Chapter 1

Introduction

Regional integration arrangements are far more than economic ideals. Politics has been a major force behind major integration schemes. The decision to proceed with economic or monetary integration or to oppose it rests on the part of existing political actors. The development and orientation of regional trade, the coordination of regional economic plans, or the formation of regional monetary unions require legal provisions, executive decisions and administrative harmony which fall within the responsibility of the highest spheres of government. Not only do political objectives motivate the establishment of regional integration schemes, political action also bring them into being and it is politics that characterizes their functioning too. As ongoing entities, these schemes are marked by conflict among participating actors over goals and over the distribution of costs and benefits just as is politics at the national level. The involvement of politics in integration schemes is more pervasive and more divisive in the case of Africa.[1] In this respect, it is instructive to note at the outset that this is a study of the politics of international cooperation with respect to monetary integration in West Africa.

The quest for monetary integration is not a new phenomenon in Africa. The decade of the 1990s saw an intensification of the monetary debate about the nature of appropriate monetary regimes not only for individual countries in Africa, but also for the entire world. Some monetary economists predict that in the near future there will only be a single or at most three common currencies worldwide, the Dollar, the Euro and possibly the Yen. Recently, Robert Mundell even speculated about a world currency created by a monetary union of the US, the European Union (EU) and

[1] S.K.B Asante, *Regionalism and Africa's Development: Expectations Realities and Challenges* (London: Macmillan, 1997), 25.

Japan.[2] In the years following the emergence of the Euro as a single currency in the EU, there has been renewed and growing interest in Africa, in fostering economic and monetary integration as a means of facilitating economic growth and development of the integration entity.

At the level of regional economic communities (RECs) in Africa, monetary cooperation is programmed to lead to single monetary zones. At the continental level, Article 44, Chapter 8 of the Treaty establishing the African Economic Community (AEC) and Article 19 of the constitutive Act of the African Union have respectively called for the establishment of an African monetary union, through the harmonization of regional monetary zones and the establishment of an African Central Bank.[3]

Background

Several attempts have been made in Africa aimed at forming monetary unions by the different regional economic groupings in the continent. In the Economic Community of Central African States (ECCAS) for example, there exists the *Communaute Economique et Monetaire de l'Afrique Centrale*, CEMAC, (the Central African Economic and Monetary Community) which shares a common currency, the CFA franc, and it is parallel to the CFA zone in West Africa. The CFA zone, created in 1945, originates from the consolidation of the French colonial economies in the 1940s and 1950s.[4] The parity was fixed at 0.5CFAF to 1 French Franc in 1948 and its

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[2] Robert A Mundell, "International Monetary Reform" *http://www.robertmundel.net/menu/main.asptype=5caT=03&themename=international520monetary20reform.*

[3] Article 44, Chapter 8 of the Treaty establishing the African Economic Community calls on member states to establish an African Monetary Union through the harmonisation of Regional Monetary zones.

[4] "History of the CFA Franc Zone," *Http://www.bceao.int/internet/bcweb.nsf/pages/umuse1.*

nominal parity was changed during the French currency reform of 1968 to 50CFAF to 1FF, its parity to the French franc remained unchanged until its devaluation in 1994.[5] The currency was initially issued by the Banque de France (French Central Bank) but this responsibility was later transferred to two regional banks created in 1955 and consolidated after independence in 1962.

Both banks were initially based in Paris but were later given greater autonomy and moved to Africa in reforms enacted between 1972 and 1974. These regional issuing banks BCEAO, *Banque Centrale des Etats d'Afrique de L'Ouest* (Central Bank of West African States) is headquartered in Dakar, Senegal and the BEAC, *Banque des Etats de L'Afrique Centrale* (Bank of Central African States) has its headquarters in Yaounde, Cameroon[6]. The official mechanism of the zone dates back to treaties signed between 1972 and 1974. It is a unique postcolonial relationship; the parity of the CFA to the French Franc (now the Euro) is fixed subject to changes agreed unanimously by members of either zone in consultation with France. The convertibility of the CFA to the FF was guaranteed by the French Government and until 1993, there was free mobility of capital transfers between France and the zone although administrative procedures hindered this in practice.[7]

The efforts at monetary integration in the Economic Community of West African States (ECOWAS), which is the main focus of this work, has several commonalities with the initiative mentioned above. The idea of a monetary union was conceived in ECOWAS when the organization was formed in 1975.[8] The organization therefore

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[5] "Growing Up With the Umbilical Cord Attached: Developments In the African Franc Zone 1994-2001," Africa Research Group, London: Foreign and Common Wealth Office, 2001,3.
[6] The BCEAO issues the *Franc de la Communaute Financiere Africaine*, while BEAC issues *Franc* de *la Cooperation financiere en Afrique Centrale.* Both are commonly referred to as the CFA. Also see Paul Collier, "Africa's External Economic Relations" *African Affairs* (1991): 90, 3348.
[7] "Regional Integrationand Food Security in Developing Countries," *http://www.fao.org/documents/ show-cdr.asp?urfile=1docrep/004/y4793e1y479304.html.*
[8] Richard Mshomba, *Africa in the Global Economy* (Boulder: Lynee Reinner, 2000), 189.

regards a monetary union as a means to counteract perceived economic and political weaknesses by putting in place regional institutions through which such a union if formed would be seen as a potent symbol. It would also lead to greater economic and political integration in the region which was the major reason why the organization was formed. The challenge therefore will be to bring together the different currencies in the region into a unique currency.

The presence of several different currencies in the West African region can be traced to the colonial monetary policies introduced by the two major colonial powers Britain and France. Any consideration of the colonial monetary policies shows that the two powers initiated and maintained unique currency systems in their respective spheres of influence. The British colonies had a currency board arrangement with the colonial currency pegged to and more or less fully backed by the Pound Sterling.[9] At independence, former British colonies distanced themselves from the Sterling and introduced unique currencies, some of which include the Naira, Cedi, dollar and the Leone. As a general rule, former British colonies moved from their currency boards to flexible exchange rates after independence.

The French for their part established a close association between currencies in the colonial territories and the French Franc. At independence, the CFA Franc was maintained by all former French colonies, including Equatorial Guinea a former Spanish colony which joined the CFA zone in 1984 and has since enjoyed unlimited French guarantee. The speedy collapse of the postcolonial currency board in former British colonies suggests that the survival of the Franc zone may ultimately have been based on the continuing flow of financial assistance to members from France that were perceived to be linked with the currency union.

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[9] John Renninger, *Multilateral Cooperation For Development in West Africa* (New York: Pergamon Press, 1979), 65.

In the early 1990s, the status of the CFA Franc in the process of European monetary integration was the subject of debate between France and her European partners, particularly Germany and the emergent European financial institutions. The French argument was that the CFA franc zone is a budgetary arrangement, because responsibility for covering deficits in the current account falls on the French Treasury not the Banque de France. The French pointed out that it has no inflationary potential aside from minor implications on the French budget.[10] They advanced further that under Section 109.5 of the Treaty of Maastricht, France was free to negotiate agreements with the CFA Franc zone countries.[11]

The link of the CFA franc to the Euro thus confirmed, France retains the role of overseeing the function of the agreements, leaving the working of the *compte d'operations,* or operations account in the hands of the French Treasury. However the financial institutions of the European Monetary Union are to have a say in any important changes to be made in this arrangement. The link with the Euro has specific consequences for the countries of the Franc Zone. The area of trade marched by the currency link is expanded as the Euro zone accounts for 50 per cent of the Franc zone's exports and 53 per cent of the zone's imports.[12] The pool of investment capital, which has moved to the Franc zone because of the monetary link, has expanded considerably. Otherwise the advantages and disadvantages of the link to the Euro remain valid. A major risk remains the asymmetry between a strong Euro and the declining prices for African exports.[13]

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[10] "Growing up with the Umbilical Cord Attached, Developments in the West African Franc Zone: 1994-2001," Africa Research Group, (London: Foreign and Common Wealth Office, 2001), 8.
[11] See Section 109.5 of the Maastricht Treaty which was signed and ratified by member countries of the EEC in 1993, and committed the participating countries to a single European currency.
[12] H. Michael and Gary Michel, "The CFA Zone and the European Monetary Union," *IMF Working Papers. Http://www.eldis.org/static/doc4717.htm.*
[13] "Growing Up with the Umbilical Cord Attached, Developments in the West African Zone: 1994-2001," African Research Group (London: Foreign and Commonwealth Office, 2001), 8-9.

The French Treasury has therefore retained sole responsibility for guaranteeing convertibility of CFA Francs into the Euro, without any monetary policy implications for the European Central Bank, which now plays the role of the Banque de France. While the two CFA Central Banks maintain an overdraft facility with the French Treasury, the amount that can be withdrawn by either bank is limited by operating rules which have been applied since 1973.[14] The BEAC and BCEAO must each keep at least 65 per cent of its foreign assets in its operation account, *compte d'operation,* with the French Treasury and provide for foreign exchange over at least 20 per cent for flight liabilities. The fixed parity between the Euro and the CFA Franc is based on the official fixed conversion rate for the French Franc and the Euro, set on January 1, 1999, at FF6.55957=Euro1.[15] In effect, the value of the CFA Franc is now fixed against the Euro. Since CFAF100=1FF, the rate has remained unchanged, the CFA Franc to Euro exchange rate is CFAF 665.957=Euro1.

It is against this background that the Non-CFA members in the West African region have agreed to bring together their different currencies into a single currency, which would eventually merge with the CFA and a new currency the "Eco," will be launched. In order to hasten the realization of this initiative, the authority of heads of state and government of the community adopted the ECOWAS Monetary Cooperation Programme (EMCP) in 1987, with the specific objective of strengthening sub regional payment systems under the West African Clearing House, (WACH) which has been replaced by the West African Monetary Agency (WAMA).

By 1999, it was however observed that the pace of implementation of the West African monetary cooperation programme was slow. Some perceived obstacles to the

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[14] "Banque de Etats De L'Afrique Centrale, Les Fisches d'identite," *http://www.izf.net/fishesindentite/beac.htm.*

[15] Jacqueline Irving, "Varied Impact on Africa Expected from New European Currency: For Better or Worse, the Euro and the CFA Franc," *Africa recovery,* Online United Nations Publication.

successful implementation of the programme included lack of political will and commitment on the part of member states, non uniformity in the adoption of the required macro economic framework and the lack of policy coordination and harmonization between the Francophone West African countries, with the exception of Guinea and their Anglophone counterparts.[16] The recognition of this problem prompted the authorities of ECOWAS at its 22nd summit in Lome (Togo) in December 1999 to adopt new approaches, which would eventually lead to the successful implementation of the ECOWAS monetary cooperation programme.

