

# INTRODUCTION OF COMMON CURRENCY "ECO" IN WEST AFRICAN STATES: PROBLEMS, CHALLENGES, AND IMPACTS ON THE NATIONAL ECONOMIES OF MEMBER STATES

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## Abstract

This paper seeks to identify the problems, challenges, and the implications of introducing a common currency 'ECO' in West Africa on the economies within the sub region. Specifically, the study focuses on the mandates of trade, the Customs, Immigration and Monetary and Payment Commission under the institution of the economic order of West Africa States. The augmented gravity model of Rose (1999), Alesina (2000), and Barro and Tenreyro (2002) was used to estimate the effects of monetary union on trade. The result shows that the performance so far of member countries as at the end of 2002 in meeting the convergence criteria revealed that it was inadequate to support the launching of the monetary union in 2004. The study concludes that though the introduction of a single currency will foster trade within the West-African sub-region, most countries have difficulty meeting the convergence criteria that will foster smooth take off of the project. It therefore recommends that the implementation of the single currency and common monetary policy in West Africa should be a gradual process as most countries within the sub-region are not politically mature, let alone to meet the convergence criteria.

## Introduction

The aim of the ECOWAS is to promote accelerated and sustained economic activities, leading to the economic unity of West African sub region; the elimination of all customs and duties on trade among member states; the establishment of a

common commercial policy towards Third World countries. In short, in accordance with the ECOWAS Treaty- Article 2, ECOWAS aims, to promote economic development, regional integration, and trade in the member states.

In pursuit of these objectives, the Authority of Heads of States and Governments realized the problem posed by the multiplicity of inconvertible currencies to inter-regional transaction. Accordingly, the Authority through the recommendations of the Governors of the Central Banks adopted the ECOWAS Monetary Zone in the year 2000. A transitional period, 1990-2000 was set to achieve this objective. Within the transitional period, the Authority approved the following measures to be implemented:

### Short Term Measures

- ✍ Liquidation of arrears in West African Clearing House (WACH)
- ✍ Introduction of new payment systems
- ✍ Introduction of a credit and guarantee fund in WACH
- ✍ Transformation of WACH into specialized agency on ECOWAS

### Medium Term Objectives

- ✍ Adjustment of exchange rates to be equilibrium levels
- ✍ Adoption of ECOWAS Exchange Rate System
- ✍ Liberation of current and capital transactions within the community
- ✍ Adoption of a market-oriented approach in the use of monetary policy tools

### Goal of the West African Monetary Zone (WAMZ)

The goal of the monetary union in ECOWAS has long been an objective of the organization, going to its formation in 1975. It is intended to

accompany a broader integration process that would include enhanced regional trade and common institutions. In the colonial period, currency boards linked sets of countries in the region. On independence, however, these currency boards were dissolved with the exception of the CFA Franc zone, which included the Francophone countries of the region.

### **The Benefits of Economic Integration**

The benefits of international trade are numerous. It has been shown conclusively that more trade is better than limited trade, while some trade is better than no trade. To facilitate trade, there is the need for a means of payments. In this direction, it is necessary to have in place some form of monetary arrangements. Such arrangements are usually predicated on established patterns of trade. Trading arrangements or blocs precede monetary cooperation. To sustain and improve on trade within geographical or economic blocs, customs procedures could be streamlined through the adoption of common rules and the institution of a common external tariff. Thus, trade within the zone adopting the common policies would become relatively easier, less costly and generate increased economies of scale over time. This explains the reasons for the proliferation of economic or regional blocs all over the world at the same time that multilateral trading arrangement is being canvassed as the answer to global prosperity.

The benefits of monetary and financial integration are no more in dispute as they are widely accepted. Agu (1992) identified these to include among others, expanded aggregate investment; improved resource allocation; increased domestic savings; enhanced financial intermediation; and greater international trade. Financial integration also serves as a stabilizer for common currency. It saves international reserves by providing alternative choices between foreign and domestic goods, services, and assets. This is not to suggest that there would be no cost to the participating

countries. However, the question is whether countries with highly protected economies will find the costs of monetary and financial integration acceptable.

These integration costs would basically from the constraints such integration impose on the pursuit of member's own national financial, monetary, and exchange rate policies. While the potential benefits from such integration generally take considerable time to be realized, the costs are immediate. Similarly, in the short-term, these benefits will not accrue to all participants in equal measure within the same time frame. However, in the long the benefits will be spread more evenly. These in part explain why members of various trade groupings in the developing countries and, indeed, in the industrialized world have been unwilling to move towards monetary and financial integration e.g. Britain.

### **Historical Background to Single Currency in West Africa**

From the historical point of view, several attempts had been made to establish economic integration in West Africa. This is evidenced particularly with the Francophone countries which had established strong economic and cultural ties with their French colonial masters whereby many aspects of the previous systems have been maintained. At independence in 1959, the countries comprising what had been the French West Africa Federation, that is all former French colonies in West Africa with the exception of Guinea, were still anxious to cooperate. This led to an agreement to form immediately, the West African Customs Union (UDAO), consisting of Dahomey, (now Benin), Togo, Ivory Coast, Mauritania, Niger, Senegal, Sudan (now Mali) and Upper Volta. Their achievements were minimal, however. As a result of the difficulties experienced in operating it, the Union was modified in 1966 to be less ambitious.

The name was also slightly modified to the Customs Union of West African States (UDEAO). After the collapse of UDEAO, the group was reshaped in 1970 to embrace twelve Francophone and Anglophone countries as the Economic Community of West Africa (CEAO). However, the formal Treaty was delayed and did not come into effect until January 1974. The major achievement of this community has been in the monetary area, a common currency (CFA Franc) being accepted for use all the community member states except Mali. There has been no example of significant cooperation in industrial or other spheres of activity, nor any significant increase in trade among the constituent countries.

A number of efforts aimed at linking smaller groups of states within the region have been made since the late 1950's. Ghana and Guinea formed a customs union in 1958, which was joined by Mali in 1964. The union survived with minimal achievement until 1963. Ghana also linked up with Upper Volta in 1960. Another attempt also includes Gambia and Senegal for the Gambia and Senegalese Economic Integration and a West Africa Free Trade Area comprising Ivory Coast, Guinea, Liberia and Sierra Leone. One of the more significant developments has been the council of Understanding (Conseil de L'entente) formed in 1959 between the Ivory Coast, Upper Volta, Niger and the Republic of Benin. It was joined in 1966 by Togo. This Council was mainly political but economic aims were included. There is a customs union and provision for some pooling of funds with elements of redistribution towards its poorer members. Achievements, unfortunately, have been minimal.

More limited attempts at cooperation have been between Sierra Leone and Liberia and between Senegal and The Gambia. In 1973, Sierra Leone and Liberia came together to form a common market, the Mano River Union. This was expanded substantially in 1980 by the addition of

Guinea.

The possibility of an Association between Senegal and The Gambia has been discussed for many years. The reason must seem obvious from the map. The two people of these countries are not ethnically distinctive, and the frontiers of The Gambia are quite arbitrary in relation to natural and economic features. However, in December 1981, the Sene-Gambia Confederation Agreement was signed. The Agreement, which did not detract from the separate existence of the two countries, was almost entirely concerned with formalities. The only reference to economics was the statement that the Confederation shall be based on development of an economic and monetary union. The content of that decision remains to be negotiated.

Major difficulties in the way of an economic union of these two countries were the different price and wage level of customs tariff. An attempt at harmonization would be likely to have a radical effect in raising prices in the Gambia. In particular, the different tariff levels create difficulties. The Gambia had low import duties, so that any move to raise them towards the level of Senegal's external duties would increase cost in prices to the Gambia. These are enough reasons (with separate and additional problems) for expecting the development of an economic and monetary union to be a slow process and to require a good deal in the way of compensatory arrangements if the Gambia was not to suffer heavy losses. However, the formation in 1975 of the Economic Community of West African States (ECOWAS), embracing all the 16 states in West African region, was the climax of these series of earlier effort to bring about closer economic cooperation among West African States.

#### **United Nations Contribution**

By the mid 1960s, the United Nations, through UNCTAD and the Economic Commission for

Africa began to throw its weight behind major regional integration efforts. Plans were evolved for four major Regional Economic Communities in Africa. These included the Eastern African Community, the Central African Community, and the Northern African Community. The fourth was to encompass the states of West Africa that now form the ECOWAS.

The initial step towards the formation of ECOWAS was taken at a conference on Industrial Coordination in West Africa held in Bamako, Mali in 1964. This was consolidated with a further conference on the same theme held in Niamey, Niger in 1966. At this conference, Articles of Association for the proposed community were drawn up. Although the relevant governments did not immediately sign these articles, an Interim Council of Ministers was set up. Nevertheless, further meetings in Dakar and Monrovia did not advance progress significantly towards the launching of the community, and it required further initiatives in the early 1970s by Nigeria and Togo, with the support of ECA to produce new momentum, culminating in the signing of ECOWAS Treaty in May 1975 in Lagos, Nigeria. In furtherance of the aim of the United Nations proposal for economic integration in West Africa, another meeting was convened in 1978 through UNCTAD on Economic Cooperation among developing countries on the theme: Trade Expansion and Regional Economic Integration among Developing Countries. This was held at Palais de Nations, Geneva from 10<sup>th</sup> to 18<sup>th</sup> April. Primarily the meeting was to assess progress made by the regional groupings thereby to fulfill the objective of the new international economic order. Wide ranging discussions were held and several activities were outlined and covered. Among these were preferential trade; state trading operations, monetary and financial cooperation; development of infrastructure, transport, and communication; restructuring and programming of industries, fiscal and balance of payment matters; training and educational facilities; establishment of joint

industrial enterprises; expansion of cultural contacts; treatment of foreign investment; transfer of technology, and preferential measures in favour of least developed countries.

#### **Institution of the Economic Order of West African States**

After the 1978 conference, member states of ECOWAS threw more weight on their efforts to catch up with the new international economic order. Nine major institutions were set up and these include:

- The Authority of Heads of States and Nations.
- The Council of Ministers.
- The Secretariat of the Community.
- The Industry, Agriculture, and Natural Resource Commission.
- The Transport, Telecommunications, and Energy Commission.
- The Trade, Customs, Immigration, and Monetary and Payment Commission.
- The Social and Cultural Affairs Commission.
- The Fund for Cooperation, Compensation, and Development (commonly called the ECOWAS Fund).
- The Tribunal of the Community.

These nine institutions had their broad and specified mandates. For the purpose of this study, I shall limit my examination of these mandates to the trade, Customs Immigration, Monetary, and Payment Commission.

#### **The Mandate of the Trade, Customs, Immigration, and Monetary and Payment Commission**

This Commission was mandated to initiate proposals for trade liberalization; mobility of factors of production; and facilitate monetary and trade payment within the region. When it went into operations, the West African Clearing House

was set up with the following objectives:

- To promote the use of the currencies of countries of member central banks for sub-regional trade and other transactions.
- To bring about savings in the use of the foreign reserves of the members.
- To encourage members of the Clearing House to liberalize trade among themselves.
- To promote monetary cooperation and consultations in the region.

Its main operation is to encourage member states to use their national currencies in payment for goods and services among member states through their central banks without the need for conversion into foreign currencies. An economic operator (individual or institution) wishing to settle a transaction through the WACH mechanism, will contact his commercial bank and give the necessary transfer instructions. The commercial banks having ensured that the particular transaction is eligible for treatment through WACH, pass the payment order to their central banks. The central banks then would advise the central bank of the country of the beneficiary who will then effect settlement in local currency on behalf of the exporter through his commercial bank.

This mechanism will spare the importer the problem of obtaining foreign currencies to finance its imports while the counterpart exporter would receive payment for his export in his local currency. However, the smooth operation of this mechanism requires an agreed means of exchange arrangements.

#### **The Introduction of West African Unit of Account (WAUA)**

In order to simplify the exchange arrangement, involving the existence of multiple currencies in the sub region and to ensure an efficient clearing mechanism, West African Units of Account

(WAUA) was introduced and linked to the SDR of the IMF. The WAUA would serve as the numeric for determining the relative strength of the currencies in the sub region.

Its operations were however faced with serious problems. At its inception, the record level of US\$ 291.2 million in volume of transaction consistently declined to US\$6.8 million by the end of 2002. This particular decline was due to the low level of intra-ECOWAS trade, owing to the slow pace of industrialization, lack of complimentary in production; lack of trade information; the existence of trade barriers; and instability in the exchange rate of national currencies.

#### **West African Monetary Agency (WAMA)**

In spite of the setbacks outlined above another milestone was taken in 1993. On May 28, 1993, a draft protocol relating to WAMA was adopted in Cotonou by governors of central banks of member states. This abolished the WACH (West African Clearing House) and brought into existence WAMA. Broader objectives were however mandated to this agency including those of WACH which were:

1. To facilitate the harmonization and coordination of monetary and fiscal policies and structural adjustment programmes of the member states.
2. To ensure the coordination and implementation of the ECOWAS Monetary Cooperation Programme.
3. To encourage the pursuit by member states of appropriate macro-economic policies conducive to market determined exchange and interest rates for intra-regional trade.
4. To initiate and promote policies and programmes on monetary integration within the region.

5. To ensure the establishment of a single monetary zone.

In continuation of WACH programmes with the West African Clearing mechanism, this agency was able, in 1998, to launch the ECOWAS Travelers Cheques Scheme. The ECOWAS travelers cheque was also denominated in the West African Unit of Accounts. The main objective was facilitating intra-ECOWAS travel (tourism) and commercial transaction and eliminating the use of foreign currencies for these types of transactions.

It was expected that this instrument would assist member countries to conserve scarce foreign exchange and limit the carriage and use of physical domestic currency notes across borders with all the accompanying risks.

However, statistics on the operations of the system indicated a less than satisfactory performance.

Whereas it had been envisaged upon introduction that about US\$448.5 million worth of cheques would be utilized within the first years of its operation, the actual total value of cheques encashed by the central banks throughout the sub region since the inception of the concept up to the end of March 2003 was only US\$40.3 million. A research study commissioned by WAMA revealed that the cheque operation was beset by a number of problems among which were:

1. Low levels of acceptability by the general public and business concerns due to inadequate sensitization in the member countries.
2. Reluctance of some banking institutions to encash the instruments.
3. Refusals of some financial institutions to quote exchange rates in relation to the WAUA.

4. Delays in the processing of documents for final settlements of balances.
5. Speculative dealings in the instruments in certain countries.

Nonetheless, WAMA could not relent in its strive to pursue the objective of reaching a single currency in the sub region. Mechanisms were put in place and the ECOWAS Monetary Cooperation Programme (EMCP) was launched whose objective was the establishment of a single monetary zone and a common currency for the ECOWAS territory through the adoption by member countries of policy measures with a view to harmonizing those monetary policies and ensuring convergence of the various national economies.

#### Measures for the Smooth Operation of EMCP

A number of measures were recommended in order to guarantee the smooth implementation of the EMCP, particularly in the areas of exchange rate, fiscal and monetary policy. Among the measures are:

1. Harmonize exchange rate regulations legislations and banking surveillance and adoption of market-determined exchange rate regime and an ECOWAS exchange rate mechanism.
2. Harmonize economic and financial statistics design and implement adjustment programmes to ensure compatibility with the sub-regional objectives.
3. Harmonize fiscal, monetary, and financial policies (especially capital and credits as well as domestic taxation systems) and liberalize the money, capital and labour.

markets

4. Establish an effective community market through trade liberalization, remove tariff and non-tariff barriers and integrate the capital markets through the establishment of regional stock exchanges.
5. Popularize the use of West African Units of Accounts (WAUA) and revitalize the sub regional clearing operations.
6. Comply with prescribed macro-economic convergence criteria.

The ECOWAS Monetary Cooperation Programme is classified into three main aspects:

- The macroeconomic convergence requirement
- The ECOWAS Multilateral surveillance mechanism
- The ECOWAS exchange rate mechanism.

These three aspects of the EMCP were seen as bold or giant strides taken to ensure compliance through member states in order to reach the objective of single monetary zone.

#### **Macroeconomic Convergence**

This is a core issue under the ECOWAS Monetary Integration Programme. Without convergence, policy coordination would be extremely difficult. This would certainly threaten the macro economic stability of the union and undermine the purchasing power of the common currency being envisaged. In pursuance of this convergence, certain indicators known as convergence criteria were adopted to evaluate economic performance of member countries.

The convergence criteria focus on price stability, prudent fiscal policies, restrictive budget deficit financing, and maintenance of adequate gross foreign reserves. These include:

1. Budget Deficit/GDP ratio (excluding grants) should be less than or equal to 4%.
2. Inflation rate should be less than or equal to 5%.
3. Central Bank financing of budget deficit should be less than or equal to 10% of previous year's tax revenue.
4. Gross external reserves should be greater than or equal to six months of import cover.

#### **Explanatory Notes on the Convergence Criteria**

The above convergence criteria are very important because only member states that have met them would be able to join the zone. The introduction of the single currency in West Africa is intended to foster economic development and growth. The fundamental requirement is for member countries to achieve some degree of convergence in macro-economic policies. The level of convergence required to be attained can be measure by the following criteria:

- **Price Stability:** Every country should make an effort to maintain stable prices by reducing its level of inflation to below 10% by the end of 2000 and 5% or below by 2002.
- **Budgetary Discipline:** All the countries are required to maintain budgetary discipline by reducing the budget deficit. The level of budgetary discipline is measured on the basis of maintaining the

annual budgetary deficit at or below a ratio of 5% of the GDP by 2000 and by 4% by 2002.

**Reduced Inflationary Financing:** In order to ensure stability in prices and the exchange rate, all the countries are expected to reduce their dependency on credit from their central banks to a sustainable non-inflationary level. Hence,

- central bank credit to the government to finance its budget deficit has been minimized to a ceiling of 10% of the previous year's fiscal receipts.
- **Health Reserve Position:** To ensure the maintenance of a minimum foreign exchange reserves position that will support average level of imports, every country is required to maintain a ratio of reserves to import cover the three months by the end of 2000 and six months by 2003.

#### Policy Instruments for the Convergence Criteria

In order to reinforce the above convergence criteria, certain policy instruments were put in place to ensure strict compliance by member states. These policy instruments were regarded as secondary criteria and they include:

- No accumulation of domestic arrears and liquidation of all outstanding debts.
- Tax receipt/GDP ratio should be greater than or equal to 20% (at least 20%).
- Salary mass/total tax receipt ratio should be less than or equal to 35% (at most %).
- Public investment finance from internal resource/tax receipt ratio should be greater

than or equal to 20% (at least 20%).

- Positive real interest rate.

Assessment of the performance of the member countries as at the end of 2002 in meeting the above criteria revealed that it was inadequate to support the launching of monetary union by 2004. No single country had been able to achieve the entire set of targets, or even had been able to sustain those achieved in previous years. In fact, the overall performance in 2002 deteriorated in comparison with the achievement in previous years.

#### Advantages of a Single Currency Unification

The regional economies of countries in the zone as well as its citizen will benefit in the following ways from the introduction of the single currency:

- **Regional Economy:** It will promote zonal market for trade and investments and thereby enhance regional economic integration for sustainable growth and development.
- **Covenant:** Government of member countries to maintain price stability and reduce inflationary trend and good foreign exchange reserve positions.
- **Workers:** The purchasing power of workers' wages will improve with a strong and stable currency that is convertible and acceptable throughout West Africa. Easy accessibility and provision of goods and services to other countries.
- **Business:** Prices to be quoted will be in known currency with no exchange admission or fees. The acquisition of foreign exchange will not be needed in the

sub region. It will also encourage trade liberalization and confidence building among the economies of member states. Traveler's acquisition of foreign exchange for intra regional travels will not be required. Commission or exchange fees will also not be paid. There will also be no need for the application of basic travelling allowance for trips within the sub-region.

### **Disadvantages of Joining a Single Currency**

The major disadvantage of joining a single monetary zone is the ceding of sovereignty over monetary policy to a super-national monetary authority or a common central bank. By so doing, national economies will lose the discretion and independence in the application of monetary policy for domestic economic management.

The consensus process by which member states agree on the monetary decisions could be another problem if it not structured properly because there will always be the tendency for the bigger economies like Nigeria, Ghana to influence decision that may not be in the best interest of other member states.

### **How Does The Introduction Of Single Currency Benefit Trade In The Region?**

Paul Mason and Catherine Pattillo agree that the benefit of a monetary union tend to be greater if the countries concerned already have a substantial amount of trade among themselves. Since transaction cost and bilateral exchange rate transactions related to that trade will be reduced. The more asymmetric and large the policy facing the countries, the greater is the cost of a fixed rate. This increases the attraction of retaining an independent monetary and exchange rate policy. Countries are less likely to face large asymmetric terms of trade policy if they have diversified economies with similar strategies. For instance, a country that exports oil and imports mainly manu-

factured goods is likely to experience different movements in its term of trade than a country exporting cocoa and importing oil.

These policies will be less of a problem if there is substantial labour mobility or there exist a system of fiscal transfer across the region. The source of shocks especially for countries whose exports are primary commodities is the term of trade. First there are very large movements of the terms of trade for several of the countries. The amplitude of the swings is especially large for Nigeria because of changes in the world price of oil, Nigeria's major export.

Secondly, these shocks to the terms of trade are typically not well correlative in large parts to the different commodities that are exported and the fact that the world prices of the different commodities are common to a number of countries in the region like cocoa, etc. Others are found only in one or two countries such as bauxite in Guinea and phosphate in Senegal and Togo. Countries like Nigeria, Guinea, Niger and Guinea-Bissau are each dependent on a single commodity for 50 percent or more of their net export earnings. The different primary commodities exported by the ECOWAS countries do not lead to a correlation in their terms of trade because while one country will be enjoying a favourable swing on the world market leading to unfavourable terms of trade the other would experience exactly the opposite effects.

Thirdly, the correlation tend to be higher for the WAEMU countries among themselves than either the correlation of WAEMU with non-WAEMU countries or the correlation among non-WAEMU countries. Hard data on labour mobility is high between some countries of the region because of traditional migration and trading patterns that cut across national boundaries. In this light, the Ivory Coast has the largest proportion of resident foreigners, which stand at 16 percent followed by the Gambia (14%) and Guinea (8%). ECOWAS has tried in this light by eliminating visa requirements

in order to have free mobility of labour, but some citizens facing residency in another country still face difficulties.

### **Fiscal Transfer**

Normally, federal or voluntary states that constitute monetary union have a mechanism that helps to absorb the various shocks hitting the different regions. In Europe, the absence of such a mechanism was viewed as a considerable drawback and a "Cohesion Fund" was quickly set up that was designed to subsidize poorer regions. The six non-WAEMU countries have also announced their intention to set up a Standardization and Corporation Fund to make temporary transfers among the converging economies of the monetary union. It has however not been set up yet but it will have an initial amount of \$100m. It will become operative once 75% of the fund has been raised. The success of such a fund however will depend on countries paying their dues and the commitment of each member country to help its neighbours during time of adverse terms of trade.

### **Currency Unification and Trade**

The effect of a common currency on trade is an important issue. The increase in trade stemming from a common currency is one of the few undisputed gains from the European Monetary Union (EMU). Even European Monetary Union skeptics, such as Feldstein (1997), agree that substituting a single currency for several national currencies reduces the transactions cost of trade within that group of countries. Indeed, this was one of the official motivations behind the EMU project (European Commission, 1990). Clearly, it is cheaper to trade between two countries that use the same currency than between countries with their own monies. The question may be asked: Does Monetary Union affect trade and output? A leading professor in this field, John C. Anyaneuce, using the work by Andrew K. Rose "Estimating the effect of Common Currencies on Trade" and

backed by notable scholar like Hall and Jones provided theoretical and empirical support to answer this question.

There are two optical currency area properties that are in assessing the net benefit from currency unions: their degree of openness, the extent of reciprocal trade among group of partner countries), and their correlation of incomes (capturing over time diverse other properties) Frankel, 1999). The postulation is that countries sharing a high level of either openness or income correlation, but preferably both properties, will find it beneficial to share a single currency. It is generally agreed that reciprocal trade and openness increase among countries sharing a single currency and a common monetary policy in response to a decline in transportation costs and a more stable exchange rate regime. However, there is lack of consensus regarding the extent by which income correlation rises or falls following monetary integration and the effective increase in reciprocal trade. What have emerged are two opposite paradigms: the "Krugman specialization hypothesis", and the "Endogeneity of OCA hypothesis".

### **The Model and Data**

This section links together bodies of research that had been published recently. The first is the effect of monetary union on trade in which we show that members of a monetary union systematically engage in more international trade. We use the augmented "gravity" model as our framework. In particular, we ask whether bilateral trade between West African countries is higher if both use the same currency, holding constant a variety of other determinants of international trade. The second relevant area concerns the subject of monetary union and growth, relying on the augmented endogenous growth framework. The underlying convergence hypothesis in the growth literature dictates that income at the end of a period depends on income at the beginning of the period, with a tendency to regress gradually towards

some long-run steady state. Convergence is conditional if it is only present after conditioning on variables such as factor accumulation. The Research Division of the West African Development Bank supplied the data set used to implement the estimations.

