

EBS/85/292

CONFIDENTIAL

December 27, 1985

To: Members of the Executive Board
From: The Acting 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. Belanger (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 S. Kanesa-Thanan

December 27, 1985

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 1985 the Ethiopian birr has depreciated in real effective terms by 10 percent since the last occasion on which developments in Ethiopia's exchange rate were brought to the attention of the Executive Board--the Article IV consultation in June 1985. 1/

The Ethiopian birr has been pegged to the U.S. dollar at an exchange rate of Br 1 = US\$0.48309 since February 1973. In nominal terms the birr has appreciated by 72 percent since 1980, reflecting the strength of the U.S. dollar relative to the currencies of Ethiopia's major trading partners. Until 1984, the relatively moderate rate of inflation in Ethiopia had limited the impact of the nominal appreciation on the real effective exchange rate. Over the 12 months from March 1984, however, consumer prices rose by 31 percent, resulting in a sharp acceleration of the pace of real effective appreciation. The increase in consumer prices over this period principally reflected the severe food scarcity resulting from the very serious shortfall in agricultural production that occurred in 1984/85. More recently, the large scale international and domestic relief efforts have been reflected in a sharp slowdown in the rate of inflation. This, along with the weakening of the U.S. dollar in recent months, has resulted in a depreciation of the birr in real effective terms equivalent to 16 percent since March 1985. Despite such recent developments, the real effective appreciation since 1980 still amounted to 49 percent by October 1985.

1/ Chairman's summing up circulated as SUR/85/66 (6/20/85).

Staff Appraisal

In concluding the 1985 Article IV consultation with Ethiopia, Directors expressed their concern about the balance of payments outlook, the low level of reserves, and the sharply increased debt burden. While praising the efforts of the authorities to contain the external deficit, Directors noted the need for measures to contain the budget deficit. Most Directors also stressed that the appreciation of the real value of the birr should be reversed and a more active and flexible exchange rate policy be considered. In light of the emergency balance of payments situation associated with the drought, temporary approval was also granted of certain restrictions on the making of payments and transfers for international transactions. Despite the recent depreciation in real effective terms, the staff notes that a substantial part of the earlier real appreciation remains. At the same time, however, recent discussions with the Ethiopian authorities indicate that some progress has been made on demand management and that the financial imbalances foreseen earlier in 1985 have been substantially contained in the latter half of the fiscal year.

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 | | | | | | |
| 1980 | | | | | | |
| I | 104.2 | 98.4 | 105.6 | 100.0 | 100.7 | 99.1 |
| II | 102.4 | 99.8 | 102.6 | 100.0 | 101.2 | 102.1 |
| III | 97.1 | 99.1 | 98.0 | 100.0 | 99.6 | 101.0 |
| IV | 96.3 | 102.7 | 93.8 | 100.0 | 98.5 | 97.8 |
| 1981 | | | | | | |
| I | 103.0 | 108.2 | 95.1 | 100.0 | 103.1 | 101.4 |
| II | 110.3 | 116.8 | 94.4 | 100.0 | 105.5 | 106.9 |
| III | 115.3 | 123.9 | 93.0 | 100.0 | 106.9 | 108.1 |
| IV | 111.4 | 120.6 | 92.3 | 100.0 | 109.0 | 108.2 |
| 1982 | | | | | | |
| I | 117.0 | 125.7 | 93.1 | 100.0 | 112.3 | 110.3 |
| II | 115.4 | 129.9 | 88.8 | 100.0 | 109.8 | 111.4 |
| III | 120.4 | 136.2 | 88.4 | 100.0 | 112.4 | 113.4 |
| IV | 124.4 | 140.1 | 88.7 | 100.0 | 115.0 | 114.5 |
| 1983 | | | | | | |
| I | 120.1 | 138.7 | 86.5 | 100.0 | 114.0 | 112.0 |
| II | 119.5 | 143.8 | 83.1 | 100.0 | 112.0 | 113.7 |
| III | 120.6 | 150.9 | 79.9 | 100.0 | 110.0 | 110.8 |
| IV | 120.8 | 154.8 | 78.0 | 100.0 | 110.4 | 110.0 |
| 1984 | | | | | | |
| I | 121.7 | 157.5 | 77.2 | 100.0 | 112.1 | 109.9 |
| II | 128.9 | 159.9 | 80.6 | 100.0 | 119.4 | 121.2 |
| III | 137.8 | 171.0 | 80.5 | 100.0 | 122.0 | 122.8 |
| IV | 150.7 | 179.4 | 83.9 | 100.0 | 130.5 | 130.1 |
| 1985 | | | | | | |
| I | 166.7 | 191.1 | 87.2 | 100.0 | 139.0 | 136.3 |
| II | 164.8 | 187.2 | 88.0 | 100.0 | 143.9 | 146.2 |
| III | 165.3 | 180.4 | 91.6 | 100.0 | 152.7 | 153.6 |
| Monthly | | | | | | |
| 1985 | | | | | | |
| Jun <u>3/</u> | 166.0 | 186.8 | 88.8 | 100.0 | 146.1 | 147.9 |
| Jul. | 166.2 | 182.0 | 91.2 | 100.0 | 151.4 | 152.8 |
| Aug. | 166.9 | 178.4 | 93.5 | 100.0 | 155.9 | 155.2 |
| Sept. | 162.9 | 180.7 | 90.1 | 100.0 | 150.8 | 152.8 |
| Oct. | 149.3 | 172.1 | 86.7 | 100.0 | 146.3 | 147.9 |
| Percentage change | | | | | | |
| June 1985- Sep. 1985 | -10.0 | -7.9 | -2.3 | -- | 0.1 | |

