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EBS/87/270

CONFIDENTIAL

December 22, 1987

To: Members of the Executive Board
From: The Secretary
Subject: Ethiopia - 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 Ethiopian birr.

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

Att: (1)

INTERNATIONAL MONETARY FUND

ETHIOPIA

Real Effective Exchange Rate - Information Notice

Prepared by the African Department and the
Exchange and Trade Relations Department

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

Approved by A.D. Ouattara and Eduard Brau

December 22, 1987

The recent evolution of Ethiopia'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 October 1987, the Ethiopian birr had depreciated in real effective terms by more than 10 percent since the last occasion on which developments in Ethiopia's exchange rate were brought to the attention of the Executive Board. 1/ The depreciation is estimated to have amounted to 11.7 percent.

Since February 1973, the birr has been pegged to the U.S. dollar at a fixed rate of Br 1 = US\$0.48309. The real effective exchange rate of the birr has thus been affected importantly by fluctuations in the exchange rate of the U.S. dollar relative to other major currencies, with sharp movements in domestic prices in Ethiopia also exerting an important influence in recent years. Despite a generally favorable relative price performance, the continued appreciation of the U.S. dollar brought the real effective exchange rate of the birr to a peak of over 70 percent above its 1980 level by mid-1985. 2/ Since then, the weakening of the birr along with the U.S. dollar, and declining domestic prices as food shortages were alleviated, brought about a real effective depreciation of the birr of some 45 percent in the period to October 1987.

1/ Ethiopia - Real Effective Exchange Rate - Information Notice, EBS/87/58, (3/11/87).

2/ Estimates of nominal and real effective exchange rates prepared for the information notice system start in 1978 only. Separate estimates reported in the staff report for the 1987 Article IV consultation indicate that the real effective exchange rate of the birr appreciated by 91 percent between January 1976 (when relatively reliable price indices became available) and June 1985. Despite the ensuing depreciation, in June 1987 the real effective exchange rate was still some 12 percent above its January 1976 level.

Exchange rate policy and developments in Ethiopia during the past few years are described in the recently issued staff report for the 1987 Article IV consultation (SM/87/266, 11/17/87) and the report on recent economic developments (SM/87/288, 12/9/87). The assessment of the staff report is that, despite the recent real effective depreciation, the exchange rate of the Ethiopian birr remains significantly overvalued and that economic performance would consequently benefit from substantial exchange rate action, including built-in flexibility, so as to enhance production and external competitiveness. It also calls for an accelerated schedule of the authorities' planned internal study of the exchange rate. The Executive Board is scheduled to conclude the 1987 Article IV consultation on December 23, 1987.

Table 1. Ethiopia: 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	116.4	129.4	90.0	100.0	112.3	110.3
II	114.8	134.2	85.5	100.0	109.8	111.4
III	119.3	140.8	84.7	100.0	112.2	113.4
IV	123.7	145.5	84.9	100.0	115.3	114.5
1983						
I	120.4	146.7	82.1	100.0	114.0	112.0
II	120.6	153.8	78.4	100.0	112.0	113.7
III	120.8	162.6	74.2	100.0	109.7	110.8
IV	121.7	167.7	72.5	100.0	110.9	110.0
1984						
I	122.6	172.1	71.2	100.0	111.9	109.9
II	130.6	176.3	74.0	100.0	119.4	121.2
III	138.5	189.3	73.1	100.0	121.4	122.8
IV	153.0	199.7	76.6	100.0	131.4	130.1
1985						
I	167.8	214.2	78.3	100.0	138.6	136.3
II	167.3	212.4	78.7	100.0	143.9	146.2
III	167.8	207.2	80.9	100.0	151.7	153.6
IV	146.6	199.4	73.5	100.0	142.0	140.4
1986						
I	132.7	192.9	68.8	100.0	136.6	134.3
II	121.9	188.6	64.6	100.0	129.8	131.9
III	113.9	182.7	62.3	100.0	126.7	128.5
IV	112.0	182.2	61.4	100.0	126.9	125.2
1987						
I	107.9	176.7	61.0	100.0	129.4	127.2
II	100.7	178.7	56.4	100.0	124.4	126.3
III	97.7	186.3	52.4	100.0	120.0	121.8
Monthly						
1987						
Mar. <u>3/</u>	106.3	177.5	59.9	100.0	128.3	126.4
April	104.0	176.3	59.0	100.0	128.0	129.9
May	99.2	177.4	55.9	100.0	123.4	125.6
June	99.0	182.3	54.3	100.0	121.8	123.5
July	98.6	186.3	52.9	100.0	119.9	118.6
Aug.	98.4	187.6	52.4	100.0	120.1	121.4
Sept.	96.1	184.9	51.9	100.0	120.1	125.3
Oct.	93.9	185.8	50.5	100.0	118.2	118.6
Percentage change						
March-Oct. 1987	-11.7	4.7	-15.7	--	-7.9	

Source: Information Notice System.

