

DOCUMENT OF INTERNATIONAL MONETARY FUND AND NOT FOR PUBLIC USE

MASTER FILES

ROOM C-120

01

EBD/86/213

August 5, 1986

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

The Secretary has received the following memorandum dated August 4, 1986 from Mr. Leonard:

I have received from my authorities in Ireland a copy of a communiqué issued by the Monetary Committee of the European Communities on August 2, 1986 and a copy of a statement issued on the same date by the Minister for Finance of the Irish Government on the adjustment of the central rate for the Irish pound in the EMS.

Copies of the communiqué and the statement are attached and I would be glad if you would circulate their contents to members of the Executive Board.

Attachments

Other Distribution:
Department Heads

MONETARY COMMITTEE
OF THE EUROPEAN COMMUNITIES

Brussels, August 2, 1986

C O M M U N I Q U E

On August 2, 1986, the Ministers and Central Bank Governors of the EEC member countries have by mutual agreement, in a common procedure involving the Commission and on the basis of a proposal from the Monetary Committee, decided on an adjustment of central rates within the European Monetary System as follows:

The Irish pound is adjusted downward by 8 percent vis-à-vis all other participating currencies.

The new ECU central rates are the following:

(in units of national currency per ECU)

LIT	1476.95
FF	6.87316
DM	2.11083
HFL	2.37833
BFR	43.1139
LFR	43.1139
DKR	7.81701
IRL	0.764976
UKL	0.679256
DRA	137.049

The new bilateral central rates and the compulsory intervention rates will be communicated by the monetary authorities in time for the opening of foreign exchange markets on August 4, 1986.

Statement by the Minister for Finance,
Mr. John Bruton T. D., on the adjustment of
the central rate for the Irish pound in the EMS

The Government, after consultation with the Central Bank, has sought and received the agreement of our EEC partners to a downward adjustment of 8 percent in the central rate for the Irish pound in the EMS.

The need for this adjustment arose from the recent sharp drop in the value of both the U.S. dollar and sterling. These two currencies account for over half of our exports and imports and their exchange rates are of major importance for Irish trade and the competitiveness of the Irish economy. The depreciation of these currencies has resulted in an unsought appreciation of the value of the Irish pound which, if maintained, would seriously damage our competitive position and would give rise to a danger of a significant loss of output and jobs in Ireland.

The exchange rate policy which has been followed since our entry into the EMS has been to maintain the stability of the Irish pound within that system. This is the appropriate policy for a small economy like ours, which is so open as regards both trade and other flows, and this policy has made a significant contribution to the reduction in the rate of inflation in recent years.

However, both the size of the recent movements in sterling and the U.S. dollar and especially the speed with which they have taken place have made it extremely difficult for the economy to adjust. This unplanned appreciation of the Irish pound would have a disproportionate effect on the exposed traded sector of the economy, affecting jobs, profits and investment in a way that would not have been suitable for balanced economic development. The immediate adverse effects on Irish output would be too great for Irish industry to bear while awaiting the feed-through of the favorable effects.

At the time of the general EMS realignment in April 1986, the Irish pound was kept with the middle group of currencies, neither revaluing nor devaluing. The present downward adjustment of the Irish pound will reverse the unsought appreciation of the currency since then. It will mean inflation will not fall to the extremely low levels which were predicted on the basis of recent exchange rates, but inflation in 1987 will be significantly below that of 1985 and earlier years.

For the full benefits of this exchange rate adjustment to be reaped, it is essential that it should not be used as a basis for higher income demands. Pay settlements so far this year, including the public sector agreement, do not adequately reflect the benefits of the current and the prospective reduction in inflation. Similarly, the social welfare

- 2 -

increases granted in the 1986 Budget have provided greater real increases than were expected, because of the favorable effects of the lower oil prices and the currency appreciation since the 1986 Budget. Lower actual inflation has resulted in their providing significantly higher real income increases than was expected at the time when the agreements were made. The more realistic level of the exchange rate will protect our competitive position and will enhance the prospect for securing satisfactory growth of output this year and for safeguarding employment.

Membership of the EMS has brought a wide and substantial range of benefits to the economy, not all of them measurable in monetary terms. As this experience shows, however, the absence of sterling from the EMS exchange rate mechanism makes Irish participation in it somewhat more difficult than would otherwise be the case. It should be stressed, however, that Ireland's dependence on trade with the United Kingdom is diminishing over time. While it would be more satisfactory from Ireland's point of view if sterling also participated in the exchange rate system, that decision is essentially one for the United Kingdom, but member countries, including Ireland, have made it clear that they would welcome participation by the United Kingdom. The Government is of the view that it is overwhelmingly in the national interest to remain a fully-participating member of the EMS.

August 2, 1986