Following the initiative of Ghana and Nigeria, consultations were held between the governments of Gambia, Guinea, Liberia and Sierra Leone. This resulted in the signing of the Accra Declaration, which stipulated the formation of a second monetary zone. The authorities of these countries committed themselves to the introduction of a single currency and the establishment of a central bank for eventual merger with the CFA zone in 2004.[17] This deadline was conspicuously shifted to 2005 and 2006.

In spite of the many obstacles and lack of progress, the desire of moving the regional body forward has been evident from the commitments portrayed by Ghana and Nigeria in recent years. At another summit in Bamako Mali, the authorities of ECOWAS formally launched and established the second monetary zone in the region, known as the West African Monetary Zone (WAMZ) and approved a set of convergence criteria to be attained by member states before the formalization of the West African monetary union.[18] This was followed by the establishment of the West African Monetary Institute in Ghana in 2001 to undertake the preparatory work

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[16] Abudu M, "Challenges to the Introduction of the Eco in the West African Monetary Zone: A Prognosis" *West African Journal of Economic and Monetary Integration.* Accra, Vol 3,no 2.2003.
[17] "The West African Monetary Zone," *http://www.alliancesforafrica.org20%for%advancingdoc.*
[18]"The West African Monetary Zone," *http://www.alliancesforafrica.org20%for%adavcingdoc.*

necessary for the creation of the West African central bank and the introduction of a single currency in the West African Monetary Zone. The institute equally has the responsibility of studying and making proposals on how to address issues of monetary policies and financial sector surveillance.[19]

The agreement establishing the West African Monetary Institute under the West African Monetary Zone stipulated that the convergence criterion adopted by member states, which included the reduction of inflation rates to at least 5 per cent and limiting deficit financing by central banks to about 10 per cent, be achieved within a stipulated time frame.[20] However there have been slippages and inconsistencies in the performances of member states in attaining the stipulated targets. While some member states were negatively affected by conflicts (Liberia, Sierra Leone and Ivory Coast) and other forms of domestic political instability (Nigeria), others experienced severe trade terms in the last few years.[21]

Overall, the will of forming a monetary union in West Africa is evident, from commitments espoused by Ghana and Nigeria among other Anglophone states. The introduction of the Euro in the European Union gave West African states renewed hope and impetus. Aside from the fact that the Euro posses as a model for imitation, the European Monetary Union (EMU) provides a demonstration effect suggesting to African countries that regional monetary integration need not have post-colonial connotations. But its use as an external agency of restraint remains a strong attraction of multi-country currency arrangements.

The adoption of the Euro in the EU affected the symbolic link of the CFA system to France, weakening the stigma that had always discouraged Anglophone countries

[19] *West African Monetary Institute,* "Macro Economic Development and Convergence Report", 2002.
[20] *West African Monetary Institute* "The Annex to Assessment of the Implementation of the West African Monetary Programme" *Country Reports*, Accra December 2003.
[21] *West African Monetary Institute* "Assessment of preparedness of the West African Monetary Zone for a Monetary Union" Accra, September, 2002.

from participating in an expanded monetary zone with their Francophone sister states. Further more, the Euro is a more attractive external anchor than any single European currency and will become much more so if and when it subsumes the Sterling. Were the U.K to join the EMU, thereby increasing the attraction of an Euro peg for Non-Franc zone countries, it is hard to avoid contemplating the prospect of greater monetary considerations promoting at last a deeper degree of cooperation across the old colonial boundaries as represented by the Anglophone/Francophone divide especially in West Africa.[22]

The transformation from the Organization of African Unity (OAU) to the African Union (AU) and its strategy of creating a common African currency as well as the emergence of the New Partnership for Africa's Development (NEPAD) provided extra motivations for African States to show more commitment towards integration. This stems from the fact that the idea of a monetary union is not new in the continent. Prior to the establishment of the African Union, in the days of the OAU, this goal was articulated by the Abuja Treaty. The 1991 Abuja Treaty outlined six stages for achieving a single monetary Zone in Africa.[23]

Up until this period, overall progress was dismally slow and there were incidences of retrogressive development, the most prominent was the collapse of the East African community. Judged by the low level of policy harmonization and cooperation, regional integration in Africa could hardly be labeled as a success story. However, in addition to establishing the AU, the Sirte Declaration calls for shortening

[22] Karis Muller, "European Monetary Union in Africa," National Europe Centre Paper No 29, Paper Presented to Conference on The European Union in International Affairs, *National Europe Centre, Australian National University,* July 2003.
[23] "Regional Cooperation in the Economic, Social and Related Fields," *United Nations Economic and Social Council, Substantive Session of 1995. Geneva, 1995.*

implementation periods in order to speed up the process for creating institutions such as the African Central Bank.[24]

The NEPAD for its part sets out a vision for the development of the continent based on the promotion of peace and security, economic growth and raising prosperity. In essence, the NEPAD is a framework for collaboration and coordination within the AU, representing therefore both a starting point for cooperation and a signpost for future regional cooperation. The monetary integration initiative has also been bolstered by the election of a democratic government and a leader who is committed to regional integration in Nigeria, the largest economy in the region. Significant steps towards commitment to integration have thus been evident from Nigeria and Ghana.

However the nature of political instability in the region creates unhealthy conditions for effective monetary integration. Recent instability in Cote d'ivoire has led the country into a technical recession, with recent growth rates of around –3%. Investors have been reluctant to invest and have in some cases withdrawn capital from the country. As Cote d' Ivoire accounted for about 40 per cent of the GDP of UEMOA, this has potentially serious consequences for the zone.[25] Europe has invested financial and political capital in the UEMOA and the expulsion of European nationals from Cote d' Ivoire in November 2004 in the wake of tensions between France and her former West African colony is particularly problematic for the country and the region at large. More over, the prevalence of domestic political instability in Nigeria in recent years has made her an erratic "hegemon" in the region and this has had negative spill over effects particularly on the smaller countries. These problems

[24] "Rising From the Ashes: Social Healing and National Reconstruction in Africa's Post Conflict States," *http://www.worldmin.org/2005/committees /committee.phpc=5.*

[25] "Growing Up With The Umbilical Cord Attached, Developments in The African Franc Zone: 1994-2001," *African Research Group* (London: Common Wealth Office, 2001), 9.

are compounded by the divisions between Anglophone and Francophone states which is further complicated by the CFA Franc system.

Equally important is the role and independence of Central Banks in the respective countries concerned. This is because central banks can accelerate economic growth, affect income distribution, influence a country's foreign relations and determine the extent of its democracy.[26] In this light, Sylvia Maxfield asserts that these institutions not only control monetary policy, but also maintain a country's financial stability and international domestic balance of payments.[27] Thus if and when a monetary union is eventually formed, the central banks of the respective countries would lose the limited authority they posses to the proposed West African Central Bank.

Going beyond central banks, monetary integration in West Africa a monetary union involving the various states in the community would have varying degrees of repercussions on domestic financial institutions in the respective countries. Some of such institutions include Micro finance institutions, (MFIs) such as savings and credit cooperatives, financial NGOs and development projects with credit components.

In each UEMOA country for example, there is considerable concentration in savings mobilization, the most important MFI holding between 51 and 90 percent of private deposits outside of the banking sector. MFIs equally hold 40 and 83 per cent of the market share of all non-bank loans.[28] They equally reach about 7 per cent households which seems little but is grater than the penetration rate of the formal; banking sector. Added to this is the fact that 50 per cent of MFIs were found in rural and remote areas. Because of the power they wield as interests groups in most

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[26] "World Bank Supports Regional Integration in West Africa," *The World Bank Group. Safricaext/senegalxtn/ocontentmdk:20012970~thestiepk296322pagepk:1411372~thestiepk3963400.htm*

[27] Sylvia Maxfield, "Gatekeepers of Growth: The International Political Economy of Central Banking in Developing Countries," *http://www.pupress.princeton.edu/titles/6069.html.*

[28] "Micro Finance Institutions in West Africa: An Overview," *Special Finance Programme in Support of Cooperative and Mutual Financial Systems (PA-SMEC) International Labour Organization. Http://www.ilo.org/public/english/employment/ent/papers/umoa.htm.*

countries in the region, the formation of a monetary union would have several consequences on these institutions.[29] It is against this background that the next section would look at the problems to be investigated.

Statement of the problem

The creation of a monetary union was high on the agenda of ECOWAS when it was formed in 1975. The advent of the European Monetary Union in 1999 sparked a new wave in cooperative monetary arrangements in West Africa. The CFA zone, widely believed to be on its last legs in 1992-1993 displayed renewed interest for wider membership as Guinea Bissau a former Portuguese colony became a member in 1997. Even though a monetary union had been envisaged in 1975 when the organization came into existence, by 1992, limited progress had been made in this regard. This was one of the reasons why the ECOWAS Treaty was reviewed and revised in 1993.[30]

Renewed interest displayed by the organization for monetary integration was drawn from the successful introduction of the Euro in the European Union. Second and most important is the recent political development in the sub region especially in Nigeria, that is, the transition from brutal military rule to one of democracy and the accession to power of a new leader who has shown commitment to regional integration.

The transformation from the Organization of African Unity (OAU) to the African Union (AU) and the formalization of the New Partnership for Africa's Development (NEPAD), which encourages deep integration among states, provided extra motivations for greater monetary integration among ECOWAS members. This is

[29] "Social Finance Unit, Programme in Support of Cooperative and Mutual Financial Systems," Micro Finance Institutions in West Africa: An Overview. *International Labour Organisation.*
[30] In July 1993, the ECOWAS Treaty was revised in a bid to accelerate economic integration and increase political cooperation.

particularly the case, since the AU treaty and that of the African Economic Community spell out the need for regions to further consolidate monetary links, as this would pave the way for an eventual African Monetary Union, supposedly with a single African currency.

Notwithstanding the observed renewed vigour, regional monetary union provisions like most of the provisions in the community remain largely unimplemented. Targets are difficult to meet and timetables are perpetually shifted. The annual summit of heads of state and governments according to some analysts remain "political jamborees and avenues for inspiring speech making, with unparallel and insignificant actions."[31] Furthermore, a major challenge the Community faces is related to the susceptibility of the economies to different shocks. The larger and more asymmetric the shocks, the greater the costs of fixed exchange rates.[32]

A major source of shocks in the region, especially for countries that export primary commodities, is in terms of trade. Large, asymmetric terms of trade shocks are less likely among monetary union members that have diversified economies with similar structures. Unfortunately the members of the community fall short on both criteria. For example Nigeria is different from its neighbours, all net oil importers in being a large oil producer, hence changes in net oil prices would affect their economies differently.