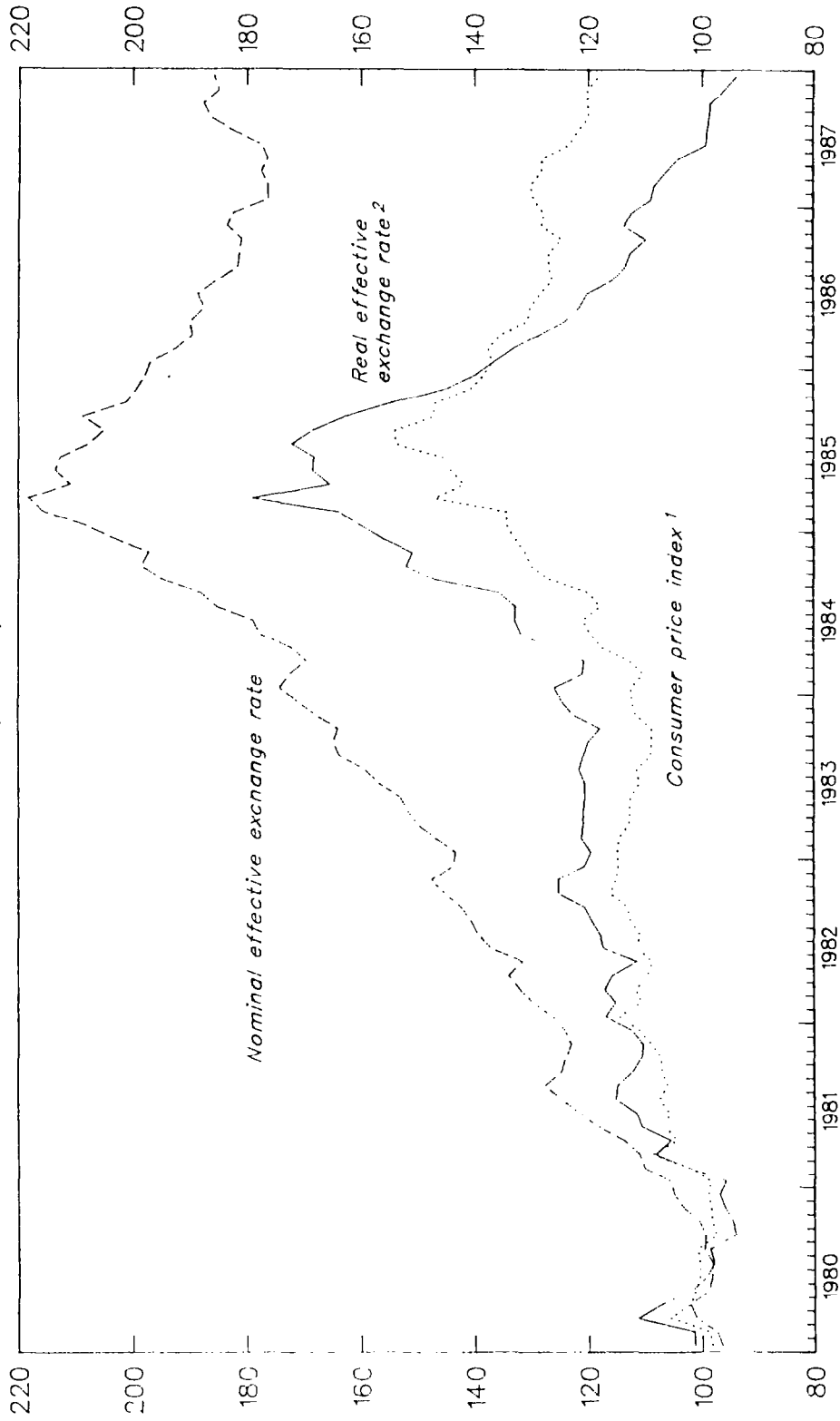
1/ Increases mean appreciation.

2/ Using seasonally adjusted price indices.

3/ Date of latest consideration by Executive Board.



CHART
ETHIOPIA
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 rates deflated by seasonally adjusted relative consumer prices; increases mean appreciation.