



IMF Strengthening Framework for Exchange Rate Surveillance

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The International Monetary Fund (IMF) is releasing today the [staff report](#) on the revised and extended methodologies for exchange rate assessments by the IMF's Consultative Group on Exchange Rate Issues (CGER)¹. The IMF Executive Board recently discussed the report in an informal Board seminar. The report is part of a broader effort to extend and deepen the IMF's framework for assessing exchange rate issues in line with its ongoing work to strengthen Fund surveillance of the global economic and financial system.

The methodologies for assessing exchange rates have been applied beyond advanced countries to cover about 20 emerging market countries using a variety of approaches.² The three complementary methodologies presented in the staff report provide a multilateral approach to help gauge the consistency of current account balances and real effective exchange rates with their underlying fundamentals. Combined with additional country-specific information, the methodologies help IMF staff reach informed judgments about medium-term real exchange rates and current account balances, weighing the relative importance of a number of economic factors affecting these key variables. The three methodologies are as follows:

- The macroeconomic balance approach—a pillar of current account and exchange rate assessments for a number of years—calculates the difference between the current account balance projected over the medium term at prevailing exchange rates and an estimated equilibrium current account balance.
- The reduced-form equilibrium real exchange rate approach estimates directly an equilibrium real exchange rate for each country as a function of medium-term fundamentals such as the net foreign asset position of the country, productivity growth in the tradables and nontradables sectors, and the terms of trade.
- The external sustainability approach calculates the difference between the actual current account balance and the balance that would stabilize the net foreign asset position of the country at some benchmark level.

Exchange Rate Assessments in Country Surveillance

The IMF is also continuing to strengthen surveillance of exchange rate issues in bilateral consultations with member countries. A recent [review](#) concluded that for 30 large economies accounting for more than 90 percent of world GDP, significant progress has been made in the way the IMF is covering exchange rate issues. As summarized in a [Public Information Notice](#), the review concluded that almost all recent Article IV reports in the sample provide: an accurate description of the de facto exchange rate regime; an assessment of its adequacy, given the specific feature of the relevant economy; an analysis of the consistency between exchange rate and other policies and external stability; and an assessment of exchange rate misalignments. Views on misalignments were often expressed in qualitative terms, but in many cases quantitative estimates—typically in the form of ranges—were also included. However, there is room for further improvement: in a number of cases, staff reports could have provided a richer analytical discussion of the factors considered by staff to reach conclusions about exchange rate misalignments. In this respect, the work of the Consultative Group will provide stronger analytical bases for the exchange rate analysis in the context of Article IV surveillance. Most Article IV papers covered by this review were also published.

Exchange Arrangement Reports

Further, the IMF is continually strengthening the process of reviewing developments and issues related to exchange arrangements, restrictions, and markets and issuing periodic reviews on the trends and developments. This includes the *Annual Report on Exchange Rate Arrangements and Restrictions*, which provides a description of the foreign exchange arrangements, exchange and trade restrictions, and relevant prudential measures of individual IMF member countries. The recently released *2006 Annual Report* incorporates changes in structure and content aimed at providing a more accurate and updated description

of the regulatory framework for current and capital account transactions.

Review of Keystone Surveillance Decision

To ensure that the foundations of IMF surveillance are clear and relevant to today's international monetary system, the IMF is reviewing the [1977 Decision on Surveillance over Exchange Rate Policies](#), which was drafted in the wake of the collapse of the Bretton Woods system of fixed exchange rate parities.

¹ The CGER has provided exchange rate assessments for a number of advanced economies since the mid-1990s.

² *Original CGER countries in the extended sample:* Australia, Canada, Japan, Sweden, Switzerland, United Kingdom, United States, euro area.

Emerging market countries: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Hungary, India, Indonesia, Israel, Korea, Malaysia, Mexico, Pakistan, Poland, Russia, South Africa, Thailand, and Turkey.

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