This research therefore seeks to find out whether the political cooperation can be harnessed in the region leading to a monetary union within the time frame set by the organization, given the new trends that are taking place in the continent and in the world. Attempts will also be made to investigate if the political will manifested by

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[31] Ibid.

[32] "The Pros and Cons of Expanded Monetary Union in West Africa," R. D. Asante and Robert Masson's interview with Jacqueline Irving of the IMF's External Relations Department in *Finance and Development,* March 2001 Vol 38, No 1.

member states can create alternative conditions in overcoming the asymmetric nature of shocks the economies in the region face and create a viable monetary union.

Research Questions

Within the context of this research, two central questions will be addressed:

- What are some of the political and economic obstacles that impede the realization of monetary integration in West Africa?
- Can the Community overcome the political and economic challenges and form a monetary union within the stipulated time frame, by harnessing political cooperation?

Limitation and Scope of Study

This study is centered on the politics of international cooperation and seeks to highlight the dynamics that are necessary for the creation of a monetary union in the West African region. The ECOWAS Treaty, which was signed in 1975, was revised in 1991 and several amendments were made, with Article 55 highlighting the need for the creation of an economic and monetary union in the community. This paper uses the period when the revised Treaty went in to force as its point of departure. However for a better understanding of the different currency systems in the region, time and space would be devoted to an historical overview of monetary cooperation in the region with particular focus of the CFA zone and the colonial Currency Board, which provided a link between Britain, and her former colonies.

Aim and Rationale

The aim of this research is to demonstrate how and why domestic political issues affect and are affected by interactions between states. The politics of international cooperation that will be the central theme in this study is the dependent variable, while economic issues form components of the independent variable. Emphasis is however laid on the political aspects of integration because even though economic factors help shape the political incentives of ECOWAS member states, and economists and central bank governors are consulted on issues of monetary integration, the ultimate decision to join or be part of an existing monetary union is made by politicians.

This research seeks to examine the politics of international cooperation in West Africa and show how this can lead to monetary integration in the community. A monetary union is of paramount importance to the Non-CFA members of ECOWAS given that their Francophone counterparts who form part of the CFA zone have relatively stable economies (with the exception of Cote D'Ivoire) and intra regional trade in the zone is higher than intra ECOWAS trade. Using the Optimum Currency Areas Theory, this research would address the prospects of forming a viable monetary union in the region based on the current state of affairs.

Another concern of this work would be to look at how the long-standing divisions between Anglophone and Francophone states in the region affect cooperation between the respective states. Focus will be on the political transition of Nigeria in 1999 and the effects this has on overall cooperation in the region. The presence of Nigeria in the ECOWAS initiative has several implications for cooperation in the region. After the introduction of democracy in that country in 1999, her foreign policy has depended on an astute "economic diplomacy" that tackles effectively issues like debt relief, foreign investment and the promotion of the objectives of continental initiatives like NEPAD.

Furthermore, a civilian regime unlike the military governments in the past faces pressure from parliament and the press and her foreign policy appears to be committed to demands, pressures and influences from the external environment to contribute to regional peace keeping. The role of Nigeria has been termed "Pax Nigeriana" which is evident through the country's efforts to achieve hegemonic leadership in Africa and has been boosted by the fact that the country accounts for over half of West Africa's population and has a 94.000 strong army that dwarfs the combined strength of those of its fourteen ECOWAS neighbours. On one side of the coin her position in West Africa could therefore mirror that of South Africa in the SADC region after 1994.

On the other side, in spite of her immense potential based on her demographic size, multiethnic population and vast oil reserves, a majority of the population remains poor. Like wise, while she has played a vital role in international peacekeeping, both under the auspices of the United Nations and through the ECOWAS Cease fire and Monitoring Group ECOMOG, the country itself has not been spared from ethnic and religious conflicts as well as other forms of political violence. The towering image of Nigeria adds another dimension to the security dilemma in the sub-region. Independent West African states are not prepared to replace the colonial yoke with the Nigerian "burden."

The Francophone states in particular have always viewed Nigeria with skepticism and suspicion. Even when they appreciate some of Nigeria's good gestures, there is always the fear of a perceived "hegemon" lurking around the corner. While Nigeria's political transition has helped in furthering integration in the community, domestic political and economic setbacks in recent years may very well play against her position as a regional leader.

Hypotheses

This research focuses on three hypothesized independent variables, whose values have been altered during the last decade and have affected in one way or the other, the prospects of an ECOWAS monetary union. Up until the 1990s, all three of the independent variables directly worked against the proposed ECOWAS monetary union. Changes that have occurred in each of the three variables over the last decade have to an extent, improved the prospects of monetary integration in the community. By testing each of the variables using available evidence we intend to highlight how each of the variables hindered cooperation before, and see how the change improved the level of cooperation particularly after 1995.

Prior to 1999, the CFA zone was linked to the French Franc and relations between France and the zone was stronger than relations with other West African states. However, the adoption of the Euro has weakened the symbolic link of the Franc zone to France and has therefore reduced the French stigma, which had hitherto discouraged Anglophone countries from participating in an expanded monetary zone with their Francophone counterparts. The shift to the Euro has improved cooperation among ECOWAS states in working towards implementing a monetary union in that they may have the option of choosing a floating currency. The Anglophone states may decide to continue the peg with the Euro as is the case with the CFA, and they would be dealing with a region in Europe and not specifically with France which has a tradition of favouring her former colonies. Prospects of deeper monetary considerations and cooperation will be improved where the U.K to join the European

Monetary Union, as this would give an added incentive to former British colonies in the region.

Secondly the democratization of Nigeria has improved cooperation among ECOWAS member states in working towards implementing a monetary union. Six years after independence, two successive coups by different groups of army officers brought the country under military rule. The Igbos, the dominant ethnic group in the Eastern region of the country declared independence as the Republic of Biafra in 1967 leading to a bloody civil war, which ended with their defeat in 1970. In 1975 a bloodless coup brought Murtala Mohammed to power but after his assassination he was replaced by his army Chief of Staff, Olusegun Obasanjo. A new constitution was drafted and elections were held in 1979, which brought in a civilian president. Nigeria returned to military rule in 1983 by a coup which established the supreme military council as the country's new ruling body.[33]

As a result of decades of political instability and uncertainty orchestrated by succeeding military regimes, the country, in spite of its size could not effectively command authority over its neighbours in moving towards integration. This situation was compounded by the expulsion of that country from the Commonwealth for human rights abuses in 1993.[34] The democratization of Nigeria in 1999 has improved cooperation among ECOWAS member states in working towards implementing a monetary union. This has also been evident in the country's contribution in fostering the objectives of the NEPAD and the active role she has played in resolving conflicts in Guinea Bissau, Liberia, Cote d'Ivoire and Sierra Leone through the ECOWAS Peace Keeping and Monitoring Group, ECOMOG.

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[33] 'Nigeria Returns to Military Rule," *U S Library of Congress, http://countrystudiesus/nigeria/3qhtm.*
[34] 'Nigeria Suspended From the Common wealth, Local Populace Stunned by Dissident Executions," *http://www.cnn.com/world/9511/nigeria.*

Thirdly, from its inception, the OAU defined itself as a body opposed to colonialism, apartheid in South Africa and foreign interference, asserting the non-aligned independence of African states during the Cold War era. In the 1980s after all African countries had achieved independence (with the exception of Namibia), the challenge of addressing the issue of continental socio-economic transformation became more urgent. This was reinforced by chronic economic decline and political decay experienced from the late 1970s. It is within this context that African leaders adopted the Lagos Plan of Action and the Final Act in 1980 that called for the establishment of the African Economic Community. Regional economic communities were to form one of the quintessential building blocks of the AEC[35].

In a changed historical and political context, the AU defines itself in terms of what Africa stands for including economic integration and stronger political commitments to uphold democracy and good governance. Another independent variable that would complement those mentioned above, and which affect this initiative include political instability in countries in the region with the Cote d'Ivoire as the most recent example as well economic asymmetries among states in the community.

Review of relevant literature

Research on monetary integration in general and in the West African region in particular is still ongoing. This section of the study identifies related sources which have relevance to the topic. In reviewing such literature, we identify authors with different views on particular issues related to regional economic and monetary integration, and make our contribution by adding relevant facts which we intend to

[35] Garth Le Pere, *Regional Economic Communities and the African Union: Quick Sand or Building Blocks,* in *The African Union Directory, 2002 40.*

put forward in the course of conducting this study in areas where such facts are lacking.

John Renninger, in his work *Multilateral Cooperation for Development in West Africa* gives an evaluative survey of the rationale for regional economic integration. He notes that the economies in West Africa are more competitive than complimentary because nearly all countries in the region produce primary products for markets of the industrialized world. As a result of this and basing his argument on the neo-classical theory of economic integration, Renninger contends that West African countries are not in a position to benefit from the static effects of regional integration.[36]

S.K.B. Asante, author of major works on African economic and political affairs however holds a different opinion. He argues that regional integration among a small group of developing countries such as those in Africa which provides for the pooling of resources can bring about results in development and enhanced bargaining power that are greater than the sum results if each country acted alone. In this respect, he concludes that regional economic integration in Africa is the only viable strategy for optimal development in the region in the contemporary economic and political circumstances in the continent as well as in the world.[37]

Another renowned author, Percy Mistry, shares the view of Asante. Mistry posits that taken individually, extant effective purchasing power in most African countries is so small and so concentrated as to render uneconomic the creation of any viable national market or industrial base. Transport costs in these countries, Mistry notes, account for between 30 and 50 per cent of the final retail price of consumer goods. He further asserts that excluding North Africa, sub Saharan African GDP is about the

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[36] John Renninger, *Multilateral Cooperation For Development in West Africa* (Oxford: Pergamon Press, 1978), 40

[37]SK.B. Asante, *Regionalism and Africa's Development: Expectations, Realities and Challenges.* (London, Macmillan Press, 1997), 32.

same as that of the Switzerland. Such challenges, he contends, make integration an attractive proposition to African leaders because it would help to overcome some of the difficulties posed by unviable markets through market enlargement.[38]

Clement Emenike for his part provides an account of the problems faced by most regional economic schemes in Africa, one of which is the size and power variability. Quoting Barrera and Haas, he states, "integration will be more successful if there is a relative power-size equilibrium among member states, that is, if no units in the proposed union present an overpowering presence in size and power vis-à-vis other units. Citing Nigeria as an example in the case of ECOWAS, he notes that Nigeria's hegemonic dominance is not conducive for the survival of the scheme.[39]

This assertion is shared by Timothy Shaw who points out that differences in size and uneven development were accountable for the demise of the East African Community. Accordingly, he writes that the economic strength of Nigeria presents ECOWAS with the major problem that small states in the community fear to be dominated and controlled by an all-powerful Nigeria. In his view, this factor will make integration in the region difficult because it is not clear if the mechanisms of the ECOWAS Treaty are sufficient to deal with the problem.[40]

