Assessing a Common Currency in Africa

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Introduction: An Overview of African Common Currencies

A common currency is a necessary condition for the realisation of the benefits of integration. The adoption of a single currency exposes domestic markets to foreign markets, thereby increasing competition between member countries and enhancing the competitiveness of national industries (Saka, Onafowokan and Adebayo, 2015). A common currency is the signification of an economic community and a united and developed people. The importance of African economies in global trade is not going to be judged by the power of each country's individual economy, for there is none, so far, or by the stability provided by the benevolent hegemony of a colonial master. Rather, the power of African economies lies in the actual share of the proposed currency in world official foreign reserves, its liquidity in international trade, and its role as a competitor against the exorbitant U.S. dollar.

Africa's experiments with common currencies are not a new phenomenon. The "Colonies

Françaises d'Afrique", or "French Colonies in Africa", better known as the CFA zone, have existed in West and Central Africa since 1945. Prior to that, the French West African Franc, as well as the British West African Pound, served as the region's official currencies. Similarly, the East African Shilling was the currency for colonial Kenya, Uganda and Tanganyika, and even before that the Indian Rupee served as the currency for the British East African states. In the 1960s, East Africa was close to developing a regional currency, but the project was destabilised by the rise of nationalistic projects like the one of General Idi Amin Dada. In the contemporary era, the region has been struggling to implement the "East African Shilling", which was last delayed in 2015 and is now expected to be released in 2021. In Southern Africa, the Southern African Customs Union (SACU), the oldest regional economic bloc in the world, pegs the currencies of Swaziland, Lesotho and Namibia to the South African rand. Besides the pegging and Common Monetary Area (CMA), the SACU has not sought to make progress towards a real common currency. West Africa, however, in the form of the Economic Community of West African States (ECOWAS) is leading in terms of common currency progress with its "ECO." Though first expected in 2003 and postponed a good number of times, the ECO is expected to be finally unveiled in 2020 (Mosegbon, 2018). In December 2019, the ECO made its strongest step with the CFA Franc (West) opting out of certain ties with France to align itself more with the ECO. Many critics, however, consider this transformation to be nothing more than a name change.

There have been varied results to the African common currencies projects. Their potential and steady progress have been hampered by a lack of political will and unfavourable economic indicators. For example, despite the CFA (Central and West) zone having existed for over 70 years, its states have remained some of the poorest in the world. Likewise, Swaziland and Lesotho have steadily featured on the list of the poorest states in the world, while Namibia is considered to be one of the most unequal states in the world with a 57.6 Gini Co-efficient in 2015, ranking it with the likes of Haiti and the Central African Republic. What is clear from both the CFA and SACU systems is that a higher power appears to be benefiting from the arrangements: France in the case of the CFA, and South Africa in the case of the SACU.

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Why are African common currency arrangements not developing their respective regions? What is happening at the regional level that is hampering real progress? Using the CFA and the SACU as case studies, the following section seeks to answer the above questions.

A Close Examination of the CFA and the SACU

There are both advantages and disadvantages to the CFA currency. The CFA franc is used in 14 African countries, with a combined population of about 150 million and $235 billion of gross domestic product. The main problem with the CFA is that it is seen as a symbol of neo-colonialism. Critics, such as those leading the anti-CFA movement, say that true economic development for the 14 states can only be achieved by getting rid of the currency (Konkobo, 2017). These critics argue that in exchange for the guarantees provided by the French treasury, African countries channel more money to France than they receive in aid. They also argue that they have no say in deciding key monetary policies agreed to by European countries, which are members of the Eurozone.