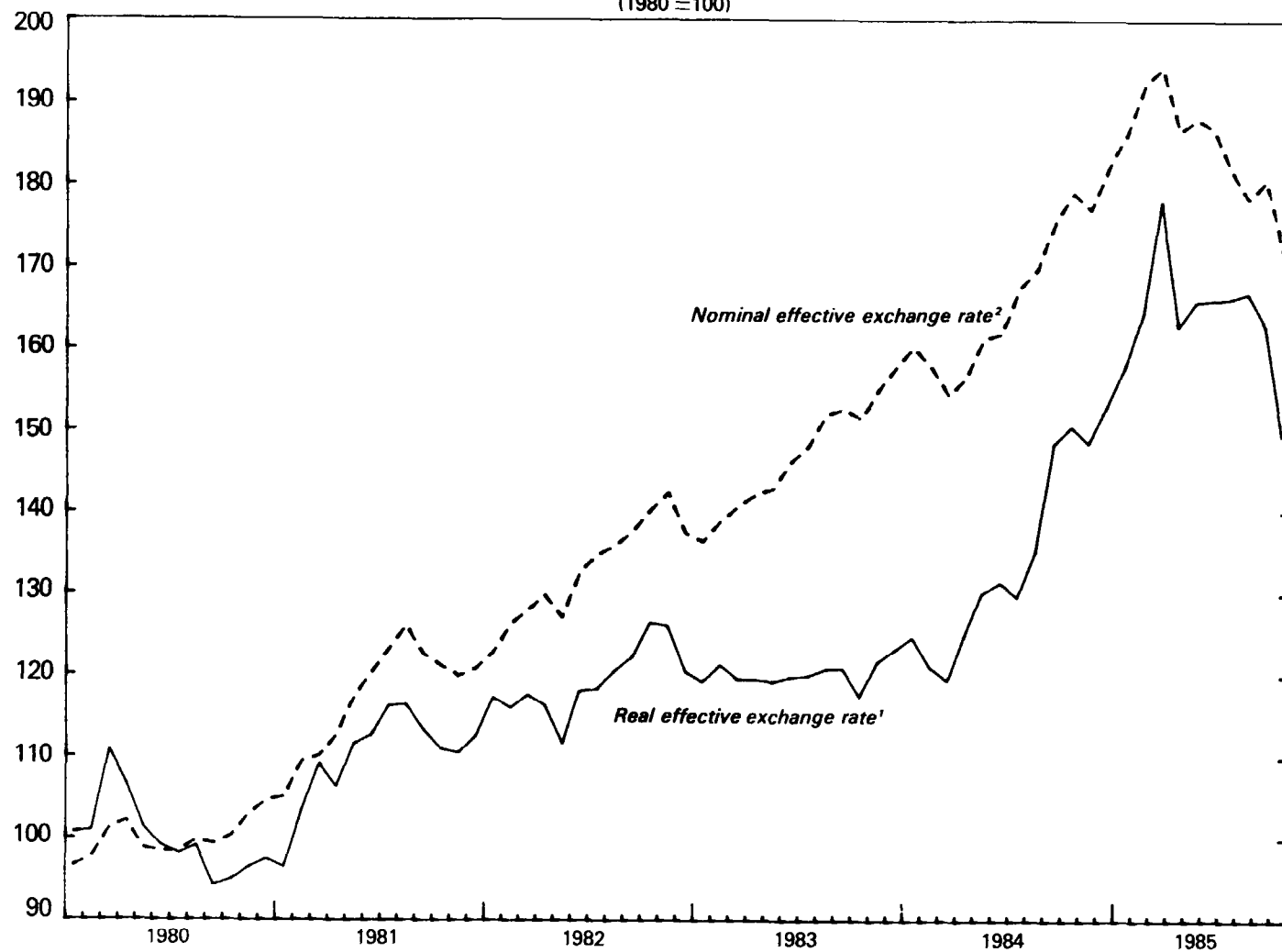
Source: Information Notice System.

1/ Increases mean appreciation.

2/ Using seasonally adjusted price indices.

3/ Date of latest consideration by Executive Board.

CHART
ETHIOPIA
EXCHANGE RATE DEVELOPMENTS
(1980 = 100)



Source: Information Notice System.

¹Trade weighted index of nominal exchange rates deflated by seasonally adjusted relative consumer price; increase mean appreciations.

²Trade-weighted index of nominal exchange rates.