Within the context of the above hypothesis, other authors have argued that Nigeria's hegemonic dominance in ECOWAS poses a major challenge to the creation of a monetary union. In this respect the suggestion of Senegal's Daouda Sow that Zaire (now the Democratic Republic of Congo) be included in the organization to

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[38] Percy Mistry, "Africa's Record of Regional Cooperation and Integration," *African Affairs*, 99(2000), 554.
[39] Clement Emenike, *The Political Economy of Foreign Policy In ECOWAS* (New York: St Martins Press, 1994), 191.
[40] See *Alternative Futures For Africa's Development* by Timothy Shaw (Colorado: West View Press, 1982),172

counterbalance Nigeria's dominance demonstrates the impact of the size power (mis) perceptions on foreign policy postulations.[41]

Conversely, Asante in *the Political Economy of Regionalism in West Africa* looks at the position of Nigeria from a different perspective. In his view, Nigeria could use her dominance to offer creative leadership in the community, a leadership aimed at maintaining the integrity of the union. In this light, he attributes Nigeria's role in the region to that which the United States once possessed in the modern world, which he describes as leadership without dominance. This leadership he asserts was tested inter alia in the role Nigeria played in the ratification of the protocol relating to the free movement of persons in the region.[42]

Furthermore, Van De Walle takes a critical look at the evolution of the CFA Franc zone since 1990.His approach centers on the relations between Franc zone members and international financial institutions. He notes that the devaluation of the CFA Franc in 1994 was on the one hand a result of its overvaluation and on the other, a major conditionality imposed by the Western donors. In this connection, he asserts that France announced that it would assist in the devaluation with a major debt relief initiative for the fourteen countries of the zone. Consequently the end of 1994 gave 3 billion US dollars given as official development funds, and 13 billion of bilateral debt was forgiven. Van De Walle therefore attributes the devaluation of the CFA as part of the conditionalities imposed by International Financial Institutions and bilateral donors.[43]

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[41] Timothy Shaw and Julius Emeka, *The Political Economy of Foreign Policy in ECOWAS* (London: St Martin's Press, 1994), 189.
[42] See Asante, *The Political Economy of Regionalism in Africa:A Decade of the Economic Community of West African States* (New York: Praeger Press, 1986),150.
[43] Nicolas Van De Walle, *African Economies and the Politics of permanent crisis* (Cambridge: Cambridge University Press, 2001), 222.

Similarly, Christopher Chapham views the devaluation of the CFA from the same perspective. He contends that overvaluation of the CFA Franc had done considerable damage to export earnings of the Franc zone states and imposed an increasing burden on the French Franc but more seriously, he notes that devaluation was externally imposed by International financial Institutions as one of the conditionalities of the Structural Adjustment Programme (SAP). Chaplam however takes a step further by comparing the devaluation of the CFA with those of other countries. He notes for example that during the same period the Ghanaian Cedi was devalued from an initial 1Cedi = 1 US Dollar in 1983 to 1Dollar = Cedi 400 by 1994.[44] That implies that between 1984 and 1994 the Cedi had depreciated by about 400 per cent against the Dollar.

For his part, Paul Collier looks at the CFA devaluation and the survival of the two central banks in the CFA zone as agencies of restraint. According to him, agencies of restraint are institutions, which protect public assets from depletion and prevent inflationary money printing. He concludes that devaluation of the CFA in 1994 was in a bid to curb real wage rigidity caused by negative external shocks and not necessarily as a condition imposed by international financial institutions.[45]

More so, Robert Thomas in the *Evolution and performance of the Economic Community of West African States* posits that one of the effects of dissimilar monetary systems in the West African region is the depressing effect on the volume of intra ECOWAS trade and its failure to galvanize payment for goods and services. With these consequences in mind, he notes that in an effort to harmonize monetary systems, the authorities in the region created the West African Clearing House in 1975 to work

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[44] Christopher Chaplam, *Africa and the international system: the Politics of State survival* (Cambridge: Cambridge University Press, 1996), 171.
[45] Paul Collier, "Africa's External Economic Relations 1960-1990" *African Affairs* (1991), 90, 339-356.

in tandem with central banks of the region. He asserts further that the West African Clearing House was created as a mechanism to facilitate intra regional trade.[46]

Nelson Magbagbeola sheds more light on the role of the West African Clearing House and other institutions set up by the organization to facilitate monetary integration. He states that in 1986, the West African Clearing House was restructured and metamorphosed into the West African Monetary Agency with an expanded mandate of promoting trade liberalization and monetary cooperation. Magbagbeola adds that the agency is further charged with the responsibility of creating necessary conditions, which would lead to the implementation of uniform monetary policies and the creation of a single currency.[47]

Furthermore, Frank Dewoto acknowledges the efforts made by ECOWAS in forging towards a monetary union, but points out that West Africa is ill prepared for a common currency because it does not have the required macro economic structures to deal with economic stress across the region. This, he maintains, is largely due to the fact that the economies in the region are not open enough to each other. Dewoto states further that barriers to intra regional trade are dominant, and constrain to factor mobility are numerous.[48]

The above analysis is shared by Paul Masson although he however takes a step further by providing some suggestions on how the organization could meet its objectives. He suggests that ECOWAS members should not rush to meet a very short proposed deadline for a monetary union .In his opinion, these countries could gain the benefits of exchange rate stability and mutual surveillance over macro economic

[46] Robert Thomas," The Origins, Evolution and Performance of ECOWAS since 1975"(PHD Dissertation, Howard University, 1987), 192.
[47]Nelson Magbagbeola, *The Quest For A West African Monetary Union: Implementation Issues, Progress and Prospects* (Ibadan: National Centre For Economic Management and Administration, 2001),1.
[48] Frank Dewoto. *Monetary Union in West Africa: Will the Benefits Accrue?* Data Bank Research, 2000.

policies through a closer form of regional cooperation, similar to the European monetary system- style mechanism. He further contends that it is important for member states of the organization to consider how the current political momentum for cooperation can contribute to improving policies in the region.[49]

For his part, Kasonga Raphael notes that interest in monetary integration in Africa dates back to the time of independence. He asserts that serious efforts were made by leaders of independent states to maintain the colonial monetary arrangements. Kasonga states that for various reasons these efforts achieved little success except in the Common Monetary Area in Southern Africa. He maintains that the period that followed the establishment of independent currencies, and central banks were characterized by over valuation of exchange rates.[50]

Paul Masson and Catherine Patillo take a broader view of monetary integration in Africa than Kasonga. They apply lessons from both experience and theory that lead to a number of conclusions. Patillo for example contends that, a monetary union among Eastern and Southern African countries seems unfeasible since a number of countries suffer from civil conflicts and drought and are far from achieving the macro economic stability of South Africa. Both authors assert further that the plan by Kenya, Uganda and Tanzania to create a common currency would favor Kenya, which unlike the two other countries exports substantial quantities of goods to its neigbours.[51]

Writing about monetary integration in Southern Africa, Yahane Khamfula contends that the issue of forming a monetary union in the Southern African Development Community (SADC) has recently received more serious attention than

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[49] See Paul Masson and Catherine Patillo. *"*Monetary Union in West Africa: An Agency or Restraint for Physical Policies." *Journal of African Economies vol11, 40.*

[50]Kasonga Raphael. *The process of Monetary integration in Eastern and Southern Africa* (Lusaka: COMESA Centre, 2002), 32.

[51]Paul Masson and Catherine Patillo. *The Monetary Geography of Africa.* (Washington: Brookings Institution Press, 2004) 45.

before. He notes that as a pacesetter to the formation of a fully-fledged monetary union in the SADC region, member states started off by adopting the Common Monetary Area (CMA) made up of Lesotho, Namibia, Swaziland and South Africa. Yahane asserts that the CMA represents a high degree of capital and market integration among SADC states. He however concludes that based on the findings of the optimum currency areas theory, the CMA cannot be transformed in to a full monetary union.[52]

Using the same approach, Olawale Ogunkola contends that like in the SADC, the states of West Africa have renewed their efforts in creating a monetary union. Monetary integration he notes is of paramount importance to the Non-CFA members of ECOWAS given that their Francophone counterparts share a common currency. Their economies are to an extent relatively stable and the degree of intra regional trade in the zone is higher than intra ECOWAS trade. Based on the findings of the currency areas theory, he concludes that ECOWAS is not yet ready for a monetary union.[53]

Franklin Vivekananda and Wilfred Ndongko, give a clear picture of the functioning of ECOWAS and problems faced by the organization. In this connection, they state that the problems of financial and monetary harmonization in the region arouse as a result of the existence of multiple monetary and currency zones in the community. They point out that because of the diversity of the economic and financial

[52] Yahane Khamfula and Mengsteab T, "South Africa and the Southern African Monetary Union: A Critical Review of Sources of Costs and Benefits" *The South African Journal Of Economics,* vol 72:1 March, 2004.
[53] Olawale Ogunkola, *The Second Monetary Zone in West Africa and the Future of a Single Monetary Zone in Sub Saharan Africa*, 9.

conditions among member states, priority policies and the objectives of member states as far as monetary integration is concerned will inevitably lead to conflict.[54]

One of the objectives of this study is show the steps the Community intends to take in bringing together the West African monetary Zone and its parallel Francophone UEMOA together which will eventually give rise to the West African Monetary Union and ultimately to the introduction of the "Eco" as a common currency. Mention will be made of the role and significance of the West African Monetary Institute established in Ghana, in 2001, in facilitating the monetary integration programme.

For his part, George Obiozo uses Neo functionalism as his theoretical framework in analyzing the viability of an economic and monetary union in West Africa. He maintains that there exists a continuation between economic integration and a political union. Both, according to him are linked together by a "spill over effect" through which the tasks and power of the central institutions are increased and integration subsequently encroaches on the politically sensitive area. He notes that the progression from a politically inspired common market to an economic union and finally to a political union among states is automatic.[55]

This study complements neo functionalism as used by Obiozo by applying Mattli's theory of regional integration among others. This theory evaluates the factors that determine the outcome of regional integration and examines the consequences of integration for non-members of a grouping. It also highlights the reasons why so many attempts at regional integration have failed while a few others have been

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[54] Franklin Vivekananda and Wilfred Ndongko, *Bilateral and Multilateral Cooperation in West Africa* (StockholmGeorge Obiozo et al, *Nigeria and ECOWAS Since 1895: Toward A Dynamic Regional Integration* (Enugu: Fourth Dimension Publishers, 1991), 3-4.lm: Bethany Books, 1990), 219.

