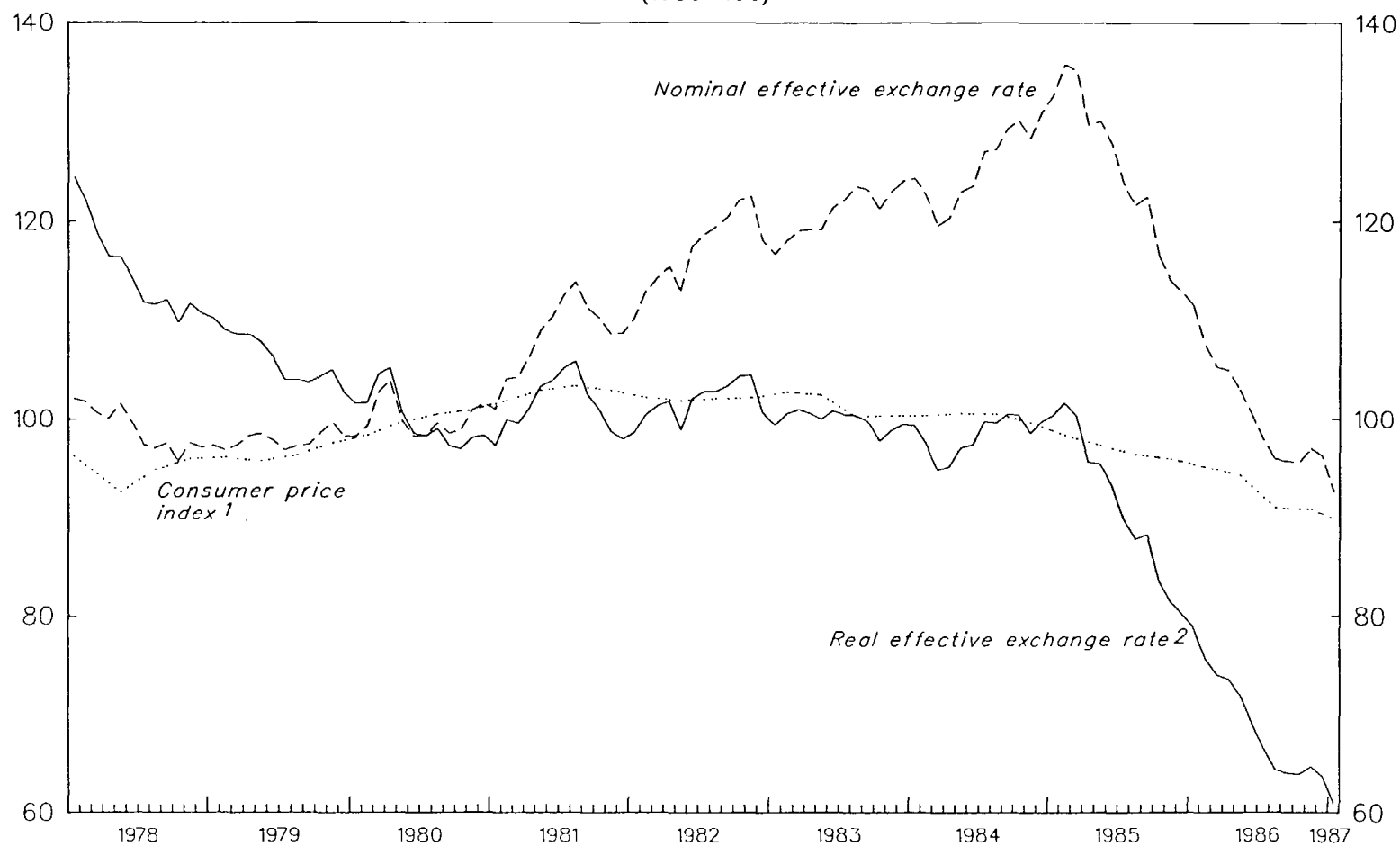
2/ Using seasonally adjusted price indices.

3/ Date of latest consideration by Executive Board.

4/ Actual price data are available only through the last quarter of 1986; data for January 1987 are extrapolated on the basis of the seasonally adjusted rate of inflation in the preceding six months.



CHART 1  
SAUDI ARABIA  
INFORMATION NOTICE SYSTEM INDEX OF REAL EFFECTIVE EXCHANGE RATE  
(1980=100)



Source: Information Notice System.

1 Seasonally adjusted.

2 Trade weighted index of nominal exchange rate deflated by seasonally adjusted consumer prices; increase means appreciation.

