

Chapter VII.

RELATIONS WITH THE REST OF THE WORLD

7.1 INDEPENDENT CURRENCIES AND CURRENCY AREAS

In discussing central banking in the context of the domestic credit market and the economic system, relations with the rest of the world were deliberately set aside for later consideration. Having defined the monetary functions of African central banks, we turned first to their dealings with the economic agents collectively known as the Banking System and the Public Administration, and then looked at what central banks can do for development, through the mobilization of savings, the enlargement of capital markets and the deliberate use of inflation.

There is yet a third sector, dealings with which give rise, in counterpart, to monetary base creation or destruction. This is the Foreign Sector. The central bank regards variations in the accounts with other countries as exogenous, because it cannot act upon them directly. Subject to government authorization, it can merely regulate some transactions (exchange controls, restrictions on imports or capital movements, etc.) or contract in its own name either to raise foreign exchange abroad (deficit position) or to place foreign exchange surpluses on international markets (surplus position).

There are, of course, a great many commercial and financial operations involving the rest of the world. In this respect Africa has

no problems differing substantially from those of other developing countries. What is peculiar though by no means exclusive to Africa, is that so many national currencies belong to some currency area or zone. If they do, this conditions foreign economic relations and up to a point determines the manner in which deficits are financed and surpluses invested. It is an interesting point that in spite of the different philosophies underlying the systems linked to the French franc and to sterling¹, recent developments and those predictable for the future suggest a very noticeable rapprochement between the two, and also between them and the countries whose currencies are independent.

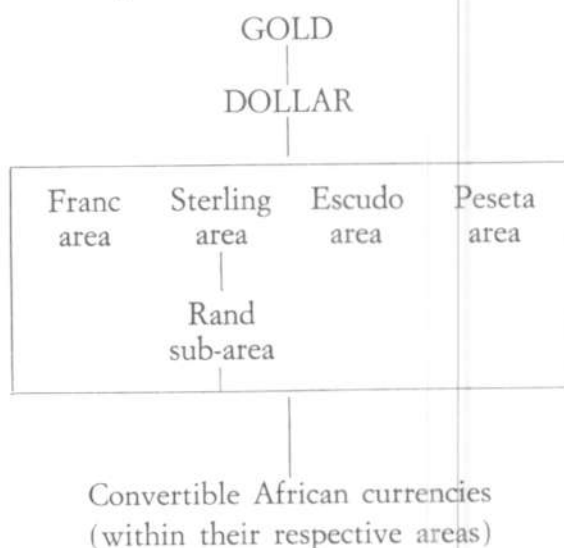
All African countries are members of the International Monetary Fund, and hence each had to declare the par value of its currency² in terms of gold. Recent monetary events, however, brought down the pillars upon which the Bretton Woods system rested, and the shape of things to come is not yet clear. The demonetization of gold (August 1971) and the adoption of flexible exchange rates (early months of 1973) abolished the stable reference points of the gold exchange standard.

¹ In terms so concise as to risk oversimplification, as the author himself warns, Robert A. Mundell (*African Trade, Politics and Money*, UN Economic Commission for Africa, January 1971, p. 48-49) writes: "The stress in France has been on Aristotelian automaticity; in England on Platonic-Keynesian management. These traditions have influenced the monetary philosophies of the former French and British systems in Africa. The French tradition has stressed the passive nature of monetary policy and the importance of exchange stability with convertibility (within the franc area); stability has been achieved at the expense of institutional development and monetary experience. The British countries by opting for monetary independence have sacrificed stability, but gained experience and better developed monetary institutions."

² For a full and up-to-date review of currency developments in all countries see Pick's *Currency Yearbook*, New York, various years.

The repercussions of the monetary crises which followed each other ever since sterling was devalued in November 1967 were profound — not only for the Western countries which caused them, but for all developing countries too and especially for those in Africa, so many of which have monetary links with Europe.

Prior to these events, the African payments system was as illustrated in the diagram below.



In addition, of course, there were the non-convertible African currencies.

It will be recalled from Chapter One that there are in Africa countries whose currency is independent and others which belong to some currency area. The distinction coincides with that between convertible and non-convertible currencies. Apart from the unique case of Liberia, which uses the US dollar¹, all the other countries

¹ Even there plans are afoot for setting up a central bank, which is to issue its own money tokens.

not belonging to any currency area have non-convertible currencies and practise exchange control, more or less strict according to the volume of reserves at hand. For these countries the only way of making payments to the rest of the world is the prior accumulation of international monetary means¹.

For the countries belonging to a currency area, the mechanism of convertibility used to rest on an absolute, though limited, guarantee by the European key-currency country (in the case of Great Britain the system was less clearly defined), which in its turn defended the value of its currency in terms of dollars and, through the latter, in terms of gold. In other words, gold was the ultimate reserve asset into which, at the fixed price of \$ 35 per ounce, the dollar holdings of the central banks of France, Great Britain, Portugal and Spain were fully convertible. The link of these nations' currencies with the dollar was their strength. And to these strongpoints the African currencies in their turn were anchored, again at a fixed rate of exchange. Payments within any currency area were made in the latter's key currency, those abroad in whatever currency the payee chose (usually one of those most common in international trade), the required sums being furnished by the European country concerned.

I have deliberately used the past in speaking of these matters, because recent events have somewhat altered the situation. Internationally, dollar-gold convertibility no longer works, and non-dollar key currencies are converted into dollars at rates quoted daily on exchange markets — where, incidentally, intervention by monetary authorities is a common occurrence.

¹ See the classification suggested by Jacques Alibert, "L'Afrique dans le système monétaire international", *Europe-France-Outremer*, December 1969.

The third kind of convertibility, of African currencies into their respective key currencies and *vice versa*, does not work in the same way in all currency areas¹.

The franc zone still exists, but pressure from some African countries and more general aspirations of independence have led to major changes, and even those are regarded mainly as a sort of halfway house pending further revisions.

The sterling area, on the other hand, has virtually ceased to exist. It never recovered from the devaluation of sterling in November 1967, and when the pound was set afloat in June 1972, this was the end. Its fortunes, and those of the franc zone, will be described in more detail in the next two sections.

The escudo and the peseta systems are still as described in Chapter One, though the former is bound to change by agreement with Portugal, now that Angola, Mozambique and Guinea Bissau are obtaining their political independence.

Generally speaking, things have been moving in the direction of African countries disengaging from their former colonial rulers, in monetary as in other matters. In the case of sterling, the process was accelerated by the persistent weakness of the British economy and by Britain's inevitable loss of importance in the world at large, after the empire fell apart; in the case of the French franc, on the other hand, the disintegrating element is the very working of the franc zone, which, along with undoubted advantages, has also brought disadvantages which ultimately prevailed.

But disengagement, followed by the adoption of non-convertible currencies, is no panacea. On the contrary, it may spell new

¹ Currency "area" and "zone" are terms which can be used indiscriminately. If one does want to make a distinction, "zone" should perhaps be reserved for those systems where the links are closer and the rules stricter, as in the French, the Portuguese and the Spanish "zones".

troubles for those countries which try to push development beyond the feasible, for they may well find that the external value of their currency becomes quite unsustainable, and then growth will not be promoted, but held back. But it certainly does mean that the country concerned assumes more direct responsibility for its own affairs, including the management of its own accounts with the rest of the world; mistakes will be made, no doubt, yet there remains the gain of more far-reaching freedom of decision.

7.2 THE FRANC ZONE

The franc zone, its history, characteristics and working have been described by many authors, some dwelling more on the good aspects and some on the bad¹. Recently, the debate has penetrated into the very councils of those responsible for the franc zone, and as a result changes of some importance were introduced.

Essentially, the franc zone works on four principles:

- (a) convertibility of currencies within the zone, via the French franc;
- (b) fixed exchange rate against the French franc;
- (c) pooling of foreign exchange reserves;
- (d) harmonization of measures in the monetary, foreign exchange and financial field.

Before looking at the main features of the system in detail, it may be well to recall that the franc zone is made up of three

¹ A useful bibliography up to 1965 will be found in Gaston Leduc, *Les institutions monétaires africaines: pays francophones*, *op. cit.*; see also IMF African Department, "The CFA Franc System", *IMF Staff Papers*, November 1963; Jan V. Mladek, "Evolution of African Currencies: The Franc Area", *IBRD-IMF Finance and Development*, September 1964; Bernard Hepp, *Monnaie et crédit en Afrique noire francophone*, *op. cit.*, p. 9-18.

In addition, reference is made to what has been said about the historical background in Chapter One.

different groups of countries (in addition, of course, to France, which is its centre).

First, there are the Overseas Departments (Guadeloupe, Martinique, French Guiana and La Réunion), which are an integral part of Metropolitan France and share a joint *Institut d'émission des Départements d'outremer*, which has its seat in Paris and is under French management¹. Very similar is the position of the French Overseas Territories². All these, either as colonies or as French territories, have no political independence, are directly under French jurisdiction and therefore obviously belong to the franc zone. One may well ask why indeed they have monetary institutions other than those of France. The reasons are of a historical, geographical and economic nature³.

¹ Although there is only one issuing institute, the currencies are different; those of the first three departments have the same value as the metropolitan franc, that of La Réunion has the parity of the CFA franc.

² In the Pacific (New Caledonia, French Polynesia, and the Wallis and Futuna Islands) the *Institut d'émission d'outremer* replaced the *Banque d'Indochine* as of 1 April 1967, and since then has been issuing the Pacific franc.

In St. Pierre et Miquelon, the CFA franc was recently replaced by the metropolitan franc; in the Comoro Archipelago, the CFA franc is still issued by the *Banque de Madagascar et des Comores*, a private commercial bank which, belying its name, does not have the issuing privilege for the Malagasy Republic.

The French Territory of the Afars and Issas, finally, does not belong to the franc zone at all. Its currency is the — non-convertible — Djibouti franc, which is not linked to the French franc.

