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# Exchange Rate Dynamics – Overvalued or Undervalued

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## Nominal / Real Effective Exchange Rate Indices of Pak Rupee

( Base 2018 = 100)

| Month  | Average          |          | Percentage Change over last Year  |        |
|--------|------------------|----------|-----------------------------------|--------|
|        | NER              | REER     | NER                               | REER   |
| Jun-16 | 89.2898          | 117.1399 | 0.74                              | 0.28   |
| Jun-17 | 90.9091          | 121.0066 | 1.81                              | 3.13   |
| Jun-18 | 78.4221          | 107.4833 | -13.82                            | -11.18 |
| Jun-19 | 62.8885          | 96.9767  | -19.81                            | -10.36 |
| Jun-20 | 99.7676          | 93.0417  | 4.96                              | 1.27   |
|        | Monthly Position |          | Percentage Change over last Month |        |
| Sep-18 | 77.8366          | 106.0149 | -8.03                             | -8.65  |
| Oct-18 | 74.3638          | 103.1371 | -4.71                             | -2.71  |
| Nov-18 | 72.7696          | 101.4948 | -1.88                             | -1.59  |
| Dec-18 | 70.0613          | 97.4692  | -3.72                             | -3.97  |
| Jan-19 | 69.3716          | 97.6124  | -0.98                             | 0.15   |
| Feb-19 | 69.2247          | 97.6775  | -0.21                             | 0.07   |
| Mar-19 | 69.0298          | 98.0660  | -0.29                             | 1.01   |
| Apr-19 | 68.2846          | 98.3519  | -1.07                             | -0.12  |
| May-19 | 66.9004          | 96.9098  | -2.03                             | -1.57  |
| Jun-19 | 62.8885          | 96.9767  | -6.00                             | -0.21  |
| Jul-19 | 60.7401          | 89.7467  | -3.61                             | -8.76  |
| Aug-19 | 62.0595          | 92.0822  | 2.19                              | 2.27   |
| Sep-19 | 63.0797          | 94.3617  | 1.64                              | 1.81   |
| Oct-19 | 63.0324          | 94.8143  | -0.07                             | 0.48   |
| Nov-19 | 62.9052          | 93.7936  | -0.19                             | -1.03  |
| Dec-19 | 63.0078          | 93.7183  | 0.11                              | -0.08  |
| Jan-20 | 62.7676          | 96.4636  | -0.35                             | 0.76   |
| Feb-20 | 63.6871          | 97.2227  | 1.43                              | 0.79   |
| Mar-20 | 62.4799          | 97.1533  | -1.90                             | -0.07  |
| Apr-20 | 61.1568          | 94.4187  | -2.12                             | -2.81  |
| May-20 | 62.5240          | 97.1981  | 2.24                              | 2.98   |
| Jun-20 | 99.7676          | 93.0417  | -4.41                             | -4.28  |
| Jul-20 | 93.6417          | 93.3023  | -0.88                             | 0.07   |
| Aug-20 | R 97.5413        | 91.7088  | -1.88                             | -1.41  |
| Sep-20 | P 98.1729        | 94.1199  | 1.00                              | 2.54   |

Sources: IMF for exchange rate, Central Banks and Bureau of Statistics websites for CPI  
P= Provisional, R= Revised

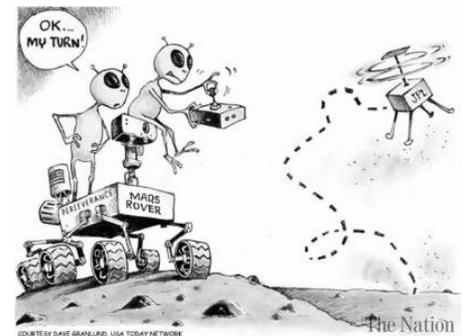
The Nation

M Ali Kemal

The exchange rate is the price of foreign exchange. It changes with a change in demand and supply of foreign exchange. The price decline is known as appreciation/revaluation of Pak Rupee while the price increase is known as depreciation/devaluation of Pak Rupee. Thus, the recent decline in the price of the exchange rate is an appreciation of Pak rupee.

Unexpectedly, Pakistani currency started appreciating from 26 August 2020 not just against the dollar but also against Euro and British Sterling from Rs168 per US Dollar to Rs157.86 per US Dollar. Today the price was around Rs159.45 per US Dollar.

(/E-Paper)



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### Past in Perspective

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### EDITORIALS

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#### December 05, 2020 Promising Partnership

(<https://nation.com.pk/05-Dec-2020/promising-partnership>).