Luigi Di Maio, Italy's foreign affairs minister, backed up the anti-French view, noting that "France is one of those countries that by printing money for 14 African states prevents their economic development and contributes to the fact that refugees die in the sea or arrive on our coasts" (Signé, 2019). Chad's long-serving President Idriss Debby in 2015 stated that the CFA pulls down African economies and that the "time has come to cut the cordon that prevent Africa to develop". He called for a restructuring of the currency in order to "enable African countries which are still using it to develop". Debates over the persistence of the CFA franc zone also focus on African states' independence and sovereignty. Metaphorical armies of unemployed youth throughout sub-Saharan Africa—which may reach over 350 million over the next two decades—are often the loudest opponents of the CFA zone. Other pro-democracy movements, like *Y'en a Marre* in Senegal and *Le Balai Citoyen* in Burkina Faso, consider the dismantling of the CFA zone as essential to their campaigns to reform their countries' respective governments. Other protestors have included Kémi Séba, a Benin-born French activist who was charged with burning CFA notes in Senegal before being deported.

Landry Signé – author of *Innovating Development Strategies in Africa: The Role of International, Regional, and National Actors* – examines the political economy of the performance and economic development strategies of CFA franc zone states from 1960 to 2010 (2019). The empirical evidence he provides showcases the CFA as both an enabler and barrier to development. For example, he notes that Guinea stands as a prime example for CFA supporters. Guinea – which has its own currency – frequently experiences currency shortages, and has a Central Bank that does not have sufficient policies to ensure stability. In this case, the ever-present CFA offers a serious solution to this conundrum. A few hundred kilometres to the east, in Ivory Coast, President Alassane Ouattara has on numerous occasions contended that the CFA zone states are better off than the Anglophone states due to growth and low inflation, whereas the poor are disproportionately affected by unpredictable inflation in Anglophone countries. Outtara has stated that the CFA is solid, well-managed, and a stabiliser for African economies (Signé, 2019).

Signé's data shows that, in terms of trade, the CFA's fixed exchange rate to the Euro has led to a greater facilitation of trade, through the reduction of uncertainty and the stabilisation of domestic prices. The logic of fixed exchange rates can be traced back to the Bretton Woods period, when 63% of developing countries had their currency pegged to that of an industrial country. The potential problems with a fixed exchange rate are mostly offset in Central African Economic and Monetary Union (CAEMU) countries, due to these countries' high levels of excess liquidity from oil revenues. However, West African Economic and Monetary Union (WAEMU) countries have experienced declining liquidity since 2004, thus suffering from the volatility of a fixed rate amidst external shocks.

Signé is of the opinion that the monetary policies in the CFA have been effective in achieving real exchange rate depreciation, which resulted in a reduction in government expenditures. As a positive effect, the unlimited convertibility of the CFA franc to the Euro has generally reduced the risk of foreign investment in CFA countries. According to Coppola, the CFA is so closely related to the Eurozone that foreign exchange risk can be negligible on trade between CFA economies and the Eurozone (2019). Although the two versions of the CFA franc are not yet integrated, they are both worth exactly the same in Euro terms, and the hard peg to the Euro means that their external value is also identical, since their foreign exchange rates float up and down with the Euro. So for nearly all intents and purposes, the 14 countries in the CFA franc currency union use the same currency, and that currency can be regarded as a version of the Euro (Coppola, 2019). This has helped the CFA zone states to survive recent falls in the price of oil and commodities without currency collapse, inflation spikes and fiscal distress.

On the other side of the debate, and besides the already-mentioned political arguments against the CFA, the empirical evidence provided by Signé shows that the CFA Franc zone as a whole has had very limited success in intra-regional trade, especially in Central Africa. The CFA zone has also been highly dependent on producing and exporting a limited number of primary commodities, and it also has a narrow industrial base. These two factors mean that the zone faces high vulnerability to external shocks. Some critics argue that the strength of the Euro may have

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discouraged exports and encouraged imports, benefiting Eurozone economies – especially France – at the expense of CFA zone countries.

The December 2019 decision to rename the West African CFA franc as the ECO and thereby cut "some of the financial links with Paris" was welcomed by many Heads of State, but the reliance on France remains in the details. The new ECO will remain pegged to the Euro, but the states in the bloc will not have to keep 50% of their reserves in the French treasury, and there will no longer be a French representative on the currency unions board. To George Ott, the transformation from CFA to ECO was largely symbolic and cosmetic, as the maintenance of the Euro peg will continue to dictate the scope of regional monetary policy decisions (2020).