[55] George Obiozo et al, *Nigeria and ECOWAS since 1985: toward a Dynamic Regional Integration* (Enugu: Fourth Dimension Publishers, 1991), 3-4.

crowned with success, and explains why non-members of a regional economic scheme seek to become members.

Conceptual and Theoretical Considerations

Walter Mattli's Theory of Regional Integration

Walter Mattli posits that the general analytical framework for understanding regional integration begins with a discussion of the factors determining the outcome of regional integration schemes, which is followed by an examination of the consequences of integration for outsiders. He defines integration as the voluntary linking in the economic domain of two or more formally independent states to the extent that the authority over key areas of domestic regulation is shifted to the super national level. Mattli's theory highlights two related puzzles of regional integration, one implicating the outsider countries in an integration process, the other, the insiders.[56]

The first puzzle, he notes, seeks to question why so many attempts at integration have failed while a few others have been crowned with success, and the second attempts to find out why outsiders (non members) seek to become insiders (members). Outsiders, he states, can become insiders either by joining an existing economic union or by creating their own regional group. Mattli holds that the first puzzle which includes the variation in outcomes is illustrated by the wide range of integration results. He contends that at one extreme, the EU has managed over the past to establish an array of institutions and policies as well as a broad and clearly defined set of rules which are hierarchically superior to domestic law and directly applicable to the member states in the union. This policy, he asserts, has boosted trade and

[56] Walter Mattli, *The logic of Regional Integration: Europe and Beyond* (Cambridge: Cambridge University Press, 1999), 99.

investment and brought unprecedented prosperity to an area long known for its economic calamities.[57]

At the other extreme, the Latin American Free Trade Area (LAFTA), the Andean Pact, like ECOWAS, have achieved limited success toward integration. According to supporters of this theory, two types of conditions need to be satisfied for integration to succeed. First the potential for economic gains must be significant. If there is little potential for gain, perhaps because regional economies lack complementarity, the process will quickly peter out.

The second condition, Mattli' contends, is the fulfillment of supply conditions. These are conditions under which political leaders are willing and able to accommodate demands for regional institutions at each step of the integration process. Willingness depends on the payoff of integration to political leaders; they may be more willing to deepen integration if such a move is expected to improve their chances of retaining power, for example by notably improving domestic economic conditions.[58]

However, even willing political leaders may be unable to supply regional institutions because of collective action problems. One such problem, coordination, is particularly salient in integration. This leads to a key supply condition; the presence of a benevolent leading country within the region seeking integration. Such a contested institutional leadership or the absence of leadership makes coordination games very difficult to resolve.[59]

Mattli argues further that willingness depends greatly on the payoff for political leaders. He states that if these leaders value political autonomy, (absence of

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[57]Ibid., 93.
[58] Ibid., 95.
[59] Walter Mattli, *The Logic of Regional Economic Integration; Europe and Beyond*, (Cambridge: Cambridge University Press, 1999), 98.

interference by supranational powers), and political power, they are unlikely to seek deep levels of integration as long as their economies are relatively prosperous. He notes that if this were the case, it would be needless to sacrifice national sovereignty and pay the price of membership in a regional group if the economy is growing relatively fast and voters are content.

The second puzzle, Mattli asserts, is the timing of the decision by outsider countries to seek integration either by joining an already existing economic union or by creating other unions. In ECOWAS for example non-members of the CFA franc zone have the option of either joining the CFA zone or consolidate the newly created West African Monetary Zone. He notes further that this puzzle is related to the first one because the outcome of an integration project may have external effects on outsiders for example through diversion in trade, investment and aid.[60] Turning to ECOWAS once again the stable nature of intra regional trade in the CFA zone and regular financial aid from France which has been constant since independence but has dim prospects of continuing in the future are some of the factors which trigger Anglophone states to form a monetary union with their Francophone counterparts.

More so, Mattli asserts that affected outsiders will have an incentive to join an economic union in the hope that accession will improve their economic performance and hence their likelihood of staying in power. Economic difficulties, some claim, can equally serve as a background condition for integration. For example the adoption of a single European Act was a response to slow economic growth in the 1980s. In the West African region, monetary integration is regarded as a means to counteract perceived economic and political weaknesses.[61] Similarly, Canada and Mexico turned

[60] Ibid.,100 .
[61] Richard Caves, *Multilateral Enterprise and Economic Analysis* (Cambridge: Cambridge University Press, 1996),46.

to the United States when their economic performance was in trouble, by forming the North American free Trade Area (NAFTA).

The linkage between trade and monetary integration in this regard stems from the fact that, both concepts are two of the five progressive stages that ultimately lead to complete economic integration. The first stage is the Preferential Trade Agreement (PTA) considered to be the lowest level of integration and countries agree at this stage to lower trade barriers between themselves. Each country sets its own trade policies vis-à-vis non-members though a most favoured national clause usually precludes preferential treatment by any member country to a non-member.[62]

Then there is the Free Trade Area. At this level, member countries remove barriers on intra-group trade for all goods or for an agreed set of goods. The ECOWAS has eliminated trade barriers for some products and reduced them for others. In addition, with regard to goods considered to have originated from ECOWAS member states, ECOWAS citizens must own at least 25 per cent of the equity capital of the enterprises producing them.

Next is the customs union, in which case member countries not only eliminate trade barriers among themselves, but also maintain common trade barriers for goods imported from non-members. The three members of the Manu River Union, in West Africa; Guinea, Liberia and Sierra Leone established a common external tariff in 1977. The *Union Douaniere et Economique de L'Afrique Centrale,* UDEAC (Central African Customs Union) in CFA zone in Central Africa was conceived in 1996 and has now been transformed to now Central African Economic and Monetary Community, CEMAC.

[62] Mare Paoline et al, "The West African Monetary Union, Springboard for Development in West Africa," Club de Bruxells, 1996.

After failing to achieve a customs union in 1990 as was originally stipulated, ECOWAS set the year 2000 as its new target date. Given the slow nature of implementation of most of its provisions, the deadline of 2000 was postponed. The next stage of economic integration extends to the customs union by allowing free movement of factors of production, (labour and capital) within the bloc. ECOWAS has shown significant progress in intra-regional immigration. A protocol on the free movement of persons and right of residence was adopted in 1979.[63]

Monetary integration is thus the last stage in the process of economic integration. It is regarded as the continuum of arrangements that promote trade. However it is important to note that not all monetary unions go through all the stages discussed above. The CFA zone for example inherited a common currency as a colonial legacy, with little regard for regional economic considerations. It was only in 1994 when the UEMOA replaced the UMOA that the issue of regional economic integration was placed as a focal point for their monetary arrangement.

It is also important to note that willingness brought about by economic difficulties is no guarantee for successful integration. Willing leaders may still find it difficult to supply integration because of collective action problems. In this connection, Duncan Snidal and Authur Stein provide useful insights into two types of collective action dilemmas that are particularly relevant to the study of regional integration. These include the prisoner's dilemma and coordination games.[64]

The prisoner's dilemma game has beneficially influenced the bulk of international cooperation literature. The Prisoner's dilemma game is the standard representation of externalities where, in the pursuit of their own private gains, actors impose costs on

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[63] Ibid.

[64] Duncan Snidal and Arthur Stein, *Why Nations Cooperate: Circumstance and Choice in International Relations* (New York: Cornell University Press, 1990), 58.

each other, independent of each other's action.[65] The extension of the two actor's prisoner dilemma game to a third actor increases the difficulties of cooperation. As the number of actors increase, information and communication problems become severe and actors in cooperative arrangements may find it easier to cheat with impunity. However the cooperation outlook brightens as the prisoner's dilemma game is played through time.[66]

Furthermore, Snidal opines that the problem in prisoner's dilemma is that in pursuing its self interest, each state imposes costs on the other independent of the other's policy while in the coordination game each state imposes costs or benefits on the other contingent upon the other's policy. The coordination game is solved if there is one state, (a regional leader) whose membership or cooperation in the group is perceived by all or a majority within the group to be more important to the group than to any other state. Such leaders might help to ease distributional issues which arise as coordination games are played over time.[67] Nigeria in the West African region has on several occasions taken the role of a regional leader particularly through the ECOWAS peacekeeping and monitoring group (ECOMOG).

The relation between the prisoner's dilemma and coordination with the problem at hand is that proponents of both concepts have advanced that, as the number of members in regional groupings increase, there is likely to be a commensurate increase in problems of communication and the tendency for states to perceive that their individual actions are less visible. In the context of ECOWAS and the CFA zone, Nigeria for example is perceived as a difficult partner for the rest of the region given the country's greater size, and large budget deficit in recent years. Moreover as a

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[65] Ibid., 59.
[66]Duncan Snidal, "Cooperation versus prisoner's Dilemma: Implications for international Cooperation and Regimes" *American political Science Review*, December 1985, 942.
[67] Snidal, "Cooperation versus prisoner's dilemma," *American Political Science review*, 1985,943.

major oil exporter, her economy differs greatly from those of its neighbours which export other primary commodities and are thus subject to different shocks. Indeed Nigeria has the potential to influence a monetary union in ways that its potential partners particularly those of the Francophone zone would find undesirable. The expansion of the long-standing CFA zone to include Nigeria would be decidedly inferior to their current situation.

Nevertheless, an increase in the number of states in a union may have an opposite effect by opening up new areas or levels of cooperation which may not be accessible to a small number of states. The conclusion that large numbers of states serve to impede cooperation is thus only a possibility because there are a large number of states involved in this issue sixteen in the case of ECOWAS. In sum therefore, even though Mattli's theory may not answer all questions pertaining to regional integration, it provides valuable insights into how and why states find it necessary to integrate their economies.[68] The next section sheds some light on the concept of monetary integration.

The Concept of Monetary Integration

In attempting to define a monetary union, it may be helpful to explain one or two concepts, which are commonly found in the literature on economic and monetary union. One such concept is monetary integration, an aspect of economic integration, which involves exchange rate unification and currency convertibility. Monetary integration is an all-embracing concept which may consist of monetary union or a

[68] "The Challenges of Economic Integration, Selected Papers for the 1992 annual Nigerian Economic Society." Ibadan: *African Book Builders,* 1992, 57.

common currency area.[69] A common currency area on the other hand entails the existence of a single currency and hence the absence of an exchange rate mechanism within the area except as it relates to converting the currency into the currencies of non-members. This distinction may however be regarded merely as an academic exercise as the two terms have come to be used interchangeably in practice.