During this period, the Dollar index has gone down by 0.7 per cent while rupee gained strength by 6.3 per cent against the dollar; 6.2 per cent against Sterling Pound and 7.9 per cent against Euro.

Pakistani rupee became the third best-performing currency in Asia after South Korean and Indonesian currency in recent times. The recent appreciation can be associated to the non-depletion of foreign exchange reserves due to an increase in remittances, deferment of loan repayment and relief aid. However, sustainability is a major question.

Court extends stay order in Sharifs' Jati Umra residence case  
(<https://nation.com.pk/29-Apr-2021/court-extends-stay-order-in-sharifs-jati-umra-residence-case>).

Alternatively, we witnessed a spike in the exchange rate due to pandemic panic in March 2020 when hot money flew out. If the spike is more than usual it is known as overshooting of the exchange rate. It is a very short term phenomenon which was instantly adjusted in a short time frame.

The spike in the exchange rate during March-April 2020 was close to 8 per cent when the exchange rate was depreciated from Rs154.23 per US Dollar on March 7, 2020, to Rs167.5 per US Dollar on April 6, 2020. The overshooting was readjusted during the next 30 days when it reached Rs158.8 on May 6, 2020, i.e., 5.5 per cent appreciation. Whereas it went up to Rs167.6 per US Dollar by June 30, 2020, floated around this par value by the end august and then started appreciating. It is now back to Rs159.45 per US Dollar. Was it overshooting and readjustment or Rs168 per US Dollar is the actual equilibrium exchange rate value and now it is overvalued.

Pakistan's currency was overvalued by as much as 20 per cent according to IMF in 2017. At that time the currency value was controlled at Rs105 per US Dollar. In Jun 2017, IMF calculated Real Effective Exchange Rate, available on the SBP website shows that exchange rate was 21.0086 per cent overvalued. The Real Effective Exchange Rate (REER) index is a nominal effective exchange rate index adjusted for relative movements in national price indicators of the home country and selected other countries (or currency unions). In November 2017 the currency was started depreciating against the dollar and reached Rs124 per US Dollar in July 2018, i.e., 15 per cent depreciation. The REER index also shows that from June 17 to June 18 there was 14.5 per cent real depreciation in the exchange rate.

India to use animal crematorium site as it struggles to cope with rise in COVID deaths  
(<https://nation.com.pk/29-Apr-2021/india-to-use-animal-crematorium-site-as-it-struggles-to-cope-with-rise-in-covid-deaths>).

Rupee depreciated further and reached Rs147 per US Dollar by May 2019, i.e., further 15.6 per cent depreciation, a total of 28.5 per cent depreciation since 2017. We can state unambiguously that overall depreciation by then has covered the overvalued part of the currency that was objected by the IMF two years ago because the inflation difference (with world inflation) during the two years was close to 6 per cent.

## LETTERS

December 05, 2020

### Democracy at home

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### Non-chemical solutions

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## E-PAPER - NAWAIWAQT



(<https://www.nawaiwaqt.com.pk/epaper>).

## POLL

Should the Council of Islamic Ideology publish guidelines for Friday sermons?

YES

In June 2019, the exchange rate depreciated by 9.9 per cent to Rs163 per US Dollar. Recalculation tells 35.6 per cent depreciation in the last two years. Since inflation difference during 2017-19 was 6 per cent, thus we can fairly say that the exchange rate was overvalued by 9.6 per cent. Similarly, REER index value in June 2019 shows 16.5 per cent real depreciation in exchange rate compared to June 2018 and the index value confirms undervaluation of the exchange rate by 9 per cent.

I call this depreciation in the exchange rate by 9.9 per cent in May-June 2019 as overshooting. The readjustment was done by 1.6 per cent in July 2019 and further 2.26 per cent in August 2020. By December 2019 the exchange rate was reached at Rs155 per US Dollar, i.e. readjustment by 5.2 per cent since June 2019. REER index value shows that after readjustment exchange rate was still undervalued by 4.28 per cent. Though, inflation rate during July-Dec 2019 was high; month-over-month accumulated 7 per cent and year on year 12.6 per cent in December 2019. Considering month over month accumulated inflation differential would eventually lead us to conclude contrary to what REER index shows. It was either close to 100 or little higher than 100, implies not undervalued.

[Electioneering for NA-249 by-elections ends 48 hours before polling \(https://nation.com.pk/29-Apr-2021/electioneering-for-na-249-by-elections-ends-48-hours-before-polling\)](https://nation.com.pk/29-Apr-2021/electioneering-for-na-249-by-elections-ends-48-hours-before-polling)

Panic attack in March 2020 led exchange rate overshoot by 6.7 per cent to Rs166 per US Dollar partly due to outflow of hot money, though readjusted in the next month by 3.42 per cent to Rs160.5 per US Dollar. However, due to loss in exports and COVID lockdown panic, it depreciated continuously and reached Rs167.2 per US Dollar by June 2020 and remained around this value by 4th week of August 2020.

