

EBS/85/236

CONFIDENTIAL

October 25, 1985

To: Members of the Executive Board  
From: The Secretary  
Subject: Paraguay - 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 Paraguayan guarani.

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

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INTERNATIONAL MONETARY FUND

PARAGUAY

Real Effective Exchange Rate--Information Notice

Prepared by the Western Hemisphere Department and the  
Exchange and Trade Relations Department

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

Approved by Marcello Caiola and Manuel Guitián

October 25, 1985

The recent evolution of Paraguay'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. Based on this index, as of August 1985 the Paraguayan guarani had depreciated in real effective terms by more than 10 percent since the last occasion on which developments in Paraguay's exchange rate were brought to the attention of the Executive Board--the notification of a change in Paraguay's exchange rate system in March 1985. <sup>1/</sup> The depreciation is estimated to have amounted to 27.0 percent.

Over the past several years, Paraguay has maintained a complex system of multiple exchange rates that severely penalizes exports and that highly subsidizes government debt service payments and petroleum imports. Since March 1985, when the exchange system was last modified, the following four basic exchange rates have been in effect: (a) ¢ 160 per U.S. dollar for public sector capital and external debt service payments and for transactions related to the Itaipu and Yacyreta hydroelectric projects; (b) ¢ 240 per U.S. dollar for 50 percent of exports at the minimum prices set by the Central Bank, for private capital transactions, and for imports of petroleum and agricultural and industrial inputs; (c) ¢ 400 per U.S. dollar for the remaining 50 percent of export proceeds based on minimum export prices; and (d) a free market exchange rate of currently around ¢ 300 per U.S. dollar for all other imports, profit remittances, and service payments, as well as for that part of export proceeds corresponding to the difference between the actual export price and the minimum export price set by the Central Bank.

The exchange rate index used in the information notice system, which is a composite of the four exchange rates mentioned above, depreciated against the U.S. dollar by 33.5 percent between March 1985 and August 1985 (Table 1). This has reflected mainly the movement in

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<sup>1/</sup> EBD/85/82 (3/21/85).

the free market exchange rate over this period from ¢ 420 per U.S. dollar to ¢ 800 per U.S. dollar, which has contributed to the marked widening in the spread between the effective rates for exports and imports (Chart 1). Despite the pick up in the 12-month rate of inflation as measured by the official consumer price index to around 30 percent in recent months, Paraguay has maintained unaltered all other exchange rates in relation to the U.S. dollar.

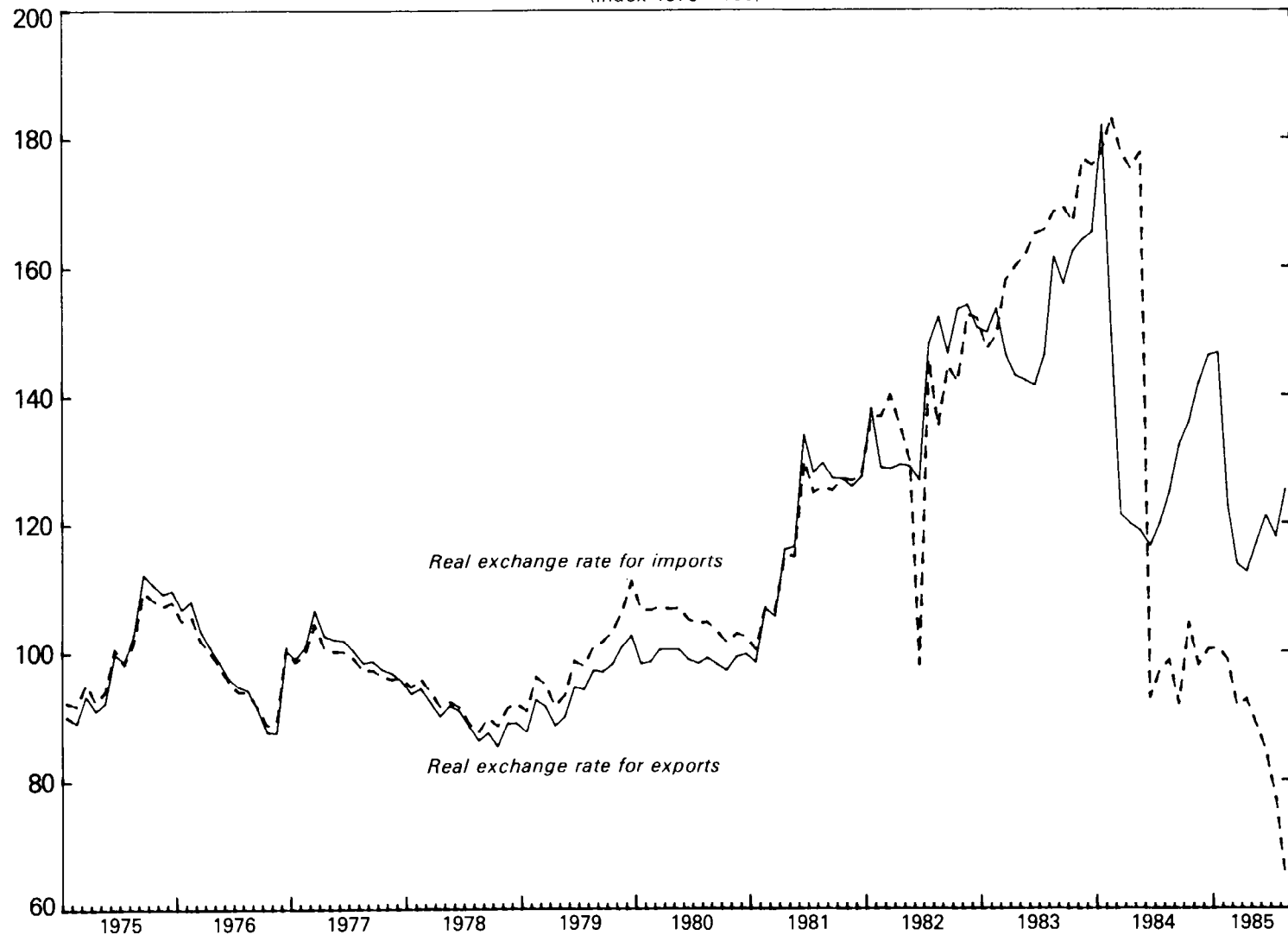
The recent sharp depreciation of the free market exchange rate has occurred against the background of a loose stance of demand management policies and a significant deterioration in Paraguay's balance of payments. A primary factor in the weakening in the external accounts in recent years has been the lower net foreign exchange inflows associated with the construction of the Itaipu and Yacyreta hydroelectric projects. These inflows, which had reached a peak of US\$450 million in 1981, have declined steadily to an estimated level of US\$70 million in 1985. Additional factors exerting pressure on Paraguay's external accounts were a considerable easing in credit policy and the maintenance of an overly appreciated exchange rate for exports. The latter manifested itself in a significant decline in overall export earnings from the levels reached in the early 1980s.