Monetary and financial integration involve a process whereby a group of countries usually in adjacent geographical areas form a monetary union characterized by the establishment of one central monetary authority which takes over the formulation of the Union's monetary and fiscal policies, the issuance of a single currency to which all the national currencies of member countries are convertible, the flow of the union's currency which is unrestricted among member countries, and the pooling of foreign exchange reserves of member countries.[70] Monetary and financial integration can also include other elements such as free movement of people, goods and capital, fixed and unalterable exchange rates, common medium term or short term economic policies, and also common structural policies as well as common institutions, as was the case when the European Economic Community adopted its economic and monetary union in 1971.[71]

In this respect, a monetary union then becomes an area within which exchange rates bear an immutable relationship to each other. If there are several currencies in the integrating zone as in ECOWAS, these currencies must be fully convertible one into the other at permanently fixed exchange rates thereby effectively creating a single currency. This could be effected through an exchange rate mechanism such as the

[69] Andre Rose, "Common Currency Areas in Practice: Can Currency Unions Explain "Home Bias?" *http://www.bankofcanada.ca/publications/working.paper/2000/rose.pdf+common+currency+area&hl=enie+utf-8.*
[70] "The Challenges of Economic Integration, Selected Papers for the 1992 Annual Conference on Nigerian economic Society," (African Book Builders, 1992), 54.
[71] Ibid.

European exchange rate mechanism or the ECOWAS exchange rate mechanism, which is yet to fully come into force.[72]

A full blown monetary union is usually characterized by a common currency, common monetary and fixed policies, a common pool of foreign exchange reserves, a harmonized credit policy and a common monetary authority or central bank which takes over the formulation of the unions monetary policy and issues a single currency to which all the currencies of the member countries are convertible.[73] The case for monetary unions is based on the grounds that the standard function of money as a medium of exchange and store of value is more effectively performed as the cost for conversion and is eliminated hence realizing real savings. Thus there would be zero transaction costs related to exchange rate variability arising from the use of different national currencies for inter-regional trade and investment.[74]

Prior to and immediately after independence, most African countries had stronger financial links with their former colonial powers than with each other. Transactions involving the use of foreign exchange were conducted by transfers through London and Paris. This phenomenon partly reflects the strictly controlled money markets of African countries and the inconvertibility of their currencies. However, with the progressive dismantling of colonial trade preferences, and achievement of greater independence, in monetary matters, this situation became unrealistic.

Another important aspect of monetary and financial integration that needs to be emphasized is the convertibility of currencies. Currency convertibility is the ability of

[72] Mike Obadan, "Exchange Rate Mechanism under the West African Monetary Zone," *http://www.cenbank.org/publications/efr/rd/2002/efrvol40-4-8.pdf.*
[73] "Monetary and Financial Integration: Evidence from the European Monetary Union," *Economic Research Data FRBSF, 2004, http://www.frbst.org/publications/economics/letter/2004/e/2004.html.*
[74] Charles Mordi, The Challenges of Monetary Union: Risks and Pitfalls and How to Respond to them," *http"//www.cenbank.org/out/publications/efr/rd/2002/efrvol40-40.pdf.*

residents and non-residents to exchange domestic currency for foreign currency. [75] Governments generally impose limitations on the use of foreign currency, which can take the form of prohibitions, taxes, special deposits, nominal ceilings or procedures for allocating foreign exchange. Monetary integration has therefore been canvassed as an important tool for promoting trade flows among countries.[76] The multiplicity of currencies and exchange rates, it has been argued, hinders trade due to the high transaction costs associated with currency conversions.[77]

The theories of optimum currency areas are usually applied to determine the feasibility of a monetary union. The various theories are built around particular concepts. Thus there is no standard theory of optimum currency areas but rather there are various approaches inspired by Robert A. Mundell's seminal article in 1961, in which he pointed out that the international system is characterized by a multiplicity of different currencies which for the most part are based on sovereign nation states. He went further to pose the question "when is it advantageous for a number of regions to relinquish their monetary sovereignty in favour of a common currency?"[78]

An optimum currency area has thus been defined as geographical and economic unit in which one currency and one monetary policy operate.[79] It is important to examine them in their totality before a decision can be taken on the desirability of a monetary union. The traditional literature suggests criterion for judging whether regions should form a currency union. These include the mobility of factors of

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[75] *The Challenges of Economic Integration selected Papers for the 1992 Annual Conference of the Nigerian Economic Society* (Ibadan: African Book Builders 1992), 57.
[76] *Trade Effects of Monetary Integration in Large Mature Economies: A Primer of the EMU* (Kiel Institute for World Economics: Kiel Working Paper, No 1137, 2002), 35.
[77] Charles O. Mordi, "The Challenges of Monetary Union: Risks and Pitfalls and How to Respond to them," *http://www.cenbank.org/out/publications/efr/rd/2002/efrvol40-4-4.pdf.*
[78] Robert Mundell, "A Theory of Optimum Currency Areas," *American Economic Review,* Vol l1 No 4, 1961, 660-662.
[79] Ronald Mackinnon, "Mundell, The Euro and Optimum Currency Areas," *http://www.econ.stanford.edu/faculty/workp/sw00009.pdf.*

production, flexibility of prices and wages, openness to trade and diversity of production.[80]

This criterion can be grouped into two, those that refer to a particular country (country specific criteria) and those that refer to choices of countries that are suitable for a currency union (union specific criteria). For instance, Mundell argued that the more mobile factors of production are within a region, the easier it is to form a monetary union.[81] On the other hand Ronald Mckinnon based his thesis on the degree of openness in trade flows. He contends that the more open an economy in terms of trade flows, the more beneficial for it to join a monetary union.[82]

Other scholars like Christopher Tower and Willet Thomas formulated the notion of degree of convergence of opinion, views and attitudes on policy integration in the areas of inflation, employment and growth. Yet others posit that the degree of product diversification, nature of demand shocks and policy complementarities are important in determining the feasibility of a monetary union. These factors taken together would appear to limit the horizon of monetary integration in several African groupings. In addition, the low levels of economic integration in ECOWAS and COMESA for example, the low degree of openness of the economies in the regions all point to the need to forge political consensus to achieve integration. Because the acquisition of the desired political will may ultimately make it possible to form a monetary union.[83] It is useful at associated benefits and costs of monetary integration.

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[80] "Case for and Against Joining An Optimum Currency Area," *http://www.columbia.edu/~ram15/eocataviv4.html.*
[81] Fadhel Kaboub, "Optimum Currency Areas," *http://www.f.students.umkc.edu/fkf/c8/oca.htm.*
[82] Herbert Grubel, "New Criteria for optimum currency Areas," *www.sfu.ca/~grube/lloyd%20festscrift .pdf.*
[83] Charles Mordi, "The Challenges of Monetary Union: Risks and Pittfalls and How to Respond to them," *http://ww.cenbank.org/out/publications/efr/rd/2002/efrvol40-4-4.*

The Benefits and Costs Associated with Monetary and Financial Integration.

Generally speaking, the virtues of monetary and financial integration appear to be widely accepted; expanded aggregate investment, improved resource allocation, enhanced financial intermediation and greater international trade. Financial integration also serves as the stabilizer for the common currency, it saves international reserves by providing alternative choices between foreign and domestic goods, services and assets.[84] The question however is whether countries with highly protected economies will fund the inevitable costs of monetary and financial integration. These costs will stem mainly from the constraints such integration may impose on the pursuit of their own national financial, monetary and exchange rate policies.[85]

While the potential benefits from such integration take considerable time to be realized, the costs are immediate. Similarly, in the short run, these benefits will not accrue to all participants in equal measure within the same time frame, although in the long run, the benefits will spread more evenly. These factors help to explain why members of various trade groupings in Africa and indeed in most of the developing world have been unwilling to move towards monetary and financial integration.[86]

Benefits

The traditional optimum currency areas literature advanced by Robert Mundell suggests that countries joining a monetary union will benefit from lower transaction costs associated with trading goods and assets in different currencies. Proponents of monetary integration assert that potential microeconomic efficiency gains from

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[84] Pierre Richard, "Benefits and Costs of International Financial Integration: Theory and Facts," *World Bank: Policy Research Working Paper Series, No 2699, 36.*
[85] A. J. Ojo, Problems of Monetary and Financial Integration in ECOWAS," Paper Presented at the West African Economic Association, 4th Biennal Conference, Lome Togo, 1986.
[86] Dadzie, K. K, "The European Economic Integration Process: Lessons for Africa" *The Bullion,* July 1990, 21-26.

joining a monetary union are due to the elimination of nominal exchange rate volatility, deeper financial integration and in the case of joining a dominant currency area like the euro, international acceptance of the currency.[87] Furthermore, renewed interest in monetary integration may not be unconnected with the increasing closer integration among regional economies around the world which calls for greater monetary coordination against the background of globalization of the world economy, disappearance of fixed exchange rate regimes and capital account liberalization Indeed capital account liberalization when combined with the attachment of some countries to exchange rate stability makes it attractive to move from a soft peg to a hard peg.[88]

Furthermore, a major argument in favour of monetary integration rests on its contribution towards reducing the misallocation of resources that may otherwise occur if speculative influences, through their impact on exchange rates distort the price of rising capital in the union. Resource allocation gains may be obtained from increased intra-union trade securities as a result of returns to different kinds of capital coming close together in the member countries. This point can be simplified under the discussion of the optimum currency areas given that two countries might want to form a monetary union to improve resource allocation.[89] Producers would regard not only their own country but also the entire common currency area as their marketing territory. If increasing returns to scale is present, producers would expand productive capacities, capital would be allocated more efficiently and labour would become a more homogenous factor of production.[90]

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[87] Danzie, K, "The European Economic Integration Process: Lessons for Africa," *The Bullion,* July 1990, 28.
[88] "Costs and Benefits of Monetary integration," *http://www.homepage.ntworld.com/peter.mklem/euro/costs&benefits.htm.*
[89] Ibid
[90] Ibid.

A further source of gain may arise from reduced costs of financial management. Monetary integration would make it possible to spread the overhead costs in financial transactions widely. In addition, part of the activities of foreign exchange-dealing institutions could be dispensed thus generating resource savings. Peter Robson and B.O Sodersten have argued that when several countries come together in a monetary union, there would be fewer disturbances caused by random shocks. They also point out that a decline in incomes in one area could be compensated by an increase in another area.[91] Thus the impact of any specific disturbance could be less as the size of the area increases.