During June 2019 to June, 2020 exchange rate was depreciated by 2.44. Whereas inflation difference stood at 8 per cent. Considering the 9.6 per cent overvalued exchange rate in June 2019, we can fairly say that it was still undervalued by 4 per cent in June 2020, though REER index shows 7 per cent overvalued exchange rate.

Since August 26, 2020 exchange rate has been continuously appreciating except for the last few days. Currently, it is at Rs159.45 per US Dollar i.e., 5.5 per cent appreciation.

Since June 2020 the appreciation was 5 per cent with 3.8 per cent month over month accumulated inflation while world inflation is less the 1-per cent. Putting aside the reasons for appreciation, appreciation plus inflation difference makes the currency overvalued in October 2020 by as much as 4 per cent, whereas, REER shows 6 per cent undervalued exchange rate. Consequently, I can conclude that the exchange rate overshoots and then readjusts.

[Shaukat Tarin to chair ECC meeting tomorrow \(https://nation.com.pk/29-Apr-2021/shaukat-tarin-to-chair-ecc-meeting-tomorrow\)](https://nation.com.pk/29-Apr-2021/shaukat-tarin-to-chair-ecc-meeting-tomorrow)

Since December 2018, according to the IMF/SBP REER index, Pakistani currency remained undervalued. Does a pertinent question arise that if the undervalued exchange rate is better for developing countries to boost exports then why it was not useful for our exports? The answer lies in the longer-term vision, structural changes

- NO
- DON'T KNOW

**VOTE**

and essential reforms which are necessary to increase exports. Following REER index if we accept that the exchange rate has remained undervalued since December 2018 but our calculation shows that after the recent appreciation it is again overvalued.

— The writer is a research economist at PIDE.

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| <p>April 13, 2021 (<a href="https://nation.com.pk/13-Apr-2021/a-promising-exchange">https://nation.com.pk/13-Apr-2021/a-promising-exchange</a>)</p> <p><b>A Promising Exchange</b><br/>           (https://nation.com.pk/13-Apr-2021/a-promising-exchange)</p> <p>10:05 PM   April 19, 2021<br/>           (https://nation.com.pk/19-Apr-2021/modernizing-dairy-sector-vital-for-more-jobs-foreign-exchange-president-alvi)</p> <p><b>Modernizing dairy sector vital for more jobs, foreign exchange: President Alvi</b><br/>           (https://nation.com.pk/19-Apr-2021/modernizing-dairy-sector-vital-for-more-jobs-foreign-exchange-president-alvi)</p> <p>2021/inflation-rate-increases-to-9.1pc-for-first-time-in-10-years<br/>           (https://nation.com.pk/20-Apr-2021/inflation-rate-increases-to-9.1pc-for-first-time-in-10-years)</p> <p><b>CM directs to ensure provision of 9.1pc fixed rate across</b><br/>           (https://nation.com.pk/20-Apr-2021/cm-directs-to-ensure-provision-of-9.1pc-fixed-rate-across)</p> | <p>1:27 PM   April 29, 2021<br/>           (https://nation.com.pk/29-Apr-2021/punjab-likely-to-impose-complete-lockdown-in-12-cities)</p> <p><b>Punjab likely to impose complete lockdown in some cities</b><br/>           (https://nation.com.pk/29-Apr-2021/punjab-likely-to-impose-complete-lockdown-in-12-cities)</p> <p>Pakistan reports record 201 deaths, 5,292 new coronavirus cases in 24 hours<br/>           (https://nation.com.pk/28-Apr-2021/pakistan-reports-record-201-deaths-5-292-new-coronavirus-cases-in-24-hours)</p> <p>Govt may impose lockdown in some districts<br/>           (https://nation.com.pk/27-Apr-2021/govt-may-impose-lockdown-in-some-districts)</p> <p>Police arrest PML-F's saved Latif<br/>           (https://nation.com.pk/27-Apr-2021/police-arrest-pml-fs-saved-latif)</p> |
| <p>ON THE NATION<br/>           2021/cm-</p> <p>1 comment<br/> <b>Court extends stay order in Sharifs' Jati ...</b></p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | <p>2021/police-violation</p> <p>1 comment<br/> <b>COAS, US' Defence Secretary</b></p> <p>1 comment<br/> <b>Ahsai says I large</b></p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |