Exchange Rate in Zambia

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Abstract

The paper analyses the main determinants of the real exchange rate in Zambia. It first gives a brief review of the Zambian economy and a review on real exchange rate studies. Then an illustrative model is presented. The study employs cointegration analysis in estimating the long-run determinants of the real exchange rates for imports and exports, and of the internal real exchange rate. The finding is that terms of trade, government consumption, and investment share all influence the real exchange rate for imports, while terms of trade, central bank reserves and trade taxes influence the real exchange rate for exports in the long-run. The internal real exchange rate is influenced by terms of trade, investment share, and the rate of growth of real GDP in the long-run. Error-correction models are then estimated. Besides the difference of the fundamentals mentioned above, aid and openness are found to impart short-run effects on the real exchange rate indices. The coefficients of adjustment are found to be-0.38,-0.79 and-0.80 respectively for the real exchange rates for imports and exports, and for the internal real exchange rate.