³ "Il s'agit d'anciennes colonies où la Banque de France n'a jamais exercé le privilège d'émission; les nouveaux instituts y ont pris la suite des vieilles banques coloniales ou de la Banque d'Indochine, qui était tout à la fois banque d'émission et banque commerciale; le maintien d'instituts spéciaux est apparu comme souhaitable, parce que la structure économique et sociale des D.O.M. et des T.O.M. est très différente de celle de la France continentale, et parce que la politique de crédit doit être adaptée à ces conditions particulières. Mais toutes précautions sont prises pour que cette politique soit néanmoins coordonnée avec celle de la métropole." (P. Calvet, "Zone franc: évolution récente et perspectives d'avenir", *Banque*, February 1974, p. 112).

The second group is much the largest and consists of all those countries which keep a *compte d'opérations*, an operations account, with the French Treasury. This is the group of most interest in the context of this book since it includes the two monetary unions of West Africa (including Mali) and of Central Africa. Until May 1973, Madagascar belonged to it, too.

Finally, there are the countries which, while issuing their own independent and non-convertible currency, yet enjoy special co-operation arrangements with France, via the *comptes d'avances* with the Bank of France. This is the system of the three Maghreb countries which, strictly speaking, are not really part of the franc zone. It will nevertheless be discussed here, if only in order to bring out the differences between the two arrangements. In any event, there are those who hope that the franc zone in the narrower sense may be moving towards a compromise solution very similar to that of Morocco, Algeria and Tunisia.

All the changes that were made in the last few years were prompted by the desire to Africanize the processes of decision-making within the issuing institutes. But not all countries chose the same way. In November 1972 the states of Central Africa, and in November 1973 those of West Africa, proceeded to a critical revision of the statutes of their respective central banks and of their co-operation agreements with France, and obtained what they regarded as improved rules for the franc zone. Two other countries, on the other hand, felt their interests would be better served by withdrawing from the franc zone altogether, setting up a central bank of their own and adopting a non-convertible currency; Mauritania did so in November 1972 and Madagascar in May 1973.

The changes which the franc zone underwent in recent years will be mentioned, as occasion arises, under the following headings to be discussed separately below:

- (a) the mechanism of the operations accounts (i.e. convertibility, fixed exchange rates and freedom of capital transfers);
- (b) the pooling of reserves;
- (c) the decision-making organs;
- (d) the impact of membership in the franc zone on economic development in individual countries;
- (e) economic, financial and commercial co-operation with France;
- (f) the particular cases of Mali, Mauritania and Madagascar;
- (g) the Maghreb countries' system of *comptes d'avances*;
- (h) outlook for the future.

(a) *The mechanism of the operations accounts.* Under a special convention between France and a country, or group of countries, the French Treasury opens a special account, called *compte d'opérations*, in the name of the central bank concerned (at present, the *Banque Centrale des Etats de l'Afrique de l'Ouest*, the *Banque des Etats de l'Afrique Centrale*, and the *Banque Centrale du Mali*). This account works in a very simple way: it is debited for all foreign exchange payments to the rest of the world (chiefly for imports and outward capital transfers), and credited for all foreign exchange receipts (chiefly for exports, tourism and capital inflows).

Until the recent changes, which will be mentioned under (b), the central bank concerned had the obligation to pay into its operations account all its foreign exchange assets, and the right to draw on it, theoretically without limit, for any foreign exchange it needed. The balance of the operations account, therefore, represented the net consolidated balance-of-payments position of each of the two monetary unions.

The account is kept solely in French francs, which means that all other foreign exchange must first be converted into francs (at the day's price on the Paris exchange market) — or *vice versa*, if foreign exchange is needed for payments outside the franc zone.

At its fixed exchange rate, 1 CFA¹ franc is at present worth 0.002 French francs, and its convertibility is guaranteed by the latter — without limits, let us say for the moment. However, being the key currency, the French franc drags the satellite along in all its parity changes. Automatic adjustments thus occurred when the French franc was devalued in 1958 and in 1969, when a two-tier exchange market was introduced in France in August 1971 and then abolished again in the spring of 1974, and when the French franc dropped out of the EEC “snake”. This mechanism obviously has serious disadvantages for the African countries of the franc zone, both because in some cases there is no economic justification for following the vicissitudes of the franc, and because the franc reserves pooled at the French Treasury in lieu of foreign exchange assets lose purchasing power². Nothing has been done to remedy

¹ The initials CFA now stand, in Central Africa, for *Coopération Financière en Afrique*. But this is only since the recent reform. Curiously enough, the same initials in colonial times qualified the currencies concerned as *franc des Colonies Françaises Africaines*, and later as *franc de la Communauté Financière Africaine*. Is there any substance behind this change of words?

² With reference to the August 1969 devaluation, J.P. Sereni (“Le franc CFA en dix questions”, *Jeune Afrique*, 16 December 1972, p. 26) notes: “La situation de l'économie française en 1969 exigeait une dévaluation du franc; au contraire, celles des économies africaines n'exigeait pas une dévaluation du CFA. Pourtant, dans l'ensemble franco-africain, c'est la logique du plus fort, du plus riche aussi, qui l'a emporté aux dépens du plus faible, qui est, bien sûr, le plus pauvre.”

More generally, we find in Mamadou Diarra, *Les Etats africains et la garantie monétaire de la France*, Dakar 1972, p. 38: “Nous croyons que le fait d'imposer aux Etats africains la parité actuelle du franc CFA est, tout compte fait, plus préjudiciable que bénéfique à la plupart d'entre eux. Cette parité fixe, commune, qui ne repose pas, on le sait, sur leur potentiel économique respectif mais tient

the first evil, which means in effect inability to manage the external value of one's own currency; but the second has been removed. Under the latest agreements with France, entries in the operations account are now valued in terms of a unit of account based on gold, special drawing rights and the European unit of account. This means that holders of French francs will sustain no loss in case of devaluation, but that the nominal value of their assets will rise in proportion to the rate of devaluation¹.

In theory, the operations account may show either a credit balance or a debit balance. The first happens when the country, or group of countries, represented by any one of the central banks of the franc zone has a surplus on its balance of payments, meaning a net surplus *vis-à-vis* all other countries inside and outside the zone. The credit balance (consisting of French francs obtained either directly or via sale of other foreign currencies) carries interest at a rate equal, in the case of the BCEAO, to the arithmetic mean of the intervention rates of the Bank of France in the market for public securities during the current quarter, or, in the case of the BEAC, to the official discount rate of the Bank of France.

The important point to note in this connection is that, barring the permanent deficit position of Mali, the countries of West and

artificiellement à un lien juridique avec une monnaie étrangère, ne permet pas aux Etats les moins favorisés de profiter des avantages d'un taux de change plus approprié qui leur permettrait de développer d'autres ressources naturelles. Un tourisme de masse, et non de luxe, par exemple, leur procurerait en même temps les ressources en devises nécessaires à leur équipement."

¹ Holders of sterling balances enjoyed a similar guarantee after the devaluation of sterling in November 1967. However, this failed to produce any lasting readjustment, because since then sterling has never again been trusted as before, and at the end of 1974 the guarantee was abolished.

Parity changes (in a downward direction) of the key currency are the most blatant manifestation of the latter's lost capacity to function as the standard of a currency area.

Central Africa (as well as Madagascar before its withdrawal from the franc zone) were always in surplus, because in each group the surpluses of some countries exceeded the deficits of others. On the current account one item is French "aid", which, while of benefit to the recipients, certainly does no harm to the donor and indeed is one of the most efficacious means of keeping French-speaking Africa economically tied to Paris¹. Be that as it may, the fact remains that, at least according to the statistics of past years, there is a flow of hard currencies from the periphery to the centre, from the poor nations to the richest in the group. For France, this is of practical advantage only when its own overall balance of payments is in deficit.

The limitless guarantee of convertibility theoretically offered by the French franc has in fact never worked. This is probably no accident, but due to the rigid conduct of monetary affairs during the last ten years or so². Let us see what happens in case there should be a debit balance on the operations account. The rules are not quite the same, though very similar, for West and Central Africa³. While the BEAC has to take corrective measures when its account has shown a net debit balance for three consecutive months, the BCEAO has to do so as soon as foreign exchange reserves fall more than 20 per cent short of sight liabilities (i.e. the monetary circulation) on a quarterly average.

¹ In any case, "aid" is a form of resource transfer practised, in varying measure, also by other developed countries.

² Sereni (*op. cit.*, p. 28) rightly points out that "l'étendue de la garantie française sera proportionnelle au degré de contrôle que conservera le gouvernement français dans l'organisation de l'émission monétaire."

³ See Articles 5-7 of the *Convention de compte d'opérations* with the BCEAO, and Articles 4-6 of that with the BEAC.

In either case, the corrective measures are the following:

- (i) the central bank concerned has to pay into its operations account its permissible working balances in foreign exchange (which are limited to 35 per cent for the BCEAO and to 20 per cent for the BEAC - see under (b) below);
- (ii) it has to use its special drawing rights;
- (iii) it has to call in, against CFA francs, the French francs and other foreign exchange in public and private hands; the extent to which it does so depends on requirements, and the relevant instructions are primarily addressed to those countries in the group which have an external payments deficit.

It is only when the mobilization of all these funds still is not enough to wipe out the debit balance on the operations account that the French guarantee comes into play, limitless as it is on paper. Interest is payable on debit balances at the rate of 1 per cent for any amount up to 5 million French francs, of 2 per cent for the slice between 5 and 10 million, and at the discount rate of the Bank of France for amounts above 10 million.

It hardly needs stressing that the chance of permanent deficit positions is very remote indeed, if only because the statutes of both central banks explicitly require them to take "appropriate" corrective measures (by unanimous or qualified majority decision, which means a French veto right), which in all likelihood take the form of restrictive monetary policies.

The final question to consider is whether convertibility via the operations account has had beneficial effects on free capital transfers and foreign investment in the franc zone.

