

AFRICAN DEVELOPMENT FUND



Exchange Rate Determination for ADF-XI (Background Paper #9)

ADF-XI Replenishment Meeting

14 – 15 March 2007

Dar-es-salaam, Tanzania

1. BACKGROUND

1.1 Under previous ADF replenishments, state participants have denominated their subscriptions in SDRs, in a currency used for the valuation of the SDR or in the currency of the state participant if such currency is freely convertible. The exchange rate used in the determination of the currency amount has typically been an average rate based on a six-month period ending before the conclusion of the negotiations. However, if during a specified period a state participant has experienced a rate of inflation in excess of 10% per annum on average, as determined by the Fund, the subscription of that state participant shall be denominated in SDRs. The inflation test is intended to help minimize the loss in the value of replenishment resources, attributable to depreciation in the national currencies of state participants with high domestic inflation rates.

2. BASIS FOR RECOMMENDATIONS

2.1 To avoid protracted discussions regarding the selection of rates, it is important that the state participants agree early in the replenishment negotiations on the reference period to be used to determine the average rate to be used. In making this determination, we propose that the same criteria as those used for prior replenishments and also for IDA be used. These criteria are as follows:

1. *Sufficient lead time*: to facilitate the process of obtaining pledging authorisations, state participants should be allowed sufficient lead time to determine the national currency amounts required to meet a specific share or SDR replenishment objective.
2. *Future dates*: the exchange rate period chosen should avoid using known rates to the extent feasible.
3. *Minimize effect of short-term currency fluctuations*: the method for determining exchange rates should mitigate short-term currency fluctuations. As a rule of thumb, a six-month period is deemed to assure this purpose.

Decision(s) Required:

ADF-XI Exchange Rate Reference Period

Recommendations / Proposal:

Deputies:

- At the *March 2007* meeting, agree on a future 6-month period over which the ADF XI exchange rates would be averaged. On the assumption that the negotiations are expected to be completed by *31 December 2007*, we propose the use of the six-month period ending *30 September 2007*.

- Also at the first meeting, agree that the period *2004-2006* would be used for purposes of the inflation rate test and that a 10% threshold should be used.

As additional background, we present as Annex 1 a summary of recent exchange rate averaging periods.

ANNEX 1

SUMMARY RECENT EXCHANGE RATE AVERAGING PERIODS			
Replenishment	Replenishment Period	Averaging Period	Inflation Period
ADF-V	1988 - 1990	Six Months ending 31 October, 1987	
ADF-VI	1991 - 1993	Six Months ending 31 December, 1990	
ADF-VII	1996 - 1998	Six Months ending 31 October, 1995	
ADF-VIII	1999 - 2001	Six Months ending 31 October, 1998	1996-1998
ADF-IX	2002 - 2004	Six Months ending 30 November, 2001	1998-2000
ADF-X	2005 - 2007	Six Months ending 30 September, 2004	2001-2003