

EBS/86/11

CONFIDENTIAL

January 17, 1986

To: Members of the Executive Board

From: The Secretary

Nigeria - 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 Nigerian naira.

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

Att: (1)

INTERNATIONAL MONETARY FUND

NIGERIA

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 S. Kanesa-Thanan

January 17, 1986

The recent evolution of Nigeria'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 1985 the Nigerian naira had depreciated in real effective terms by more than 10 percent since the last occasion on which the Executive Board had an opportunity to discuss Nigeria's exchange rate policy--the 1985 Article IV consultation in June 1985. 1/ The depreciation is estimated to have amounted to 12.2 percent.

Since February 1978 the Nigerian naira has been linked in a flexible manner to a basket which is composed of the currencies of Nigeria's seven principal trading partners and reflects their share in Nigeria's imports. Frequently, exchange rate quotations have resulted in large broken cross-rates, notably in the case of the U.S. dollar and the pound sterling; these, however, have recently declined in magnitude.

From January 1981 to December 1984, the cumulative depreciation of the naira against the dollar amounted to 34 percent. However, in view of the concurrent appreciation of the U.S. dollar, the naira appreciated by 19 percent in nominal effective terms during this period. Reflecting the relatively high domestic inflation rate, the appreciation of the naira in real effective terms was even more pronounced, reaching 74 percent. This appreciation has since been partly reversed as the continued depreciation of the naira vis-à-vis the U.S. dollar and improved domestic price performance have resulted in depreciations of 11.6 percent in real effective terms during the first semester of 1985 and a further estimated 12.2 percent from June to October. 2/

1/ Chairman's Summing-Up circulated as SUR/85/68 (6/21/85).

2/ From July onward seasonally adjusted consumer price data are extrapolated.

Staff Appraisal

At the conclusion of the 1985 Article IV consultation on June 17, 1985, Executive Directors noted with considerable concern that in 1984 the Nigerian economy had experienced for the fourth consecutive year a combination of economic recession and high inflation, and that further import payments arrears had accumulated. Directors noted that the fiscal deficit had been reduced in 1984, but observed that an adjustment strategy based solely on fiscal retrenchment increased the adjustment burden in terms of reduced growth and employment levels. Most Directors stressed that in particular a shift toward a realistic and flexible exchange rate policy, beginning with a substantial exchange rate adjustment, was needed to correct relative price distortions, bolster investor and consumer confidence, stabilize expectations, stem capital flight, and create an environment conducive to orderly and steady economic recovery. Directors also urged fundamental reforms in the trade system, including less reliance on administrative controls and countertrade arrangements and the adoption of appropriate tariff policies.

Since the last Article IV consultation, the authorities have continued to rely primarily on demand restraint and administrative controls in their attempt to restore internal and external balance. No progress has been made in liberalizing the trade system, and indeed, in October 1985 imports of certain staple foods were prohibited until further notice. Developments in the effective exchange rate of the naira since the end of 1984, while in the appropriate direction, appear insufficient to stem the excess demand for foreign exchange, especially in light of the recent weakening of the international petroleum market. In the recent Budget statement for 1986, the authorities announced their intention to introduce a two-tier foreign exchange market. The Executive Board will be provided with information on the system as soon as it is put into effect.

A comprehensive package of adjustment policies, including measures to correct deep-rooted structural problems and cost-price distortions continues to be required. Nigeria is on the standard 12-month Article IV consultation cycle, and the staff mission to conduct the 1986 Article IV consultation discussions is tentatively planned for March 1986.

Table 1. Nigeria: 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						
1981						
Q1	113.8	106.7	106.7	99.3	114.6	113.1
Q2	113.6	105.6	107.6	90.4	119.0	119.6
Q3	111.1	102.4	108.5	81.5	123.2	125.1
Q4	111.8	103.2	108.4	85.0	126.4	125.5
1982						
Q1	113.5	105.5	107.7	83.4	128.3	126.6
Q2	112.0	106.3	105.4	81.1	128.4	128.9
Q3	114.4	110.3	103.7	80.2	129.0	131.2
Q4	120.6	115.5	106.5	79.9	133.7	133.7
1983						
Q1	124.7	112.7	110.6	79.4	142.3	140.4
Q2	130.3	112.5	115.9	76.6	151.9	152.6
Q3	139.0	112.9	123.2	73.1	165.1	168.0
Q4	152.9	115.3	132.6	73.0	182.0	180.4
1984						
Q1	164.6	117.3	140.4	73.0	196.5	193.7
Q2	186.9	118.7	157.4	72.8	224.2	225.5
Q3	204.4	124.3	164.6	71.2	238.5	242.8
Q4	200.8	126.3	159.1	69.0	235.4	233.3
1985						
Q1	199.6	126.1	158.3	64.5	239.2	235.5
Q2	177.9	114.9	154.9	61.4	238.9	240.3
Q3	164.0	107.4	152.8	60.6	239.0	
Monthly						
1985						
June <u>3/</u>	173.8	113.7	152.9	61.1	237.3	240.3
July	167.0	109.3	152.9	61.1	238.1 <u>4/</u>	
Aug.	163.1	106.8	152.8	60.9	239.0	
Sept.	161.9	106.1	152.7	59.7	239.8	
Oct.	152.6	100.1	152.6	59.2	240.7	
Percentage						
Jun 1985-						
Oct 1985	-12.2	-12.0	-0.2	-3.0	1.4	

Source: Information Notice System.