The CFA's transformation into the ECO is all but theoretical, given that the ECO must first circulate in the other non-CFA states to be considered a true ECO.

Three key challenges have prevented this from happening. Firstly, there is inconsistency in decision-making by the heads of governments of member states. Over the years, new governments, new policies, *coups d'état,* or simple invasions in the case of Ivory Coast in 2011, have delayed true ECO circulation. Secondly, non-CFA zone states (i.e. WAEMU members) have not satisfied the convergence criteria for the adoption of the new currency. Key criteria such as maintaining a budget deficit of less than 3% of GDP; a public debt ratio of less than 70% of GDP; an annual inflation rate of less than 10%; and a minimum of three months of import cover mean that it appears unlikely that the majority of the WAEMU countries will meet all these criteria by the very ambitious inception date of July 2020 (Ott, 2020). Thirdly (and quite surprisingly in the context of anti-colonial sentiments), it appears that in the face of the demise of the CFA franc, its benefits become more clear. The CFA is tied to fixed rates, which works well with the undiversified cash crop economies of the CFA. Booms and busts and other fluctuations in the market mean that the exchange rate of the CFA is relatively unaffected. Even in the face of political and election instabilities, the CFA remains unaffected. So, while often labelled as a neo-colonial system, the economic rationality of the CFA franc cannot be ignored.

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Regarding the SACU, the penultimate question to ask is whether SACU members really aspire to the next level of economic integration. Overall, the SACU is about protecting South African interests, which dominate the region. Intra-SACU exports in 2017, which accounted for $14 billion, were dominated by South Africa, which accounted for 71% of total exports. South Africa also accounts for 87% of SACU's exports to the world (Chidede, 2018).

Except for Botswana with its stronger pula, all SACU members are part of a Common Monetary Agreement (CMA). In a CMA, there exists an anchor currency that is accepted as a medium of exchange within the monetary area. This anchor currency is accompanied by rules that govern a CMA's operations, such as limiting the mandate of local central banks within a CMA (notably the financing of fiscal deficits through monetary expansion, so-called quantitative easing); maintaining sound macroeconomic performance; and uniform guidelines for prospective and existing members. Other rules relate to the governance of inflation rates – both current and expected – and keeping a CMA's internal exchange rates within the margins of the de facto currency. In the case of the SACU CMA, the South African rand acts as the anchor currency, and the policies of the South African Reserve Bank (SARB) are widely influential among the CMA states of Namibia, Lesotho and Swaziland. Botswana is the only member of the SACU to stand outside of the CMA, instead managing its currency based on a basket of currencies, of which the South African rand holds an approximate 60% weighting (Nene and Patroba, 2013).

This "unfair weighting" is natural given that Lesotho, Swaziland and Namibia combined

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provide less than 4% of the total GDP of the CMA region. At the same time, their financial systems lack the high level of sophistication of the South African financial system (Van Zyl, 2003). This means that South Africa's monetary and exchange policy is transmitted across the SACU (Chidede, 2018). Despite the fact that the CMA is not a full monetary union because members do not have a single currency and single central bank, monetary integration in this CMA is considered high, with CMA members generally able to withstand shocks. While stronger monetary cooperation within the Southern African Development Community (SADC) will be a slow process, this integration initiative will eventually create a major challenge for the CMA. It remains to be seen whether the CMA has a pivotal role to play in the larger SADC initiative. Monetary cooperation in the SADC could eventually entail an entirely different framework, or it could come about by extension of the CMA arrangements to include more SADC countries, as and when they are willing and able to join. Expanding the membership of the CMA would be more complicated than in the past, because new members would not share the history of the South African currency being legal tender. The CMA arrangements have, however, in the past proved to be very flexible and this could be a big advantage (Van Zyl, 2003).