More so, advocates of monetary unions assert that a favourable effect of monetary integration may be to provide an agency of restraint over macroeconomic policies generally, if the monetary union contains convergence criteria requiring conservative monetary and fiscal policies. Paul Masson in this regard, contends that they are more likely to be effective if there is some external link, for instance, an external currency peg, and a visible indicator of balance of payments pressure such as the level of reserves.[92] The CFA zones have a fixed peg to the Euro as well as a guarantee of convertibility of their currency from the French Treasury, but they are forced to take emergency measures if the reserves cover ratio falls below a certain level. There is however a serious debate over the effectiveness of this external agency of restraint, especially since one of the CFA Franc zones, the *Communaute` Economique` et Monitaire de L'Afrique Centrale* (CEMAC), has exhibited little fiscal discipline. This monetary union was not enough to provide fiscal discipline and needs to be reinforced

[91] Ibid.
[92] Paul Masson and Catherine Pattillo, "Monetary Union in West Africa: An Agency of Restraint For Fiscal Policies?" *Journal of African Economies* vol 11, Number 3, 342.

by parallel regional arrangements and or links to financial and technical assistance of industrial countries that makes it costly to violate the rules of the monetary union. [93]

It has also been argued that given the fixity of exchange rates under a monetary union arrangement, speculative capital flows would be eliminated, thereby relieving the authorities of frustration in their monetary control. All things being equal, a monetary zone with a supranational currency would be more stable and safer for capital mobility. Long-term interest rates would decline and be less volatile.[94] This was the experience of Europe where interest rates declined in a number of countries notably, Ireland, Italy, Portugal and Spain. In effect, this development made it easier to reduce fiscal deficits and promote growth. Beautiful as this scenario seems, theorists of monetary and financial integration warn that it has some qualifications given that the fixity of exchange rates may not be perfectly certain, depending on the particular evolutionary stage of a currency union.[95]

They point out further that when the possibility of an exchange rate misalignment within the union threatens and the country concerned is discouraged from making a prompt decision due to probable overall reluctance of the union to disrupt the unified rate, it may be that speculative capital flows are larger than they otherwise would have been.[96] This is particularly evident in the politically unstable region of West Africa where the risk of volatility in portfolio flows in the near term cannot be ruled out.

More so, monetary integration theorists advance that monetary union involving a common currency is tantamount to the unification of the national capital markets of

[93] Ibid.,243.
[94] Chris Itsede "The Challenge of Monetary Union: Gains and Opportunities," *http://www.cenbank.org/out/publications/er/rd/2002/efrvol40-40-4-3.pdf.*
[95] Ibid.
[96] Chris Itsede, 'The Challenge of Monetary Unions: Gains and Opportunities," *http://www.cenbank..org/out/publications/er/rd/2002/efrvol40-40-4-3.pdf.*

the integrating countries. This, they argue, promotes market deepening, greater competition and more investment opportunities for institutional and individual investors. Banks, brokerage firms, issuing houses and other capital market operators can expand their operations rapidly for investible funds held by savers in cross border accounts. Private firms and public entities issuing debt instruments would have a larger pool to tap into.[97] For instance, adoption of a common currency by members of the West African Monetary Zone (WAMZ) implies that the nationals of the zone could freely trade on the Nigerian Stock Exchange and Ghana Stock Exchange without exchange rate or currency risks.

However, a major challenge in this regard may be that the combined effect of increased competition and a large market could result in a fall in long run interest rates, which is a critical condition for sustained economic growth. In fact, the viability and growth of some domestic capital markets would be somewhat limited without opening their doors to the regional possibilities. It is in this regard that some economists recommend that in order to ensure a safe level and viable playing turf, a unified capital market should have a common regulatory framework with common rules, standards and ethics that would guide cross-border investments within the integrating zone.[98]

Lastly, there are huge seignorage gains and losses from the issuance of a common currency, especially if monetary integration results in significant expansion in intra-union trade. The large amount involved in the printing of union currency would entail a relatively lower unit cost of printing compared to printing national currencies. All things considered, opportunities for seignorage, profit from the issue of interest free currency abound more in a monetary union than in a national economy. Logical as

[97] Job Abiodun Oluninshola, "Concepts Objectives and Rational For Monetary Integration," *http://www . cenbank.org/out/publications/guidelines/pid/2004/wamz.pdf.*
[98] Ibid,.

this issue seems, it is a tricky one that could make or mar a monetary union. The problem is that it has been estimated that seignorage contributes about 0.5 per cent of the gross domestic product of most countries. The issue at stake concerns one of the principal sources of income to a central bank in a developing economy. Since rationalization of currency printing would gradually eliminate this source of revenue to the national economies, it is important that an acceptable modality for apportioning seignorage gains is agreed at the initial stage. Not even the advanced economies of Europe failed to negotiate this corner with due caution.[99] The EU compromise was to phase in an agreed formula for distributing seignorage gains. We now look at the perceived costs of monetary integration.

Costs

The single most important cost of a monetary union derives from the fact that when a country relinquishes its national currency, it also relinquishes an important instrument of economic policy. That is to say, it loses its ability to conduct its national monetary policy. In other words, in a full monetary union, the central bank either ceases to exist or has no real power.[100] It loses national sovereignty in the use of monetary instruments such as the exchange rate and the interest rate. This implies that a nation joining a monetary union will not be able anymore to change the price of its currency (by devaluations and revaluations) or to determine the quality of the national currency in circulation.[101]

[99] Chris Itsede, "The Challenge of Monetary unions: Gains and Opportunities," *http://www.cenbank. Org/out/efr/2002/efrvol40-4-3.pdf.*
[100] Patrick Minford, "The Costs and Benefits of Economic and Monetary Union to the UK Economy- the Fifth Overview Test, Cardiff Business School, *http://www.euro-know.org/bfrosemutest588.pdf.*
[101] Simon Wren-Lewis, EMU: A Simple Guide to Pro and Cons" University of Exeter, *htt://www.ex. ac.uk/~swrenlew/emu-article-article-for-new-economy-final.pdf.*

The use of the exchange and interest rate as policy instruments for example is useful for an individual country because nations are different in several respects that could require changes in these key price variables to occur. Such areas include shifts in demand, different preferences of countries about inflation and unemployment, differences in labour market institutions, differences in legal systems, differences in growth rates and different fiscal systems as well as the seignorage problem.[102] Thus the loss of independent monetary policy may constrain the ability of individual countries in a monetary union to effectively tackle these issues.

Another potential cost of monetary integration is related to the likelihood of the economies in the monetary union facing different shocks. This is the problem of asymmetric shocks, that is, shocks which in turn affect some members and not others and here the use of the exchange rate is useful. Since economies linked to a monetary union must necessarily adopt the same monetary policy, such a monetary policy may inevitably prove inappropriate in the face of very different shocks. The larger and more asymmetric the shocks, the greater the cost of a fixed exchange rate since the economies experiencing the most shocks do not have the luxury of adjusting the exchange rate to address the problem.[103] For the proposed West African Monetary Zone countries, the problem of asymmetric shocks is real especially because these countries, with the exception of Nigeria export mainly primary commodities whose terms of trade shocks have been substantial over time and their economies are less diversified.

Problems may emerge when economies with different fundamental economic structures, levels of efficiency, productivity and inflation are integrated under a single

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[102] S. Timori, *Toward Monetary Cooperation in West Africa, in Economic Cooperation and Regional Integration in Africa*, Naceur Bourename et al eds, (Nairobi: African Academy of Sciences, 1996), 44
[103] S.Timori *Towards Monetary Cooperation in West Africa,* in *Economic Cooperation and Regional Integration in Africa,* eds Naceur Bourename et al. (Nairobi: African Academy of Sciences, 1996), 143.

currency. If all economies were the same, and had similar objectives, they would possibly adopt the same policies and respond in the same way to changing circumstances thus eliminating many of the disadvantages of fixed exchange rates. The main rationale for fixing exchange rates is because economies are not all the same and it is necessary to constrain national monetary authorities from short-term political aims for the sake of overall efficiency gain.[104]

Following from the above it is germane to point out that a common currency raises some policy challenges including the possibility of differences in the transmission mechanism of monetary policy in member countries due to differences in institutional frameworks and the financial intermediation process. Inflation and output growth may be more sensitive to changes in short term interest rates in some countries than in others due to differences in bank lending, relative to other forms of financing, differences in household norms towards indebtedness and differences in fixed and flexible interest rates in debt instruments.[105] It is easier to adopt a single currency in countries with similar transmission mechanisms of monetary policy.

Challenges equally transcend political, economic, and institutional factors, which on the surface may appear trivial but indeed have implications for long term sustainability of a monetary union. One such challenge is the political will and commitment on the part of member states particularly in developing countries.[106] In the West African region for instance, it must be acknowledged that the six predominantly Anglophone countries of the second monetary zone and particularly so on the part of Ghana and Nigeria have demonstrated strong political will and greater and more specific commitments to proceed with monetary integration. Indeed such

[104] Ibid.,146.
[105] Stanley Fisher, "Exchange Rate Regimes: Is the Bipolar View Correct?" *IMF, Finance and Development, 2001, Vol 38, No 2.*
[106] Helmut Wagner, "Pitfalls for European Enlargement Process- Challenges for Monetary Policy," *http://www.fr.cfsde/papers/wagner.pdf.*

political will and commitments are unparallel in the history of the formation of monetary unions. The issue at hand is how to transfer this to the larger group of the ECOWAS membership so that the planned single zone comes to fruition with minimal delay. Thus building up political credibility is both a challenge and a risk that monetary union members will have to contend with. The next section highlights the importance of exchange rate regimes and their implications for domestic economy and actors within it.

Exchange Rate Regimes and Their Implications for Domestic Economies.

An exchange rate is a rate at which one currency can be exchanged for another. There are two ways the price of a currency can be determined against another. A fixed or pegged rate and a floating or adjusting rate. A fixed rate is a rate the government or central bank sets and maintains as the official exchange rate. A set price is determined against a major world currency, usually the US Dollar, and other major currencies such as the Euro, the Yen, or a basket of currencies. In order to maintain the local exchange rate, the central bank buys and sells its own currency on the foreign exchange market in return for the currency to which it is pegged. It usually has an institutional guarantee that it will stay fixed at least in the form of a currency board, or dollarization of monetary union.[107]

Unlike the fixed exchange rate, a floating or adjusting exchange rate is determined by the private market through supply and demand. A floating rate is often termed "self-correcting" as any differences in supply and demand will automatically be corrected in the market. If demand for a currency is low for example, its value will decrease thus making imported goods more expensive and thus stimulating demand

[107] "Floating and Fixed Exchange Rates," *Http://www.investopedia.com/articles/03/020603.asp*

for local goods and services. This in turn will generate more jobs and hence an auto-correction would occur in the market.[108] A floating exchange is therefore constantly changing.