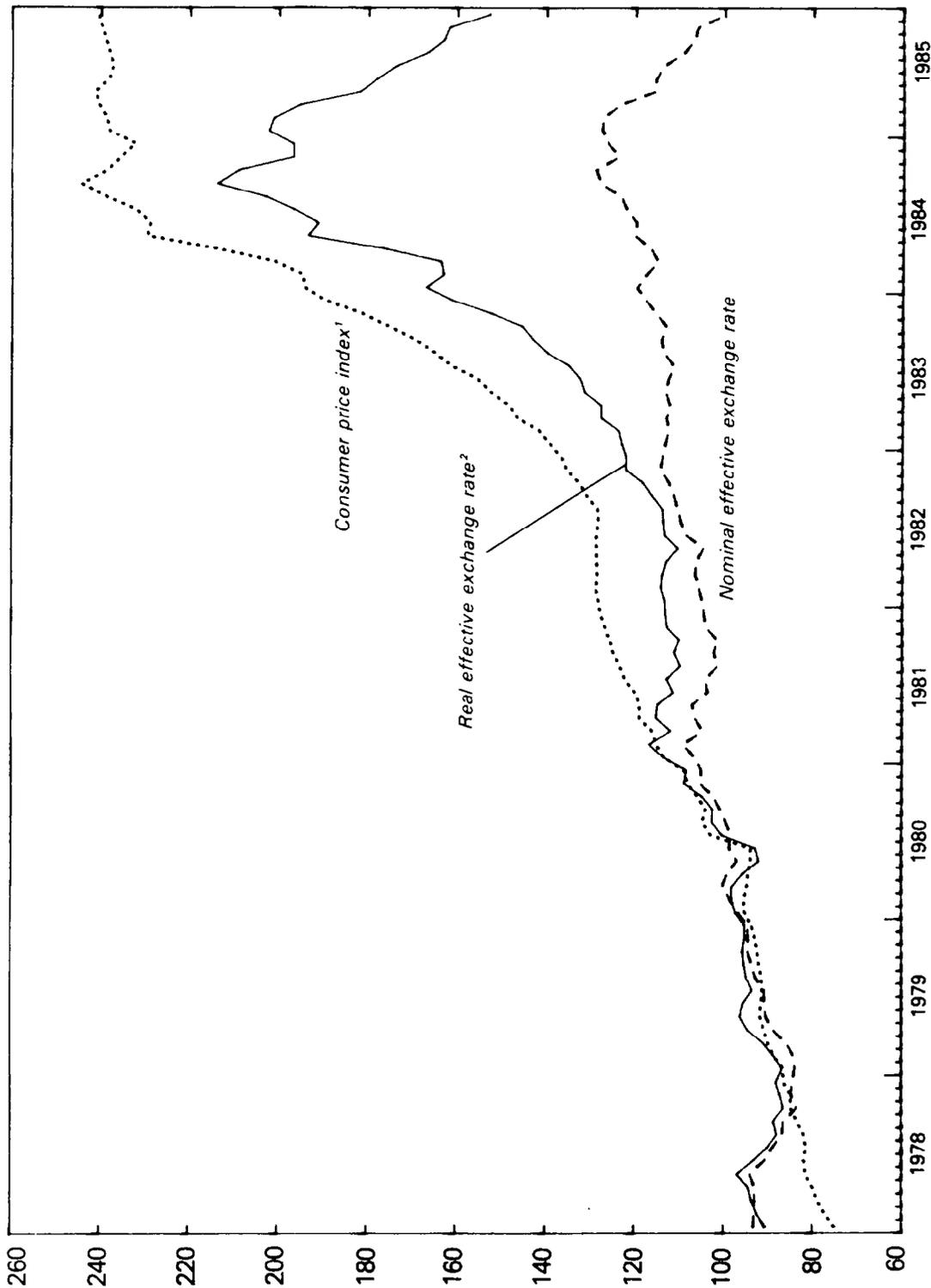
1/ Increases mean appreciation.

2/ Using seasonally adjusted price indices.

3/ Date of latest consideration by Executive Board.

4/ From July onward data are extrapolated.

CHART
NIGERIA
REAL EFFECTIVE EXCHANGE RATE AND RELATED SERIES
(1980 = 100)



Source: Information Notice System.
1 Seasonally adjusted.
2 Trade weighted index of nominal effective exchange rate deflated by seasonally adjusted consumer prices; increase means appreciation