Freedom of capital transfers, of course, applies only within the zone (and even there some foreign exchange limitations were introduced in 1969), and not indiscriminately to all countries outside

it. Freedom of transfer, which implies freedom of subsequent repatriation, should attract a conspicuous volume of foreign capital to the countries of the franc zone. In practice this has not always happened, because other conditions, too, are necessary for bringing in capital from abroad; these include first and foremost a wealth of natural resources not so far exploited, and there are few countries in this fortunate position¹.

On the contrary, freedom of transfer has fostered a flow of capital from African countries to France, where interest rates were always higher, not least because of the cheap money policy of the two multinational central banks. Far from negligible amounts were thus placed in France by African citizens and by French expatriates, with all the harmful consequences of such a drain of resources².

¹ Comparing the position of French-speaking Africa with that of Brazil, Diarra (*ibid.*, p. 37) concludes: "Lorsque ces deux conditions sont réunies, à savoir l'existence de ressources naturelles à exploiter et l'intérêt et l'urgence que représente leur exploitation aux yeux des investisseurs, on peut même dire que peu importe alors qu'il y ait, ou non, inflation, qu'il y ait ou non contrôle des changes; ce qui prime c'est le besoin de faire des affaires en réalisant les investissements indispensables."

² See P. and S. Guillaumont, "Zone franc et développement: les différentes caractéristiques de la zone franc et leurs effets sur le développement sont-ils dissociables?", in: Tremblay, ed., *Africa and Monetary Integration*, Montreal 1972.

Rather bitter comments come from Kaïs, "Non à l'aventure individuelle", *Jeune Afrique*, 16 December 1972, p. 29: "Depuis 1962, avec des périodes de pointes et des accalmies (selon les vicissitudes politiques), un mouvement récurrent a systématiquement rapatrié 'à l'ombre', en France, le plus clair de l'épargne productive africaine. Il suffit d'analyser les rapports des banques centrales pour être en mesure d'affirmer que le marché financier parisien a largement récupéré les fonds dispensés à grand fracas publicitaire par l'aide publique française en Afrique.

Conclusion: la France n'est pas en réalité, comme l'affirme son gouvernement et le voudrait son président, le pays industrialisé le plus généreux envers le Tiers Monde. Le contraire est plus proche de la vérité et cela à cause de (ou grâce à) la zone franc."

(b) *The pooling of reserves.* The pooling of foreign exchange reserves is one of the major features of the franc zone. As has already been mentioned, these reserves must be held in French francs, even if receipts were in some other currency (which has to be converted into francs). Until the statutory reforms of November 1972 for Central Africa, and of November 1973 for West Africa, the rule was that 100 per cent of foreign assets must be so held; now this rule has been relaxed somewhat in order to give the countries concerned more freedom of decision in the management of their own reserves. The following exceptions are now allowed:

- (i) current working balances;
- (ii) the sums needed for meeting obligations to the International Monetary Fund;
- (iii) such other sums as the highest authorities of the two central banks decide to hold in currencies other than French francs, up to a maximum of 35 per cent of total reserves in the case of the BCEAO and of 20 per cent in that of the BEAC¹.

These assets may be invested in current accounts with other central banks or the Bank for International Settlements, or else in negotiable securities with two or more years to run, provided these are denominated in convertible currencies and issued by international organizations of which the African countries concerned are members.

After these reforms, there seems quite a lot to be said for this pool of reserves, which gives deficit countries in the franc zone access to foreign exchange without having to introduce severe

¹ The IMF gold quota and the allocation of special drawing rights are excluded from the computation.

restrictions in the short run¹ — though these do become necessary later, if the situation does not improve in the meantime. The pooling of reserves also makes for their more rational management; there are bound to be economies in their use in international trade, since the balances of individual countries will quite often cancel each other². For France this has meant around 10 per cent of its total reserves in recent years, not really enough to matter. The situation is strikingly different in the sterling area, whose members used to hold sterling balances far in excess of Britain's foreign reserves. It was these sterling balances which exercised such heavy pressure upon the pound in 1967 that it eventually had to be devalued. From this point of view, France always did much better.

(c) *The decision-making organs.* The reforms of 1972 and 1973 brought some considerable changes to the composition of the highest organs both of the BEAC and the West African Monetary Union. However, they were changes more of form than of substance, for while France now has fewer members in these

¹ This advantage is stressed by T.H. Pa'Uru, "L'Union Monétaire Ouest Africaine", *Banque*, September 1970, p. 750: "Pour de petits pays en voie de développement dont les recettes extérieures proviennent essentiellement de l'exportation sur des marchés souvent incertains de quelques productions, une seule parfois, le plus souvent agricoles et sujettes à de considérables variations de récolte, la mise en commun de leurs réserves de change donne assurément une meilleure base à leur monnaie. En fait, il a été possible à plusieurs pays de l'Union monétaire de continuer à financer leur activité économique sans restriction particulière de change et sans encadrement sévère de crédit, en dépit de la contraction et même de la disparition de leur participation au pool commun des réserves."

The same points are made in IMF African Department Study Group, "Financial Arrangements of Countries Using the CFA franc", *IMF Staff Papers*, July 1969.

² In 1969, the ratio of official reserves to imports was 41.8 for developing primary-producing countries, 20.9 for those of the West African Monetary Union, 17.6 for those of the Central African one, and 11.6 for Madagascar.

councils, it retains control over major decisions via the unanimity or qualified majority voting rule¹.

The *Banque des Etats de l'Afrique Centrale* is now governed by a 12-member Board of Directors, of whom four each sit for Cameroon and France, and 1 each for the other four member states (Central African Republic, Chad, Congo and Gabon). Previously, 14 out of 26 directors were French.

In the West African Monetary Union, the former Council has been replaced by two decision-making units: at the apex, the Conference of Heads of State takes unanimous decisions on all matters not resolved by the other group, the Council of Ministers of the Union, whose very considerable responsibilities are spelled out in Articles 6 to 13 of the constituent treaty². The Union's central bank itself, the BCEAO, continues to be governed by its Board of Directors, which now has two members each for the six African member states — Dahomey, Ivory Coast, Niger, Senegal, Togo and Upper Volta — and two for France. This means France now has one seventh of the membership as against one third earlier, but again it retains a veto right in certain decisions.

Even if this is only one step towards more independence, it still is an advance in this particular field too, and as such testifies

¹ What R.H. Green and A. Seidman wrote a few years ago (*Unity or Poverty? The Economics of Pan-Africanism*, Harmondsworth, Penguin, 1968) still holds: France has a voice in drafting African development plans and helps to finance them, and in effect controls monetary and credit policy via customs and trade agreements — and therefore still has a dominant influence on the direction of economic development in French-speaking Africa.

² Mamadou Diarra ("Un pas en avant, mais à quand le prochain?", *Le Monde*, 18 December 1973) rightly asks "s'il n'aurait pas été plus simple et moins lourd de prévoir la réunion à deux niveaux de l'ancien conseil, d'autant que le nouveau conseil des ministres de l'Union se voit confier des attributions qui empiètent singulièrement sur celles du conseil d'administration."

to the Africans' determination to assume responsibility for the management of their own joint institutions.

(d) *The impact of membership in the franc zone on economic development in individual countries.* Monetary policy in the countries of the franc zone has always been dominated by balance-of-payments equilibrium, or, in other words, by the maintenance of a non-negative balance on the operations account. There was no room, therefore, for inflationary deficit spending¹. From the strictly monetary point of view, this speaks well for a system based on French-African co-operation which, in the first ten post-independence years, kept the CFA franc enviably stable.

But the reverse of the medal is, of course, that credit to the economy and the state has always had to be rationed, in terms both of amounts and maturities. Often it was long-term productive investment expenditure which has had to mark time, which meant retarding the development process².

¹ See above, section 6.7.

Robert A. Mundell (*op. cit.*, p. 33) sums the system up as follows: "Balance of payments equilibrium is maintained by rigid financial discipline of the member countries, the governments of which are prevented from using the Central Bank as a source of inflationary finance. Government accounts must be balanced except insofar as the government has cash reserves at its disposal or can acquire extra credits from one of the common banks or from abroad.

The financial discipline has had the merit of inhibiting the French franc countries from piling up foreign debts but it has also led to complaints of an excessive monetary conservatism inhibiting economic development."

² For detailed discussion, see P. Guillaumont and S. Jeanneney, "Les instruments de la politique monétaire dans l'UMOA", *Annales africaines*, 1967; S. Amin, "Pour un aménagement du système monétaire des pays africains de la zone franc", *Le Mois en Afrique*, May 1969; J.P. Sereni, "A qui profite la zone franc?", *Jeune Afrique*, 12 October 1971. The last-named author protests, in provocative tones: "Agiter l'épouvantail des exemples guinéens ou maliens pour persuader du contraire les Africains n'est pas sérieux. Ce n'est pas parce que le Mali ou la Guinée ont recouvré leur indépendance monétaire qu'ils ont connu

In time, this unsatisfactory state of affairs came to be perceived more keenly and the first move to remedy it was a shift, from 1967 on, from the previous ultraconservative monetary policy to a more dynamic approach. More recently, amendments to the statutes of the BCEAO and the BEAC brought further improvements¹. Medium-term paper is now rediscounted by the BCEAO up to ten years, and by the BEAC up to seven years. The ceiling for central bank advances to local governments was raised to 20 per cent of the preceding year's fiscal revenue, thus helping them to cover their requirements for investment expenditure. Finally, a new regional development bank for West Africa was created, under the name of *Banque Ouest Africaine de Développement* (BOAD)². Its purpose is to promote balanced economic development in member states and to foster economic integration in its region³. Its initial capital of 2,400

une très forte inflation, mais parce que la politique économique choisie était erronée. C'est vrai que le système actuel interdit à ses membres de tels errements, mais cet avantage est payé trop cher."

¹ Actually, the situation was rather different in the two monetary unions. In the UMOA only the government of Dahomey drew heavily on central bank credit (within the permissible limits, of course), while in Central Africa all the states except Cameroon did so. P. and S. Guillaumont (*op. cit.*, p. 40) suggest that this difference "traduit peut-être le fait que les pays de l'UMOA, plus conscients de la solidarité qui les unit, sont plus soucieux d'équilibre monétaire."