SACU summarises Africa's ventures in common currencies. It highlights the uncertainties of whether the benefits of deeper monetary integration outweigh the cost and the precaution of hegemonic dynamics which are common in Africa's regions. Linking a local currency to an anchor currency can improve macroeconomic stability, as opposed to operating under a flexible exchange rate. Under a flexible exchange rate regime, commodity prices often become unstable, and can in turn create disturbances in smaller economies, particularly if their currencies are depreciating, thereby resulting in general price-level volatility. However, although a CMA would have a better capacity to cope with these disturbances, it would have less capacity to deal with the idiosyncratic shocks and development challenges that might only occur in certain member states, which would have lost their capacity to tailor monetary policy to their needs through the centralisation of monetary control. Individual countries could face the effects of differentiated external shocks due to differences in their production, consumption and expenditure patterns; market characteristics (monopolistic/competitive); and level of openness, among others. Asymmetric shocks could cause havoc to individual economies under independent currencies (Nene and Patroba, 2013).

The institutionalised framework of trade, financial and other non-economic links, such as infrastructure, binds SACU states ever closer to South Africa and, in doing so, limits their scope for independent action (Mingst, 2008). The progress in SACU is slow due to a lack of authority within these forums, overlapping membership, and political turmoil in some countries (Cox, 1996). This creates an ideal platform for South Africa to push its agenda. It is of paramount importance that the Botswana, Namibia, Lesotho and Swaziland (BNLS) states be stable in all facets (socially, politically and economically), so as not to impede on the South African economy. While this dependency can, to an extent, be taxing on South Africa, it also works to its benefit because it provides viable opportunities for investment, trade and migrant labour in and from those states.

According to Van Zyl, in view of the progress already realised by the CMA under SACU, it could be worthwhile for countries to move towards a full monetary union by using a single currency. South Africa, particularly the SARB, could then continue to play the leading role in this process, capitalising on the experience of the CMA (Van Zyl, 2003). Nene and Patroba also back up this view, noting that it would be beneficial for SACU to establish a monetary union. In such a case, the SARB could continue formulating a monetary policy for a possible SACU monetary union. A key challenge in obtaining this goal is the disparity across SACU member states and their poor macroeconomic performance over the years (Nene and Patroba, 2013).

Conclusion

In sum, there is potential for African common currencies. According to Oladele, a common currency can be created with a lot less difficulty than our African leaders have so far led us to believe (Mosegbon, 2018). In an empirical study by Karras, it was concluded that African states like Uganda, Ghana and Guinea have a lot to gain from a monetary union, but also a lot to lose from it. Economies like Morocco, Ivory Coast and Gabon have little to lose by adopting a common currency, but also have little to gain from it. Nigeria is a more promising candidate for membership in an African monetary union than Kenya, and Zambia is an unambiguously better candidate than either Benin or Mauritius (Karras, 2006). The mix of benefits and constraints is visible in both the CFA and SACU. Overall, both these unions have shown incredible durability in highly unstable or unequal regions. This seems to validate many of the benefits of such unions, with the regions showing consistently low and stable inflation rates.

In surveying the literature around African common currencies and their dynamics, the most important details to success are well-coordinated monetary and fiscal policies. The coordination of such policies is a necessary foundation. A strong emphasis needs to be put on reducing the fiscal deficit of states seeking to join a monetary union. Reducing inflation and debt levels and increasing reserve holdings will also ensure that the benefits of monetary integration outweigh the costs. Okafor suggests that to benefit from economic and monetary integration, regions need to deal with the sources of fiscal policy distortion through better management of their economies (2013).

Using the CFA and SACU as yardsticks, an African Monetary Union would be most challenging to implement and would require countries to adhere to strict fiscal rules, similar to those in the CFA zone, until stability was achieved. This strategy requires significant investment and capital mobility to ensure a strong exchange rate union and currency convertibility. Movement of labour and capital are necessary to spur economic growth and stabilise relatively different economies. The appeal of an integrated African Monetary Union is the tremendous potential to increase intra-regional trade and encourage domestic production capabilities. However, another monetary union may lead to problems of dependence, such as those experienced by countries in the CFA franc zone. ■

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