In concluding the 1984 Article IV consultation with Paraguay, <sup>1/</sup> Directors underlined the drawbacks of Paraguay's system of multiple exchange rates and they urged that measures be taken toward the unification of the exchange rate at a realistic level. Discussions were recently concluded with the Paraguayan authorities for the 1985 Article IV consultations. The staff report for the consultation, which is expected to be circulated to the Board in November, will include a detailed review of recent developments in the exchange rate of the guarani and an appraisal of their implications for policy.

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<sup>1/</sup> At EBM/85/5(1/11/85). The Chairman's summing-up was circulated as SUR/85/4.

CHART 1  
PARAGUAY  
REAL EFFECTIVE EXCHANGE RATE<sup>1</sup>  
(Index 1975 = 100)



<sup>1</sup>Based on average exchange rates applicable to Paraguay's registered trade in terms of relative consumer prices. An increase in the index reflects a real appreciation of the exchange rate.



Table. Paraguay: 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)
<b>Quarterly</b>						
<b>1980</b>						
I	101.3	94.2	107.3	100.0	92.4	92.9
II	101.9	98.4	103.2	100.0	98.7	98.1
III	99.2	101.0	97.9	100.0	102.7	102.5
IV	97.7	106.4	91.5	100.0	106.2	106.6
<b>1981</b>						
I	101.5	116.3	87.0	100.0	111.1	111.5
II	114.7	143.5	79.9	100.0	114.4	113.6
III	119.8	167.1	71.5	100.0	114.7	114.5
IV	119.1	181.3	65.5	100.0	115.7	116.4
<b>1982</b>						
I	120.9	200.1	60.3	93.1	118.7	119.1
II	117.6	210.8	55.6	86.7	120.9	119.9
III	123.9	254.5	48.7	85.1	121.4	121.3
IV	135.2	306.9	44.0	85.1	125.7	126.6
<b>1983</b>						
I	138.1	349.9	39.5	81.8	131.1	131.5
II	144.1	416.7	34.5	80.8	134.5	133.4
III	142.9	474.9	30.1	77.2	141.6	141.6
IV	146.5	592.5	24.7	78.1	144.6	145.7
<b>1984</b>						
I	149.0	701.1	21.2	76.7	149.8	150.2
II	115.1	629.5	18.1	58.3	158.8	157.1
III	88.7	560.7	15.8	40.9	170.6	170.6
IV	102.6	751.4	13.7	42.3	184.9	186.3
<b>1985</b>						
I	103.4	933.2	11.1	40.3	189.4	189.9
II	85.6	966.5	8.9	32.4	197.0	194.8
<b>Monthly</b>						
<b>1985</b>						
March <u>3/</u>	96.7	938.5	10.3	37.1	191.5	191.9
April	88.3	926.8	9.5	34.9	194.2	192.3
May	85.1	958.9	8.8	31.9	197.5	194.9
June	83.5	1,013.8	8.2	30.3	199.3	197.1
July	78.3	984.9	7.9	28.9	199.5	198.3
August	70.6	846.4	8.3	24.6	217.6	218.5
<b>Percentage change</b>						
March 1985- Aug. 1985	-27.0	-9.8	-19.0	-33.5	13.6	

Source: Information Notice System.

- 1/ Increases mean appreciation.  
2/ Using seasonally adjusted price indices.  
3/ Date of latest consideration by Executive Board.

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