² See the agreement of 14 November 1973, by which the bank was set up, as well as its statutes.

³ Article 2 of the BOAD statutes outlines its tasks as follows: "La Banque, directement ou par l'intermédiaire de filiales ou de fonds spéciaux constitués par elle ou d'institutions financières nationales, devra contribuer notamment:

1) à la collecte de disponibilités intérieures en conformité avec les législations nationales;

2) à la recherche de capitaux extérieurs par emprunts ou obtention de fonds de concours non remboursables;

3) au financement par participation au capital, par octroi de prêts, avals, bonifications d'intérêts, à des investissements ou activités ayant pour objet:

— la construction ou l'amélioration d'infrastructures nécessaires au développement,

million CFA francs was contributed in equal parts by the BCEAO and by the governments of the West African monetary union.

The BOAD is the second regional development bank in Africa, after the East African Development Bank. Its creation, together with the relaxation of credit regulations, is a clear expression of the need and urgency of channelling more long-term resources to development projects. Implicitly, it also reveals the shortcomings of the former rigid monetary management in this respect. Now, the new approach will have to be put into effect.

(e) *Economic, financial and commercial co-operation with France.* This, then, is what monetary co-operation with France means. In the financial and commercial, and more generally speaking the economic field, new developments came in the wake of the creation of the European Economic Community and the association with it of French-speaking Africa under the Yaoundé Convention¹.

In the broader view, a critical assessment of the franc zone must needs encompass also financial and commercial aspects. As regards the first, it is common knowledge that at present much the largest volume of aid comes from France directly, via the *Fonds*

- l'amélioration des conditions et moyens de production,
- l'établissement de nouvelles activités,
- le transfert de la propriété des moyens de production et de distribution des biens et services à des personnes morales ou privées ressortissant de l'Union ou de l'un de ses membres, ou à des personnes physiques nationales de l'Union;
- 4) à l'élaboration et à l'appréciation technique et financière des projets de développement et à la création et au fonctionnement des organismes chargés de leur exécution."

¹ "Si les relations avec la France restent les plus exclusives dans le domaine monétaire, c'est parce qu'en matière d'union monétaire l'intégration économique européenne est la moins avancée." (Guillaumont, *op. cit.*, p. 31). Later in the same paper (p. 31-52) the authors examine in some detail the various aspects of co-operation with France.

d'Aide et de Coopération, and from the EEC, via the European Development Fund (EDF)¹. This aid takes a variety of forms, like grants, contributions to the budget, technical assistance, fellowships for training and advanced courses, and cultural co-operation. With these funds the African countries concerned keep their external accounts in surplus and cover their budget deficits, which other countries do by printing money. To finance deficits by foreign exchange inflows rather than by inflation would certainly be preferable, if it did not inevitably entail foreign interference and thus keep recipient countries in a state of subordination. From this point of view, French aid remains subject to much the same reservations as apply to transfers from other industrial nations. Furthermore, French aid, while relatively large in terms of GNP, has the defect of concentration in the franc zone, where political influences can be exerted most readily.

Commercially speaking, there is no doubt that in colonial times the French monetary guarantee carried ample rewards in the shape of terms of trade favourable to France and of preferential trade flows. With the accession to independence and the association agreements with the EEC, trade arrangements became somewhat more equitable, though they are still far from optimal. Trade relations have been improving steadily for Africa, but there is always the danger that European countries and the United States may revert to protectionist practices in order to escape from the external payments difficulties due to the higher cost of oil.

(f) *The particular cases of Mali, Mauritania and Madagascar.*
Apart from Guinea, which broke its ties with the franc zone on

¹ For statistics and interpretation, see IMF African Department Study Group, "Financial Arrangements of Countries Using the CFA Franc", *op. cit.*, p. 374-87.

the morrow of independence because its people, in the words of President Sékou Touré, "préfère la liberté dans la pauvreté à l'opulence dans l'esclavage"¹, three other countries have to be mentioned separately, so as to explain their different choices in the monetary field.

First the case of Mali, whose position seems somewhat contradictory and not quite clear. When the West African Monetary Union was set up in 1962, Mali was a partner to the treaty, but subsequently refused to ratify it, and in that same year withdrew from the franc zone². But this monetary adventure, which lasted from 1962 to 1967, was a complete failure. It was part of a political and economic vision rather similar to that of Guinea, but unlike Guinea, Mali soon started negotiations with France which led to a devaluation of the Mali franc by 50 per cent and to a new special agreement for convertibility via an operations account. This agreement was signed in February 1967 and provided for a possible re-entry of Mali into the Union, once its monetary affairs were straightened out. But this has not happened, or at any rate not on the occasion of the revisions of November 1973. The reasons for this are unknown to me, though there must have

¹ Text of the proclamation published in the *Journal officiel de la République de Guinée*, 1 March 1960.

Mamadou Diarra, *Les Etats africains et la garantie monétaire de la France*, *op. cit.*, p. 44-53, gives a very good illustration of the failures of Guinea's monetary experience, and suggests possible explanations. In conclusion, the author asks: "Peut-on dire, d'après ce qui précède, que c'est le fait d'avoir voulu exercer sa souveraineté monétaire qui est la véritable cause des difficultés que connaît la Guinée? On ne peut ... sérieusement le prétendre. Ces difficultés ont été aggravées par l'absence de cadres nationaux préparés à prendre la direction d'opérations qui leur ont été confiées du jour au lendemain et, dans certains cas, par le manque évident d'esprit civique — toutes choses d'ailleurs auxquelles le régime colonial et ses méthodes ne sont pas étrangers."

² For details see Gaston Leduc, *op. cit.*, p. 241-51.

been some other than monetary; generally speaking, I am inclined to share Diarra's critical view¹.

Mauritania withdrew quite recently, in November 1972, both from the West African Monetary Union and from the franc zone, after ten years of common monetary management. The results, after the required six months' notice, were a new independent central bank and a non-convertible currency². Mauritania thus went in the opposite direction from Mali, and its motives, like those of Guinea, were the political ones of obtaining independence for an active policy of socialism³.

It is too soon to pass judgment on the results of the radical changes introduced, though the Mauritaniens are a sober people who, one may hope, will make prudent use of their increased

¹ "Le Mali se serait peut-être rendu compte qu'il n'avait le choix qu'entre deux solutions: ou se joindre à la Guinée pour mener leur expérience ensemble, ou demeurer avec les autres Etats au sein de l'Union monétaire — comme nous persistons à penser que la Guinée elle-même aurait dû le faire — pour servir d'élément moteur à une évolution rapide vers un système monétaire indépendant. C'est pourquoi la tentative malienne doit être jugée plus sévèrement, surtout dans la mesure où son échec, qui était prévisible, peut être pris — on ne manque pas déjà de le faire — comme un argument trop facile contre l'indépendance monétaire." (Diarra, *ibid.*, p. 54).

² See *Jeune Afrique*, "La Banque Centrale de Mauritanie", Interview with Ahmed Ould Daddah, Governor of the Central Bank of Mauritania, 13 October 1973, and M. Penouil, "La coopération monétaire en Afrique de l'Ouest: un édifice utile mais encore très fragile", *Le Monde Diplomatique*, August 1973, p. 19.

³ As P. Calvet (*op. cit.*, p. 115) explains: "La République islamique de Mauritanie s'est détachée de la zone pour des motifs d'ordre essentiellement politique, en s'abstenant d'ailleurs de donner à cette décision le caractère d'un geste dirigé contre la France. Les mauritaniens se sentaient mal à l'aise au sein de la BCEAO: il n'y a jamais eu d'entente parfaite entre la Mauritanie et les pays d'Afrique Noire; le Gouvernement de Nouakchott entendait d'autre part poursuivre une politique de socialisation, pour laquelle il désirait avoir une monnaie nationale entièrement indépendante."

nominal purchasing power. Certainly, the experiment is being followed with the greatest interest both in Africa and in the Arab world (which has already offered foreign exchange "gifts" to the new central bank), because, if successful, it would provide welcome proof that monetary sovereignty can be both feasible and fruitful.

In Madagascar, finally, the monetary changes of May 1973 followed the more radical political ones of the year before. No new central bank was set up (instead, the statutes of the existing one were amended), but the country withdrew from the franc zone, which thereby lost one of its more important members. Strict exchange controls were introduced and these apply also to France, whose future relations with the island can be expected to be confined to trade and co-operation.

(g) *The Maghreb countries' system of "comptes d'avances"*. All the African countries so far considered are either full members of the franc zone (the six states of the West African and the five of the Central African Monetary Union, and Mali), or they do not belong to it at all (Guinea, Mauritania and Madagascar).

The three Maghreb countries are in a sort of intermediary position¹. Each has its own, non-convertible currency and its national central bank, each practices exchange control and manages its own reserves; but, because of continuing strong commercial and financial connections with the former colonial power, each has negotiated a special agreement with France and has adopted the system of the so-called *comptes d'avances*.

¹ See Mustaphe Doghmi, *Le rôle de la Banque du Maroc dans le système monétaire et bancaire*, op. cit., p. 235-39; Bruno Rossignoli, *The Banking System of Algeria*, op. cit., p. 77-81; Robert Bistolfi, *Structure économique et indépendance monétaire. L'expérience monétaire de la Tunisie et ses enseignements*, op. cit., p. 126-60; Paolo Mottura, *The Banking System of Tunisia, 1956-70*, op. cit., p. 50-55.

This system works through two accounts opened by the Bank of France in the name of each of the three central banks concerned. The first is credited with transfers to the African country and debited with those from it; the second is in effect a credit line up to a pre-established amount, which can be drawn upon when the first account shows a debit balance.