Over the past 150 years, the world has experienced three broad international monetary orders. For about fifty years before World War One and again in a modified form in the 1920s, most of the world was on the classical gold standard. Governments committed themselves to exchange gold for currency at an announced rate. From the late 1940s until the early 1970s, the Capitalist world was organized into the Bretton Woods monetary order. Under Bretton Woods, currencies were fixed to the US dollar and the US dollar was fixed to gold. However, national governments could change their exchange rates when they deemed it necessary. Under this adjustable peg system, currencies were as firmly fixed as under the classical gold standard.[109] Since 1973, the reigning order has been one in which the largest countries have had floating national currencies, while smaller countries have tended to either fix against one of the major currencies or to allow their currencies to float with varying degrees of government management.

Monetary regimes can be regional as well as global. Within the international free-for-all that has prevailed since 1973, a number of regional fixed rate systems have emerged. Some countries have fixed their currency to that of a larger nation. The CFA zone ties the currencies of fourteen states in West and Central Africa to the each other and to the Euro. Several countries in Latin America and the Caribbean have pegged their exchange rates to the US dollar. European monetary integration which began with a limited regional agreement evolved into a Deutsche mark line and eventually

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[108] Ibid

[109] Lawrence Broz, "The Political Economy of Exchange Rates," *http://www.people.fas.harvard.edu/~/~ frieden/oxfordversion.*

became a monetary union with a single currency (Euro) and a common Central Bank (European Central Bank). It is equally important to point out that the exchange rates of Swaziland and Lesotho are indeed pegged to the South African Rand.[110]

The intermediate regime that is usually excluded is the adjustable peg, the system embodied in the post Bretton Woods era, under which a country could normally have a fixed exchange rate but reserves the right to change this in extreme circumstances, (fundamental disequilibrium). William Johnson argues that the Bretton Woods system was inherently vulnerable in speculative crises in a world of high capital mobility and therefore sought to design systems that would embody enough flexibility to avoid misalignments emerging and to ensure that authorities did not find themselves in a position of offering the market a one way bet. This led to the literature in the late 1960s of crawling pegs and wider bands and in the late 1990s to that of target zones.[111]

In the light of this, Johnson came up with the "BBC Rules" as intermediate options, where BBC stands for Basket, Band and Crawl. The basket part of the proposal suggested that countries with diversified trade would do better to peg to a basket of currencies that would roughly stabilize their effective exchange rate, rather than to a single currency. This, he argues, would largely insulate countries from disturbances to trade competitiveness, output and inflation from capricious variations in third currency exchange rates notably the gyrations between the dollar, the Euro and the Yen.[112] However this does not imply that every country would be advised to adopt a basket peg.

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[110] Cletus Dordunoo and Dominique Njinkeu, 'Foreign Exchange Rate Regimes and Macroeconomic Performance in Sub-Saharan Africa," *Journal of African Economies* vol 6, Number 3 1996, 123.
[111] William Johnson , "Designing a middle Way Between Fixed and Flexible Exchange Rates," A Paper Presented at A Conference on "Monetary and Exchange Rate Policies :Options for Egypt ." Egyptian Centre for Economic Studies, November 2002.
[112]Ibid.

Johnson advanced several reasons for supporting the wide band. The first reason is to make sure that the authorities do not get in to a no-win situation of trying to defend a disequilibrium exchange rate at all precisely. A second reason is to give scope for an independent monetary policy to be used for anti cyclical purposes when a country found its cycle out of sync with the world norm. A third is to permit the parity (center of the band) to be adjusted, to keep it in line with the fundamentals, without provoking expectations of discrete exchange rate changes that might destabilize the markets.[113]

The final element of the BBC formula as advanced by Johnson is the crawl. This is used most often with the view to neutralize differential inflation. It can also be used to steer inflation down over time, though it could run the risk of undermining competitiveness if pursued too dogmatically. Given that it is difficult for regimes to be either fixed or fully flexible, the intermediate options could in principle, allow countries to reap the benefits of fixed or flexible regimes without incurring some of their hard costs.

It would however be instructive to look at the exchange regimes in Africa and analyze their performances in past years in relation to economic growth and inflation rates as well as trade. The dividing line between two groups of countries covered in this analysis is the foreign exchange adopted, these include the CFA zone for instance which in the past was pegged to the French Franc and now to the Euro, and other countries in Sub-Saharan Africa which have floating exchange rates. The main characteristics of the CFA zone as noted above is clearly the common currency, which was until 1999, freely convertible to the French Franc (and now to the Euro) at a fixed rate thus providing an anchor for economic and financial policies. By contrast, other

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[113] Ibid.

Sub-Saharan African Countries called for the present purposes "non-CFA" countries, have their own national currencies whose exchange rates have frequently been adjusted in response to external shocks or other undesirable changes in relative competitiveness.

With regard to growth and inflation it has been observed that in the past two decades, average economic growth in the two African regions demarcated for the purpose of this study, have been the weakest in the developing world. With continued rapid population growth, average per capita income has stagnated at a very low level. The output has been uneven both over time and across countries. Total output of the CFAF countries expanded relatively rapidly in the early 1980s but tended to shrink thereafter. In fact it was only with the devaluation of the CFA Franc in January 1994 that a partial recovery of output was triggered. The profile of growth has been a little different in the non-CFA zone, which since the mid 1980s experienced positive real per capita income growth.[114]

Inflation in the non-CFA countries has however been persistently higher than in the CFA area. Indeed consumer price inflation rose to more than 40 per cent in 1994-1995, exceeding that of the sharply devalued CFA countries by a large margin. The main factor contributing to the comparatively low inflation in the CFA has no doubt been the nominal anchor provided by the CFA Francs fixed at parity vis-à-vis the French Franc and now the Euro. Statistically, real GDP in the CFA zone countries increased by 4.3 per cent in 1981-85, 0.4 per cent in 1986 -93 and 2.8 per cent from 1994-1995, while for the Non-CFA countries, real GDP increased by 0.4 per cent in 1981-85, 4.4 per cent in 1986-93 and 3.0 per cent from 1994-1995.[115] It can therefore be argued that based on the past performances in the two regions, countries with

[114] Marc Klau, "Exchange Rate Regimes and Inflation and Output in Sub-Saharan African Countries," *BIS Working Paper* Bank For International Settlement, Monetary and Economic Development, 1998.
[115] Ibid.

pegged exchange rates had relatively low rates of inflation between 1981 and 1994 while those with floating exchange rates known for the purpose of this analysis as non-CFA countries, had higher growth rates than members of the CFA zone between 1986 and 1995.

As far as fiscal indicators are concerned, tight monetary policy pursued in the CFA zone to defend the fixed parity was not supported by budgetary restraint. Indeed the government budget deficit in terms of GDP has always been sizeable and since 1985, has exceeded that of the non-CFA countries by a large margin. This difference in budgetary performance can be traced to the revenue side, where the CFA Franc countries saw their public sector revenue relative to GDP declining. This underscores the difficulties faced by CFA Franc countries (and for that matter countries with fixed or pegged exchange rates) in consolidating their budgetary positions in periods of stagnant or declining output. Furthermore, the continued rise in the wage bill in relation to GDP crowded out important infrastructure investment projects.[116] By contrast, the non-CFA countries succeeded in keeping the growth of the government wage bill below that over expenditure, partly by reducing the size of their civil service and partly because nominal wage adjustments lagged behind rapid increases in consumer prices.

As far as trade is concerned, Ibrahim Elbadawi notes that fixed nominal exchange rates require conditions that are likely to be satisfied in African countries. In particular, a country should undertake a large proportion of its trade with the country to whose currency it pegs and has similar inflation levels and it should adopt an

[116] Ibid

institutional arrangement that assures credibility that the fixed rate commitment will be honored.[117]

As far as terms of trade are concerned, CFA zone countries recorded 95 per cent between 1986- 93 and 69 per cent in the period 1994-95. Non-CFA recorded 73 per cent from 1986-93 and 61 per cent between 1994 and 1995. In terms of trade performance, CFA zone countries fared better than their counterparts with adjusting regimes. On the other extreme, floating exchange rates are deemed to be excessively volatile. Consequently some economists opt for a managed system in which the currency is allowed to float within a band and where the authority intervenes only when the rate approaches the edges.[118]

Based on the above analysis, it can be said that there is no single exchange rate regime that is best for all countries in Africa in all circumstances. Member countries continue to have scope to choose the type of exchange rate regime that best suits their needs always with the proviso that the chosen regime must be credibly supported by policies consistent with their choice. Which exchange rate regime and associated policies are appropriate for a country depends on its particular circumstances. While increased capital mobility has been leading an increasing number of countries to either end of the spectrum, between firmly fixed rates or free floating, intermediate regimes like those recommended by Johnson William are likely to remain viable and appropriate in many cases.

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[117] Ibrahim Elbadawi and Raimundo Soto, 'Introduction to the December 1995 Plenary Session on Exchange Rates" *Journal of African Economies, Vol* 6, No 3, 1996, 3.
[118]Ibid., 4.

Research Methodology

This research is centered on treaties, statistical analysis, theories and concepts and economic and financial institutions. The data for the research has been organized into primary and secondary sources. The primary data consists of unpublished works, such as conference papers, documented interviews with economists, and reports as well as sources from the internet. These sources provide original information and data on historical and present trends towards economic and monetary integration as well as the politics of international cooperation, not only in Africa but also in other areas of the world. As far as internet sources are concerned, the ECOWAS official website and that for the West African Monetary Institute in Ghana, as well as a range of relevant sites are considered indispensable to the writing of this study. Of equal importance has been online information from a source who works at the West African Monetary Institute in Ghana and provided me with up to date information on the workings of the institute, which has as one of its aims the formation of the West African Central Bank.

Secondary sources include books, journals articles, United Nation's publications as well as publications from the IMF and World Bank. Most of these were retrieved from libraries around Wits campus, particularly from the South African Institute of International Affairs (SAIIA), the University of Pretoria Library, the Library of the University of South Africa, and more importantly from the Africa Institute of South Africa in Pretoria. These sources form the core of the study as they provide information on political/political economic aspects of interactions between states, theories of monetary integration, as well as recent developments in the continent.

Organization of Work

The first chapter outlined fundamental goals, the theoretical framework as well as the methodology. Chapter two highlights historical aspects of African experiences with monetary cooperation with a focus on the CFA zone for former French colonies and the West African Currency Board for British colonies. At best the historical record in West Africa has been one of mixed success and future monetary cooperation in Africa should build on lessons provided by the success and failures of the past. Chapter three highlights the quest for monetary integration in ECOWAS and the extent to which the organization has pursued this initiative. This chapter equally gives an assessment of the viability of a monetary union in the region using the optimum currency areas theory. Chapter four focuses on the obstacles and or challenges to the monetary integration initiative in West Africa. It highlights the dynamics involved in political cooperation among states and shows the extent to which, Nigeria's democratic transition, political instability in the region, political commitment or the lack thereof affects plans for a regional monetary union. This work ends with a conclusion, which outlines the findings of the research.