### **The Trade Equation**

We use the "augmented gravity model" of Rose (1999): see also Frankel and Rose, 2000; Alesina, Barro, and Tenreyro, 2002) to estimate the effects of monetary union on trade. The model is "augmented" in that the "standard gravity model" only includes income and distance variables. According to this model, export from one country to another country are explained by their economic sizes (GDP) or GNP, population, or per capita income), direct geographical distances and a set of dummies incorporating some kind of institutional characteristics common to specific flows. A high level of income in the exporting country indicates a high level of production, which increases the availability of goods for exports. A high level of income in the importing country suggests higher imports. Thus, using GDP as one of the determinants to the potential foreign trade is straightforward. All things being equal, a larger GDP in one country must create a larger demand for imports and a larger GDP in countries that creates a larger supply for exports to total production.

With regard to population size, several studies show that it proxies that physical size of the economy and the population has a negative effect on the openness ratio. This is justified by the fact that a larger country enjoys greater self-sufficiency under the assumption of economies of scale and larger natural resources endowments. However, the coefficient estimates for population of the exporter/importer may be positive or negative, depending on whether the country exports/imports less when it is big (absorption effect) or whether a big country exports/imports more than a small country (economies of scale).

Tastes for imported goods (presumed to be luxuries) rise with per capita incomes, hence an unexpected positive effect of per capita incomes in the importing country. A positive finding for exporter per capital incomes, assumes that per capita income is a proxy for capital intensity, with a positive coefficient suggesting that the class of goods exported was relatively capital intensive. It is common to expand the basic gravity model by adding other variables. For instance, variables are added to control for common language, common border, common colonial history, common currency, land lockedness and insularity. Usually, these variables are introduced as dummies in the gravity equation (International Trade Centre, UNCTAD/WTO (2003).

### **Multilateral Surveillance Mechanism**

This aspect of ECOWAS Monetary Cooperation Programme (EMCP) involves continuous monitoring of the economic and financial policies of member states to ensure the achievement of the closest coordination and convergence of the national economies.

The West Africa Monetary Agency (WAMA), an autonomous body of ECOWAS has the overall responsibility for the multilateral surveillance. It is charged with coordinating the activities of the sub region with the objective of creating the synergy and cooperation required to move the process of integration forward.

WAMA undertakes this responsibility by disseminating half-yearly questionnaires on member central banks that serves as the main source of its data and information requirements. It also undertakes periodic missions to member countries where pertinent issues relating to macro-economic policy and compliance with the convergence criteria are discussed with central bank officials and governmental agencies responsible for monetary integration in the various countries.

## The ECOWAS Exchange Rate Mechanism (EERM)

This is an operation framework that has been designed to help monitor and manage the developments in exchange rates of the various national currencies. The relevant technical documents have been finalized but are yet to be implemented due to the absence of certain prerequisite such as:

- 7 Adopting a convertibility agreement of national currencies of ECOWAS member countries.
- 7 Lifting all forms of restrictions on current and capital transaction between member states.
- 7 Abolishing restrictions on the use of material currencies in intra regional trade.

Notwithstanding the various economic obstacles so far encountered, the implement (WAMA) still saw the need for the introduction of a single currency and common monetary policy in West Africa, as the prospects are very bright. In the first place, the existence of the CFA Franc monetary zone serves as a model for the second monetary zone for the other countries in the sub region. The fast track approach has also given a big push to the integration process, and more than ever before, ECOWAS member countries had become increasingly aware of the need and benefits of monetary and economic integration. In effect, all ECOWAS countries are forging ahead in adjusting their economies to meet the stringent economic convergence criteria, despite the numerous setbacks. We hope that the aim and objectives envisaged by the Heads of States and Nations of the region will be achieved in due course.

## Conclusion

It is indeed necessary for a single currency and common monetary policy zone in West Africa as

an aid to prosperity and economic growth in the sub-region. But one should stop short and think of the road to its implementation.

Like the European Union which today have set up a single currency called euro; so many rivers were crossed and a lot of sacrifice and effort were ushered to achieve the common monetary zone in Europe. Some of these efforts were not evidence in West Africa. For instance must intra-regional trade is not in existence in the region. The question of abolishing trade barriers that are diversified would cause some member states to suffer because much of their source of revenue comes from these areas when little or no intra-regional trade exists. Considering also the lack of political will which is lacking in the region, creates a serious bottleneck in the road to the achievement of such a noble venture. Above all, the implementation of the programme is faced with a heavy competition by the IMF and World Bank whose support is found to be contrary with the implementation policies of the intended regional integration. These policies always supersede the regional policies; as a result, targets set by regional groupings are always at variance with actual result obtained at end periods.

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