This arrangement safeguards the monetary independence of Morocco, Algeria and Tunisia (none of which, incidentally, followed the French franc into devaluation in August 1969) and offers a limited guarantee of convertibility for their currencies, subject to compliance with the terms of the protocols of agreement which are renegotiated from time to time. Given that the limitless guarantee of convertibility vouchsafed by the mechanism of the operations accounts is more theoretical than real, and moreover involves heavy commitments in counterpart, the question is whether the system of *comptes d'avances* (France willing) would not be a better way of serving the interests of French-speaking Africa south of the Sahara. This question will be considered under (h) below, in an attempt to outline the possible monetary future of these countries.

(h) *Outlook for the future.* The franc zone, that paragon of *dirigisme* and automaticity in monetary affairs, has, then, itself not escaped radical transformation. The immobility and rigidity of colonial times have given way under a ferment of innovations and new awareness on the part of African nations.

It is not easy to predict along what lines monetary emancipation is likely to proceed, because the shape of things to come obviously depends not alone on decisions taken in Africa by individual countries or groups of countries, but very much also on France's own future position in relation to European integration and, more generally, to the new international monetary system in the seventies

and eighties. In ascending order of probability, four possible cases may be envisaged.

(a) The franc zone will remain much as it is today, with all the advantages and disadvantages that have been described. This is the view — or the hope — of Francophiles, and it is shared, though not openly, by some leading African personalities who feel that, when all is said and done, it is safer not to cut the umbilical cord by which African countries are attached to their former colonial ruler ¹.

(b) The franc zone will disintegrate altogether and will be followed by independent monetary systems like those of Guinea, Mauritania and Madagascar, or indeed of any other country responsible for the management of its own non-convertible currency. Given that monetary unification in Europe has got nowhere so far, this solution does not seem to go against the historical trend, since the African countries concerned never enjoyed monetary independence in the first place ².

¹ Diarra (*ibid.*, p. 26-27) rightly observes: "L'absence de réaction des dirigeants africains — que l'on pourrait croire délibérée chez les plus avertis d'entre eux — tient à diverses raisons. Ce sont: tout d'abord la persistance entre les dirigeants actuels, malgré les apparences, de vieilles rivalités personnelles entre anciens cadres de l'époque coloniale qui les empêchent de s'unir dans un domaine aussi essentiel que celui de la monnaie, par exemple, autrement que sous l'égide de l'ancienne Métropole. A cela on peut ajouter aussi, chez certains d'entre eux, le manque de confiance dans l'homme noir, également hérité du régime colonial, qui leur fait souvent préférer leur propre point de vue ou celui de l'étranger à ceux de leurs propres nationaux. Ce sont ensuite, chez certains dirigeants, des ambitions personnelles qui, malheureusement, ne se confondent pas toujours avec les intérêts vrais de leur pays. C'est, enfin et surtout, la sécurité que chacun d'eux semble trouver dans l'organisation monétaire actuelle."

² It is worth quoting in full the following passage from P. Calvet, (*ibid.*, p. 118): "La monnaie est l'un des attributs fondamentaux de la souveraineté de l'Etat. Il n'est pas étonnant que certains gouvernements veuillent, de ce point de vue, se dégager de toute alliance monétaire et poursuivre dans ce domaine une

(c) The franc zone will undergo such bold changes as are needed to satisfy its members' aspirations for independence, but without abandoning the advantages of some monetary alliance¹. This would probably mean separate national currencies issued by separate central banks linked by a regional (West and/or Central African) multilateral clearing mechanism rather like the European Payments Union, which served the countries of Europe very well in the fifties before convertibility was restored to their currencies. Foreign exchange would be available from two sources: from a common fund set up by member countries for pooling such surpluses as may accrue from time to time to any one of them, and from the Bank of France via the credit lines it would open on *comptes d'avances* as a witness to continuing co-operation between France and its former dependencies. The external value of African currencies would thus be guaranteed in the first place by inter-African solidarity, and as a second line of defence by French credits. However, this arrangement would probably differ from the present system to the extent that there would be more discrimination in helping one country or another, depending on the relative soundness of its monetary policy.

(d) The franc zone will, either in rigid or in flexible form, be absorbed by the European monetary area, to the extent that the latter really becomes an expression of economic integration among

politique totalement indépendante. On peut essayer de leur faire remarquer qu'ils vont ainsi à contrecourant de l'évolution de ce temps, puisque la Communauté Economique Européenne s'efforce, depuis des années, de créer une Union économique et monétaire, et que, sur le plan international, il est généralement admis que la destruction du système de Bretton Woods est une catastrophe à laquelle il faut porter remède. Mais s'ils persistent dans leur décision il ne peut être question d'y faire obstacle."

¹ There are a number of proposals of this kind, varying in some detail or other, and set out systematically by Diarra, *ibid.*, p. 63-68.

member nations. Even now Europe (with France still in the lead) is opening up towards Africa in the field of commercial and financial co-operation, and this is bound to encompass additional African countries if the members of the sterling area enter into association with the EEC. If this happens, it will be natural for certain monetary practices, too, to consolidate so that, at least implicitly, the result will be a new, large currency area. This is bound to take time, and above all must wait upon Europe getting on with its own unification. But we have learnt that little can be expected from any attempt to put monetary integration, based on some ingenious device or other, before economic integration.

7.3 THE STERLING AREA

Picking up the discussion of the sterling area where we left it in Chapter One, we recall that the main rules of membership in this originally informal system born from established practice were the following ¹:

- (a) holding the bulk of official reserves in sterling;
- (b) holding a more or less large proportion of private financial assets in London;
- (c) channelling foreign exchange transactions with countries outside the sterling area through the London market;
- (d) free payments within the area;
- (e) drawing on London as the main source of capital.

Much of all this no longer applies now, or not fully. The sterling area has been steadily disintegrating with the decline of

¹ See, among others, Jan V. Mladek, "Evolution of African Currencies: The Sterling Area and Unattached Currencies", *IBRD-IMF Finance and Development*, December 1964, and R. Higonnet, "Réflexions sur la zone sterling", *Economie Appliquée*, October-December 1958.

sterling as an international currency¹, and in this its fortunes are quite unlike those of the franc zone. Just because sterling used to be so prominent as an international reserve currency, it is in terms of this aspect that the sterling area's decline² can best be explained.

After the second world war and up to the floating of sterling in June 1972, the sterling area — or Scheduled Territories, as it was called after 1947 — consisted of the following countries: Australia, New Zealand, South Africa, India, Pakistan, Ceylon, in the Caribbean zone the Bahamas, Bermuda, British Honduras and Guiana, in black Africa Nigeria, Gambia, Ghana, Sierra Leone, Kenya, Tanzania, Uganda, Malawi and Zambia, in the Far East Brunei, Hong Kong, Malaysia and Singapore, in the Middle East Jordan, Kuwait, South Yemen and other Persian Gulf territories, and some other countries like Cyprus, Iceland, Ireland and Malta.

¹ What happened is concisely summarized by A.R. Conan, "Re-structuring the Sterling Area", *The Banker*, May 1968, p. 430: "Perhaps the real trouble is that the sterling area can no longer operate on the traditional basis. Ultimately the strength of the pound is dependent on the balance of payments between the system and the rest of the world; this balance (not the out-turn for Britain alone) determines the level of the reserves. Formerly the working of the system in relation to the non-sterling world involved reciprocal links between Britain and the rest of the sterling area; more specifically, the deficit of the former was set against the surplus of the latter. Now (if recent trends persist) the system can no longer function in that way: Britain still has a deficit with the non-sterling world, but the overseas sector no longer earns a surplus to cover it."

² The titles of some of the works which shed light on these events read almost like a running commentary on the successive stages of a long agony — note the dates: S. Venkataraman, "Sunset over the Sterling Area", *The Economic Weekly* (Bombay), 15 February 1958; J. Avenir, "Les facteurs de désintégration de l'espace sterling", *Revue juridique et économique du Sud-Ouest*, 1958; H.A. Spengler, "Is the Sterling Area Disintegrating?", *The Banker*, January 1964; H. Lever, "Ending the Reserve Role of Sterling", *The Banker*, January 1971; Paul Bureau, "Death of the Sterling Area", *The Banker*, August 1972.

Let us see how they all observed the first of the rules of membership. In September 1949, on the occasion of the first postwar devaluation of the pound, all of them with very few exceptions followed suit — an impressive demonstration of cohesion.

But when, in December 1958, Britain joined the world's other leading industrial nations in declaring external currency convertibility, much of the group's *raison d'être* disappeared. For current payments, a distinction was made between two categories: sterling on resident (i.e. Scheduled Territories) account, and sterling on external account. The latter were owned by persons or companies outside the sterling area, and were, upon request, convertible into other foreign exchange; their position was thus much like that of resident accounts, except that the latter were subject to exchange control for transfers to anywhere outside the Scheduled Territories. For capital movements, on the other hand, residents were given more freedom¹.

Throughout the sixties, the situation of sterling worsened along with the weakness of the British economy and the deterioration of Britain's external payments, not to speak of occasional speculative pressure². In 1966 came the first of several Basle arrangements³, a stand-by credit by a consortium of central banks to help Britain meet the demand for conversion of sterling into other currencies.

¹ The Midland Bank Review, "The Evolution of the Sterling Area: What it Signifies Today", February 1972, p. 12, rightly states that "the granting of convertibility to external sterling is the most noteworthy overt event affecting the position of the sterling area which can be pinpointed between the devaluations of 1949 and 1967."

² Among many, reference is made to G. Stamatii, *Il sistema monetario internazionale*, Turin 1973, p. 69-82.

³ Named after the seat of the Bank for International Settlements, which co-ordinated all these rescue operations. For details, see Sergio Bortolani, *Le funzioni monetarie della Banca dei Regolamenti Internazionali*, Milan 1968, p. 19-21.

But this credit facility did not prevent a second devaluation. In November 1967, sterling was devalued by 14.3 per cent, a move which must be seen as the starting point of all the successive monetary crises which eventually culminated in the collapse of the Bretton Woods system. On this occasion the response of the sterling area was far from unanimous, and indeed most countries did the opposite of what they had done in 1946. In Africa, only Sierra Leone, Gambia and Malawi followed suit; all the others kept the dollar parity of their currencies unaltered, which meant revaluation against sterling.

A new Basle stand-by credit followed in September 1968¹, to prop up the ailing pound. To discourage the sterling area's central banks and other official institutions from completely off-loading all their sterling balances, Britain at the same time offered a dollar value guarantee for any sterling balances in excess of 10 per cent of any country's total reserves, in case of future devaluations².

Nevertheless more and more sterling area currencies disengaged from the pound and established a dollar link instead between August and December 1971, and after the Smithsonian Agreement of 18 December 1971 and its general realignment of exchange rate relationships.

When the pound was eventually floated in June 1972, the response in the remaining sterling area was more mixed than ever³.

¹ See New Zealand Chancellor of the Exchequer, "The Basle Facility and the Sterling Area", *Reserve Bank of New Zealand Bulletin*, October 1968.

² For more detail see M. Crawford, "Guarantees for the Sterling Area: A Stronger System Emerges from Basle", *The Round Table*, 1969.

³ At that point, the Bank for International Settlements, in its 43rd Annual Report, 18 June 1973, p. 170, distinguished three main groups of sterling area

Some countries whose ties with sterling were already weak, chose to make the final break on the grounds that Britain had failed to notify them in advance of the decision to float¹.

The first basic rule of the sterling area, then, was flouted by most of its members, partly no doubt because of a natural process of commercial and financial diversification, but chiefly because of the key currency's own instability. Devaluation, external convertibility and fluctuations all made for disintegration, with no hope of offsetting factors even in the medium run. Since then we have had Britain's tormented entry into the Common Market, upheavals in the international monetary system, and now the repercussions of the oil crisis — and all the time the growing independence of sovereign nations. It is safe to predict an irreversible process by which each country will henceforth adapt its own monetary and foreign exchange policy to the moment's requirements.

countries. A first group whose currencies were already anchored to the dollar and which did not alter the dollar parity of their currencies: Australia, Ghana, Iceland, Jordan, Kenya, New Zealand, Nigeria, Pakistan, Tanzania, Uganda, Western Samoa and Zambia. A second group gave up their previous sterling link and anchored their currencies to the dollar by maintaining their dollar parity: Cyprus, Hong Kong, Kuwait, Malaysia, Oman and Singapore. The third group floated their currencies along with sterling: Bangladesh, Barbados, Botswana, Fiji, Gambia, Guiana, India, Ireland, Jamaica, Lesotho, Malawi, Mauritius, Sierra Leone, South Africa, Swaziland, and Trinidad and Tobago. Sri Lanka returned from a dollar to a sterling link, Malta chose unilateral, controlled floating. Iraq, finally, though not part of the sterling area, anchored its currency to sterling shortly before it was set afloat.

¹ The following laconic statement is by Paul Bureau ("Death of the Sterling Area", *The Banker*, August 1972, n. 1028): "The sterling area, on which the sun never set, now consists of the United Kingdom, the Channel Islands, the Isle of Man and, ironically, the Republic of Ireland. Its recent spectacular contraction was a direct consequence of the floating of sterling on June 23."

As regards the second and third rule, the maintenance of official and private sterling balances, the risks of sudden conversions has been a permanent threat to the stability of the sterling area, along with the crisis of confidence in the pound. The two phenomena are, of course, interdependent, in so far as the weakness of sterling raised apprehensions and hence led to conversions, which in turn worsened the position.

With the decline of the pound's function as an international currency, the problem arose of how (gradually) to withdraw from circulation official sterling balances at sight or on short notice. A number of proposals were put forward to this end¹, and the one chosen for the time being was to fund these liabilities by transforming them into a long-term debt. This was done not for all the sterling balances, but for only part of them, and the operation was made possible thanks to central bank co-operation. Once the international monetary system is restructured and the European Monetary Union exists on more than paper, more durable solutions can be thought of within the framework either of the IMF or the EEC. Meanwhile the African countries concerned have followed the trend and, notwithstanding the intervening dollar guarantee, have run down their sterling balances.

Even greater concern was caused by liquid sterling assets in the hands of private owners, both from the sterling area and from outside it. An appreciable part of these will no doubt always remain in circulation, for transactions purposes, but these liabilities certainly

¹ See R. Ossola and P. Savona, "The Future of Sterling: A Logical Approach", *The Round Table*, October 1971; H. Weise, *The Role of Sterling after Britain's Entry into the European Economic Community: A Continental View*, Tilburg 1972, p. 13-17; H. Lever, *op. cit.*, p. 21-22; M. Crawford, "Funding the Sterling Balances", *The Banker*, July 1968.

represent the most volatile and least controllable portion of the whole of the overseas sterling balances, for there is always a danger of sudden and massive conversions in any sterling crisis¹. However, while in the past the parity had to be defended within the margins of fluctuation, sterling can now be sold only at rates which penalize the vendor, since daily rates are determined by market forces (corrected, if the Bank of England sees fit, by official intervention).

So the loosening of the ties with Britain shows up, too, in the composition of member countries' official reserves and in private sterling holdings. Much the same can be said of the other conditions of membership, i.e. exchange control regulations and the absolute primacy of London as the system's financial centre.

So far as current operations are concerned, external convertibility left only trifling differences in the treatment of sterling owners inside and outside the sterling area. For capital movements, there is at present a preferential regime for member countries², but even so transfers are no longer absolutely free. Nor are the regulations as uniform as they used to be, because each country has adopted its own controls.

London has lost some of its pre-eminence as the area's financial centre, in direct consequence of the difficulties into which the pound got and of the measures taken to reduce the balance-of-payments deficit, which include restrictions on outward capital transfers. Member countries have found other sources for raising funds in various forms, in substitution of the London capital market. But the latter has adapted itself and for some years past has done a

¹ See R.G. Holloway, "The Burden of the Sterling Area", *The Bankers' Magazine*, July 1968.

² For details of the regulations, see Paul Bareau, *ibid.*, p. 1029-31, and Midland Bank Review, *op. cit.*, p. 14-15.

huge business in Euro-currencies, for which it has become the leading centre¹.

We must conclude that the disintegration of the sterling area has to all intents and purposes reached its final stage, without official declarations or explicit abrogations, just as informally as the system arose in the last century. Unlike French-speaking Africa, the African nations of the sterling area had been free, on the morrow of independence, to set up their own central banks; if they continued to adhere to the sterling area, it was perhaps mostly for historical reasons and in the hope of a gradual transition to diversification of trade and financial flows. The ill fortunes of the pound in recent years probably did no more than accelerate a process which in any case was inevitable. At least no obstacles were piled up against the inevitable, as seems to be happening in the franc zone.

If the European Economic Community overcomes its present divisions and moves towards monetary union, and if the successor to the Yaoundé Convention associates also the English-speaking nations of Africa with the EEC, then the natural outcome must sooner or later be the emergence of a vast Euro-African currency area. But what it will be like is hard to imagine at present.

7.4 CONCLUSIONS: ASPECTS OF AN INTERNATIONAL DEVELOPMENT STRATEGY

More than once in this book there has been occasion to stress the importance of promoting development "from within", by means

¹ Bureau has some doubts on this matter (*ibid.*, p. 1031): "London will in future as in the past adjust itself to changing circumstances and will transact business in other currencies. It must, however, be doubted whether any national centre of an international market, can reach its full potential by dealing in terms of a currency which is not its own."

of co-ordinated action by the public and the private sector. This must indeed be the basic choice, to be pursued without impatience, and drawing on all local resources and capacity.

But it has also been made clear how close are the ties of African economies with the rest of the world. In the commercial, the financial and the monetary fields the present unsatisfactory situation will be improved by negotiations or, more probably, by a trial of strength between the new and the industrial nations. An attempt is made below to outline the major aims to be pursued¹.

(1) *Commercial relations*

The situation of developing countries is well illustrated by the global figures of Table 11. Comparing 1960 with 1970, it will be seen how little headway was made during the sixties in remedying a state of affairs which perpetuates an international division of labour harshly unfavourable to the Third World.

Proposals have been put forward for (a) commodity agreements and buffer stocks financed by international organizations, so as to mitigate price fluctuations; (b) trade liberalization through the dismantlement of restrictions and duties on the industrial countries' imports from developing ones, a guaranteed minimum share for their competitive products in markets of industrial countries, the abolition of special preferences (such as are enshrined in the Yaoundé Convention), and duty-free entry to developed countries for manufactures from developing ones (extension of the Kennedy round to them).

¹ These largely reflect the demands put forward by the Group of 77 on the occasion of the third UNCTAD Conference. See also UNCTAD, *International Development Strategy in Action*, Santiago del Chile 1972.

TABLE 11

SHARE OF PRIMARY PRODUCTS AND MANUFACTURES IN THE TOTAL EXPORTS OF DEVELOPING AND DEVELOPED COUNTRIES, 1960 AND 1970

	Exports (millions \$)		Share in total exports (per cent)	
	1960	1970	1960	1970
<i>Developing countries</i>				
Primary products	22.0	41.2	85.0	75.9
Manufactures	3.8	12.7	14.6	23.4
Various	0.1	0.4	0.4	0.7
Total exports	25.9	54.3	100.0	100.0
<i>Developed countries</i>				
Primary products	25.3	51.4	30.8	22.9
Manufactures	54.0	169.1	65.9	75.4
Various	2.7	3.7	3.3	1.7
Total exports	82.0	224.2	100.0	100.0

Source: United Nations.

Africa, of course, has a formidable dilemma because any privileges it gains in its negotiations with Europe¹ would imply discrimination against other developing countries.

(2) *Financial relations*

In order to help developing countries cover at least part of the shortage of their scarcest factor of production, capital, a flow of

¹ From the voluminous literature on the relations between Europe and Africa, reference is made to the following: M. Andreis, *L'Africa e la Comunità Economica Europea*, Turin 1967, and, among more recent works, C. Secchi, "Il rinnovo dell'associazione tra la CEE e i SAMA e le tendenze della politica comunitaria verso i paesi sottosviluppati", *Rivista Internazionale di Scienze Economiche e Commerciali*, November 1973, and *Una nuova associazione fra l'Europa dei nove e l'Africa*, Istituto per le relazioni tra l'Italia e i paesi dell'Africa, America Latina e Medio Oriente, Milan, 29-30 March 1974.

funds of various origin has been, and continues to be, directed towards their economies.

But the total of transfers actually carried out in the sixties fell short of even the modest target set by the United Nations for the First Development Decade, that is, a net amount of resources (after reimbursements) equal to 1 per cent of the combined gross national product of the industrial nations. The shortfall is illustrated in Table 12.

Transfers are made under three headings: grants, loans and investments. The following comments may be made about each.

(a) *Grants*. These are in essence gifts of various kinds, which need not be repaid and come from governments, public or private agencies. In absolute terms, their amount hardly changed from the beginning to the end of the sixties, but their share in the total flow of resources declined from 45 per cent in 1961 to 21 per cent in 1971 — which goes to show the dislike of — especially official — donors for a type of aid which brings benefit to the recipients but very little to themselves.

(b) *Loans*. Loans may be for the short term, but more often are for the medium or long term. They have to be repaid in instalments over a more or less lengthy period, and carry either market terms ("hard loans") or concessional terms ("soft loans" — i.e. for very long periods and/or at zero or low interest rates).

According to their source, loans may be public or private, and multilateral or bilateral.

Public loans preponderate. They are granted directly by governments or by parastatal agencies. If they are bilateral, only two countries are involved: the donor and the recipient country. The amount of such loans did grow during the sixties both in absolute and in relative terms, but certainly not at a spectacular

TABLE 12

FLOW OF FINANCIAL RESOURCES TO DEVELOPING COUNTRIES, 1960 TO 1970

Year	Net total flow of financial resources to developing countries (billion \$)	UN target of 1 per cent of GNP (billion \$)	Proportion of target achieved (per cent)
1960	8.1	9.1	0.89
1961	9.2	9.6	0.95
1962	8.4	10.4	0.80
1963	8.3	11.2	0.76
1964	9.6	12.1	0.79
1965	10.3	13.1	0.77
1966	10.4	14.4	0.71
1967	11.4	15.3	0.74
1968	13.4	16.7	0.80
1969	13.8	18.4	0.75
1970	15.0	19.9	0.75

Source: OECD.

rate; taking together loans from the Development Assistance Committee (DAC), which in practice means the most advanced Western nations, and disbursements by countries with a centralized economy, they amounted to just over 4 billion dollars in 1971, or to one quarter of the total flow of financial resources to the Third World. Bilateral loans are only too often "tied", which means that recipient countries are obliged to spend the proceeds on buying machines, equipment or other goods in the lending country, so that the effective cost of the loan is higher than its terms suggest. In addition, of course, there may well be political strings.

With a view to obviating some of these drawbacks, loans have been provided for some years past also by international organizations

which collect funds mainly from industrial nations (through capital subscriptions, bond issues and various contributions) and channel them to developing ones to finance so-called priority projects. Outstanding among these organizations is the World Bank group, which consists of the International Bank for Reconstruction and Development (IBRD) itself and its two affiliates, the International Development Association (IDA) and the International Finance Corporation (IFC). Between them, these three closely related institutions offer a variety of development finance ranging from loans at market terms through concessional loans to equity participation in private enterprises.

Next, there are several regional organizations for separate continents, which mobilize additional resources from industrial nations and redistribute any funds pooled by developing ones. In Africa, the relevant institution is the African Development Bank, whose principal purpose is to finance regional projects beyond the scope of national development banks, the idea being thereby to foster economic integration among the countries of any one region.

But a loan does not end with its disbursement; it involves a very heavy burden of external debt charges, which it is proposed to alleviate by conversion into long-term bonds. The debt burden increased very sharply in the wake of the rise of oil prices towards the end of 1973, but it is not inconceivable that the oil producers may, for political reasons, channel some of their higher export earnings back to "friendly" African nations, on a bilateral or a multilateral basis¹.

¹ Some possible ways of doing so are examined in Sergio Bortolani, "Aspetti dei trasferimenti di capitali verso i paesi in via di sviluppo", *Il Risparmio*, May 1974, p. 20-24 (offprint). See also M. Develle and J.P. Villain, "Les Arabo-dollars", *Banque*, May 1974.

(c) *Investments.* The distinguishing feature of investments as against grants and loans is that they represent venture capital. The return outflow of funds depends on earnings and may take the form of profit repatriation, not to speak of possible disinvestment. Investments are most often private and have grown so much over the years that they now account for almost half of all the funds transferred to the Third World. Those of multinational companies stand out for their generally larger amounts and greater project diversification.

Such transfers involve serious disadvantages, political, economic and social alike; on the other hand, the host countries are so short of some vital factors of production — capital, technology and management capacity — that they cannot afford to close themselves off completely. An acceptable compromise might be a sort of controlled openness, with specified conditions for foreign investment. It certainly is a fact that while investment by multinationals has done nothing to alter the prevailing “philosophy” of the international division of labour, it has historically worked in favour of developing countries. There is, of course, room for improvement, and developing countries would do well to insist on the following points when accepting foreign investment ¹.

(i) The investment project should fit into the country's development plan and not be extraneous to it. It should act as a “development pole” in terms of the effects of the foreign investment on domestic social purposes (construction of schools, public health and recreation amenities, basic infrastructures).

(ii) It is of the utmost importance to attend to the training of local skilled labour, technicians and managerial staff. Indigenous

¹ See Bortolani, *ibid.*, p. 10-12.

skills of these kinds are scarce or indeed totally lacking in developing countries today, and only training can provide them for the future on a self-sustaining basis. This is obviously a slow process projecting into the medium- or even long-term future, involving, as it does, the gradual replacement of present foreign personnel; but the important point is to make sure that the foreign investment project, which in the first place is something "from outside", does not remain for ever extraneous and non-assimilated by the people of developing countries. Everything must be done not to allow the conviction and certainty to take root locally that in certain critical situations everything can ultimately be set right by the foreign technician. Of course, training is a troublesome business and the results are not always brilliant, and in addition one has to overcome the indifference of local people to such notions as maintenance, amortization, renewal, and generally a dynamic approach. The governments of developing countries are well aware of this, and have for some time past done what they could to improve instruction at various levels. But any hope of an at least partially independent future depends crucially on combining general cultural advance with the absorption of techniques transplanted from abroad. This is difficult enough in the beginning, but probably a necessary stage in acquiring certain intellectual capacities which after a few generations may generate original contributions.

(iii) In the interests of safeguarding national independence to the extent possible, governments would be well advised to follow the growing practice of classifying projects in accordance with a detailed investment code, specifying the sectors in which foreign participation is acceptable, those in which it is precluded and those open to joint ventures.

(iv) In any event, highly labour-intensive investments are preferable. Many developing countries in the past made the mistake of, perhaps unconsciously, orienting foreign investors towards capital-intensive projects by a policy of artificially low interest rates. What attracts multinational companies is not the low cost of local borrowing (cheaper than in their countries of origin), but the low cost of labour, and labour-intensive projects should help at least to alleviate unemployment¹.

(v) Some restrictions need to be imposed on export of profits, and this is general practice nowadays; but these must not be carried to extremes, lest foreign investors are frightened off altogether. Capitalist enterprise, after all, works in order to earn profits and to expand; subject to profits being adequately ascertained and taxed (say at 50 per cent), it is more important to insist on the other conditions mentioned above than to be too obstinate about the ultimately inevitable outflow of resources through profit repatriation. Unfortunately, African governments have often been short-sighted enough to make room for something like the following adverse course of events: governments want the profits of foreign enterprise to be high, because they themselves can then pocket correspondingly more either as joint partners or through taxation; high profits are obtained by leaving the management of the enterprise to the foreign investor; this discourages or delays the appointment of local personnel to top posts and lengthens the road to technological independence.

(vi) Once an enterprise has been successfully started, it is desirable that local investors should have a chance of buying shares in it, which means that the multinational company and the state

¹ See section 4.7 above.

must give up part of their holdings. Even if it is only a small part, it will help to spread equity ownership and to create and broaden local capital markets ¹.

(vii) With reference to the problem of control of the new company, there is a case for local participation on the largest possible scale. But even a majority holding by the state does not always help, because experience has shown that effective control nevertheless remains in the hands of the multinational company with its superior management and technical capacity. The only lasting solution lies in training local personnel, as discussed under point (ii) above.

(viii) Generally speaking, the best results are obtained by co-ordinated action at supra-national level. It is easy for multinational companies with their branches throughout the world to have a bargaining advantage over individual governments, whom they can play off against each other if necessary. Only by means of appropriate groupings (by commodities, by geographical area) can developing countries hope to strengthen their bargaining power *vis-à-vis* the big multinationals.

(3) *Monetary relations*

Any major change in the monetary relations between developing countries and the rest of the world depends upon a reform of the international monetary system. Recommendations for reform were published last June by the Committee of Twenty, or to give it its full official name, the Committee on Reform of the International Monetary System and Related Issues ². While there is a general

¹ See section 6.4 above.

² Committee of Twenty, "Outline of Reform and Accompanying Annexes", *IMF Survey*, 17 June 1974, p. 193-208.

consensus on some of these recommendations, others still await even preliminary agreement.

Among the latter figures one of more interest to the Third World than almost any other, namely, changes in the mechanism of SDR allocation¹. At present, special drawing rights are a means of channelling new liquid resources to developing countries, which received 27 per cent of the total, this being the sum of their IMF quotas². A question springs immediately to mind: Is it right that all the poor countries together, numerous as they are and beset by the most pressing financial needs, should get barely more than one quarter of total allocations? Since SDRs are destined in the future to play a decisive part as a component of liquidity, reserve asset and means of payment, is it possible and realistic to hope that the SDR scheme will be so altered as to make more generous allowance for the needs of developing countries?

This is what is known as the link problem, the link, that is, between SDR creation and development financing. It has been debated at length for months, nay years, by experts and scholars, by committees and full-scale official assemblies (UNCTAD, IMF, the

¹ Special drawing rights have, since 1 January 1970, been a new instrument of international liquidity. They are created by the IMF and allocated by it to member nations in proportion to their Fund quotas. The first allocation, for the years 1970-72, amounted to SDR 9.5 billion, which were a net addition to gold, dollars and other strong currencies used for payments among the central banks of different nations. The conventional value of special drawing rights is 0.888671 gram of fine gold, but they are neither convertible into nor backed by gold. Their effective value lies in acceptance by the countries participating in the scheme, which means central banks are committed to accept SDRs (up to specified amounts) in payment for their credits as an alternative to settlement by other assets.

² Africa as a whole (excluding South Africa) gets only just over 5 per cent of the total.

Association of African Central Banks, and others)¹. Briefly, two types of link are proposed: one organic or direct, the other inorganic or indirect. The first would imply that a more or less sizeable part of SDRs be used directly to finance development, leaving the remainder to be allocated as at present; the second type of link would require the IMF to credit part of the SDRs to the finance institutions of the World Bank group, to be used by them for loans to developing countries.

In either case there would be a larger automatic flow of resources to the Third World and in time this flow might partially or wholly replace today's bilateral capital transfers, with all their snags and limitations.

Without underestimating the implications of this link for international liquidity and its possible inflationary effects², such a system would surely be a real breakthrough in the unbalanced relations between the developed and the developing world, and it would narrow the gap without imposing unduly heavy conditions upon the latter. The interest rate on SDRs was raised as of 1 July 1974, from 1.5 to 5 per cent; if it were brought even closer to market levels, this would admittedly put an inevitable burden upon

¹ As a small selection of writings on this problem, see Gottfried von Haberler, "The case against the link", *Banca Nazionale del Lavoro Quarterly Review*, March 1971; C. Secchi, "Diritti speciali di prelievo e finanziamento dello sviluppo: i termini del problema", *Rivista Internazionale di Scienze Economiche e Commerciali*, June 1972; Vittorio Barattieri, "Diritti speciali di prelievo e finanziamento dello sviluppo: una analisi dei costi e benefici", *Bancaria*, December 1972.

² The Committee of Twenty (*ibid.*, p. 208) is specific: "The establishment of a link has not been agreed. It is however generally agreed that, if a link were to be established, the amount of SDR allocations and the principal characteristics of SDRs should continue to be determined solely on the basis of global monetary requirements and that these characteristics should be the same for all SDRs whether distributed through normal allocations or through a link."

developing countries, but would also induce the sellers of capital goods (the industrial nations) to keep the SDRs received in payment for their supplies. The system would not be free, but it would have the merit of institutionalizing a transfer mechanism carrying the ultimate guarantee of supra-national control either by the International Monetary Fund or by the World Bank.

These proposals have had a mixed reception so far. Developing countries obviously have welcomed a link in one form or another; the leading industrial nations are divided. A majority seems to be in favour of a link (including Italy, which has supported the "inorganic" type of link ever since 1969), but two, the United States and Germany, are against it. It is perhaps hardly surprising that the world's richest nation should be hostile to such a scheme. Behind the superficial arguments put forward by Secretary of the Treasury George P. Shultz at the IBRD annual meeting at Nairobi in September 1973¹ it is easy to detect the much deeper concern that some day a new means of international settlement might replace the dollar, the chief vehicle of American expansion in the world. There is another point, too: the link mechanism would surely lead to a distribution of the industrial nations' supplies on different criteria from those prevailing today, and this would most probably mean a reduction in those from the United States.

This clash on the question of the new function of special drawing rights in connection with the reform of the international

¹ "We feel the so-called SDR-aid link would in practice serve well neither monetary stability nor economic development. Experience strongly demonstrates the wisdom of keeping separate the function of money creation — which is what SDR is all about — and the essentially political decision of resource transfer and redistribution." (George P. Shultz, *Speech to the Annual Meeting of the Board of Governors*, IBRD Summary Proceedings, Nairobi, 24-28 September 1973, p. 191).

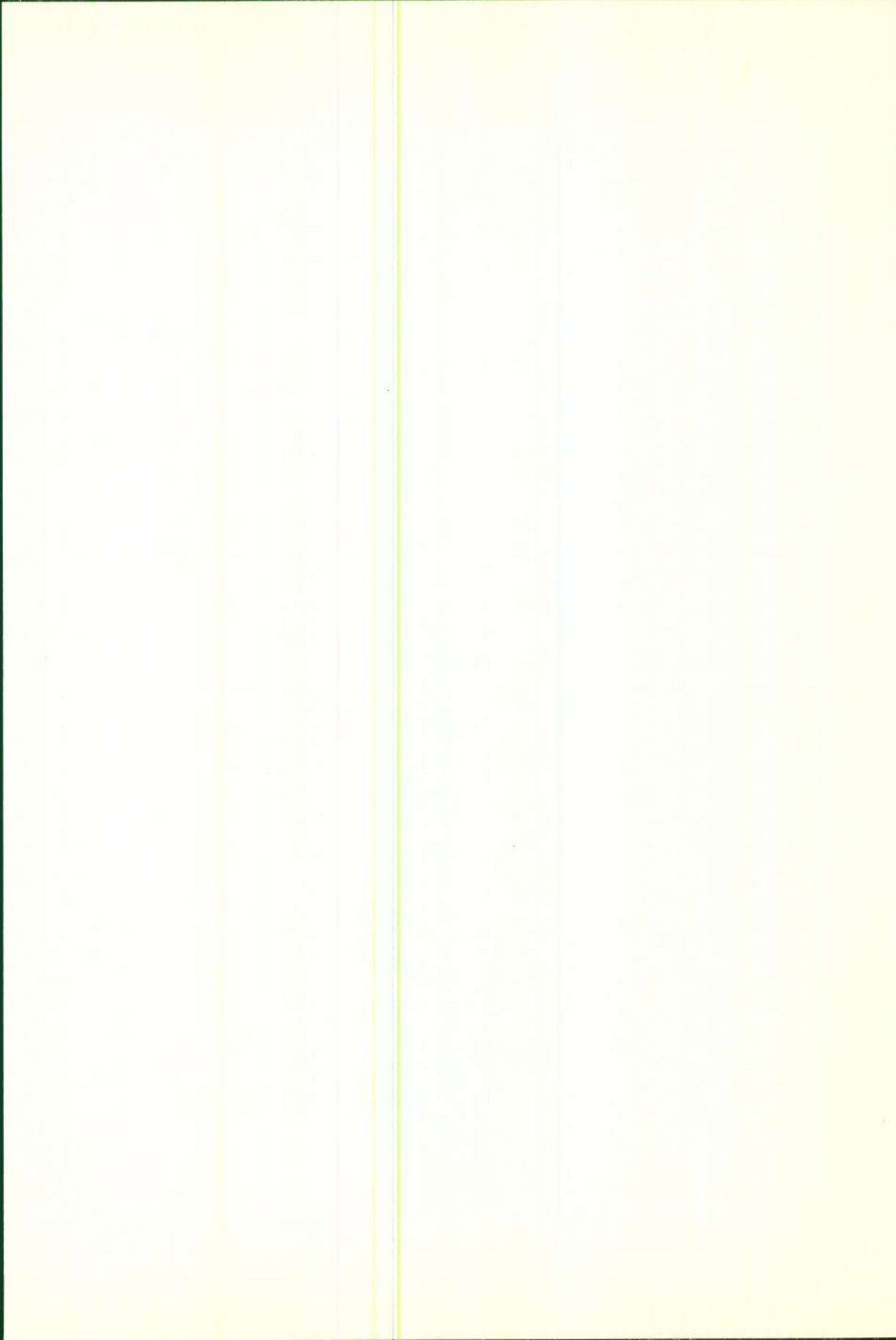
monetary system is assuredly of great import, for ultimately only global solutions can in the long run really benefit the Third World.

The central banks of Africa¹, in their turn, are fervent supporters of the idea and recommend the adoption of an organic link, as well as a distribution key which makes special allowance for the needs of the poorest among the developing countries.

¹ See Association of African Central Banks, *Report of the Third Regular Meeting*, Lagos, 20-24 August 1973, United Nations Economic Commission for Africa, p. 9.

ABBREVIATIONS

AEF	Afrique Equatoriale Française	GATT	General Agreement on Tariffs and Trade
AOF	Afrique Occidentale Française	GDP	Gross Domestic Product
BAT	Banque de l'Algérie et de la Tunisie	GIHOC	Ghana Industrial Holding Company
BCEAEC	Banque Centrale des Etats de l'Afrique Equatoriale et du Cameroun	GNP	Gross National Product
BCEAO	Banque Centrale des Etats de l'Afrique de l'Ouest	IBRD	International Bank for Reconstruction and Development
BEAC	Banque des Etats de l'Afrique Centrale	IDA	International Development Association
BIAO	Banque Internationale pour l'Afrique Occidentale	IFC	International Finance Corporation
BNDA	Banque Nationale pour le Développement Agricole (Ivory Coast)	IMF	International Monetary Fund
BOAD	Banque Ouest-Africaine de Développement	IRI	Istituto per la Ricostruzione Industriale (Italy)
CFA	Communauté Financière Africaine	ISBI	International Savings Banks Institute
CFA	Coopération Financière en Afrique	SDRs	Special Drawing Rights
DAC	Development Assistance Committee	UAR	United Arab Republic
EDF	European Development Fund	UDEAC	Union Douanière et Economique de l'Afrique Centrale
EEC	European Economic Community	UMOA	Union Monétaire Ouest-Africaine
FAO	Food and Agriculture Organization of the United Nations	UN	United Nations
FINAFRICA	Centre for Financial Aid to African Countries (Milan)	UNCTAD	United Nations Conference on Trade and Development
		US, USA	United States of America
		USSR	Union of Soviet Socialist Republics



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