Regional Integration Policy Paper
Challenges towards Regional Financial Integration and Monetary Coordination in the West African Monetary Zone and the East African Community

Author: Gabriel Mougani

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REGIONAL INTEGRATION POLICY PAPER

Challenges towards Regional Financial Integration and Monetary Coordination in the West African Monetary Zone and the East African Community

Analysis and Policy Recommendations

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Supervisor: Moono Mupotola
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ABBREVIATIONS

ADB (AfDB) : African Development Bank
ADF : African Development Fund
AMU : Arab Maghreb Union
ASEAN : Association of Southeast Asian Nations
BEAC : Bank of Central African States
CBK : Central Bank of Kenya
CEMAC : Central African Economic and Monetary Community
CMIPC : Capital Markets, Insurance and Pension Committee
CEO : Chief Executive Officer
CET : Common External Tariff
COMESA : Common Market of East and Southern Africa
CSP : Country Strategy Paper
DP : Development partner
DSE : Dar es-salaam Stock Exchange
EAC : East African Community
EAMI : East African Monetary Institute
EAMU : East African Monetary Union
ECB : European Central Bank
ECBS : European Central Banks System
ECOSTAT : ECOWAS Institute for Statistics
ECOWAS : Economic Community of West African States
EEC : European Economic Community
EFTS : ECOWAS Free Trade Scheme
EMCP : ECOWAS Monetary Cooperation Programme
EMI : European Monetary Institute
EMU : Economic and Monetary Union
ERM : Exchange Rate Mechanism
ETLS : ECOWAS Trade Liberalization Scheme
EU : European Union
FSAP : Financial Sector Assessment program
FSDRP : Financial System Development and Regionalization
GSE : Ghana Stock Exchange
HLTF : High Level Task Force
<table>
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<tr>
<th>Acronym</th>
<th>Description</th>
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<tbody>
<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IFRS</td>
<td>International Financial Reporting Standards</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>KSMS</td>
<td>Kenya School of Monetary Studies</td>
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<td>MAC</td>
<td>Monetary Affairs Committee</td>
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<td>MC</td>
<td>Monetary Coordination</td>
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<td>MoU</td>
<td>Memorandum of Understanding</td>
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<td>NSE</td>
<td>Nairobi Stock Exchange</td>
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<td>NSCs</td>
<td>National Sensitisation Committees</td>
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<td>OCA</td>
<td>Optimum Currency Area</td>
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<td>ONRI</td>
<td>NEPAD, Regional Integration and Trade Department</td>
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<td>ONRI.2</td>
<td>Regional Integration and Trade Division</td>
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<tr>
<td>PTS</td>
<td>Permanent Technical Secretariat</td>
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<td>RCMDC</td>
<td>Regional Capital Market Development Committee</td>
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<td>RFI</td>
<td>Regional Financial Integration</td>
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<td>RISP</td>
<td>Regional Integration Strategy Paper</td>
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<td>RMP</td>
<td>Reserve Monetary Program</td>
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<td>RTGS</td>
<td>Real Time Gross Settlement</td>
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<tr>
<td>SIDA</td>
<td>Swedish International Development Agency</td>
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<tr>
<td>USAID</td>
<td>United States Agency for International Development</td>
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<tr>
<td>XNSA</td>
<td>Nigerian Stock Exchange</td>
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<td>WABA</td>
<td>West African Bankers Association</td>
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<tr>
<td>WACB</td>
<td>West African Central Bank</td>
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<tr>
<td>WAEMU</td>
<td>West African Economic and Monetary Union</td>
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<td>WAFSA</td>
<td>West African Financial Surveillance Authority</td>
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<td>WAMI</td>
<td>West African Monetary Institute</td>
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<td>WAMZ</td>
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The views expressed in this report are those of the author and do not necessarily represent those of the Bank, other institutions or persons mentioned.
FOREWORD

To foster regional economic, monetary and financial integration in the West African Monetary Zone and the East African Community, institutional frameworks and a range of policies have been put in place. Outstanding progress has been achieved towards economic integration (including the progressive development of regional infrastructure and the removal of some barriers to intra-regional trade). However, progress in the economic convergence as well as monetary coordination and financial sector integration has been slow.

Indeed, the timeframes set by both African RECs to complete the integration of their financial and monetary systems seem to be very ambitious, the more so as the history of the Euro Zone shows that a very long period is needed to attain the ultimate stage of single currency. The Euro Zone example also shows that the establishment of a monetary union is facilitated when there is prior monetary coordination and a sufficient degree of regional financial integration. Therefore, the Euro Zone model should incite African RECs to adopt a cautious and gradual approach towards monetary union by fulfilling some minimum prerequisite conditions (such as a sufficient degree of trade and economic integration, a relatively advanced financial system and market integration, and an adequate level of monetary cooperation to provide a base for vibrant coordination of monetary and trade policies). Both regions should take appropriate steps and undertake more technical preparations prior to the expected implementation date to ensure that member countries will not suffer the same difficulties as those in the Eurozone.

In addition, some clear lessons emerge from the Eurozone crisis that directly relate to the WAMZ and EAC and its path toward creating a monetary union. Policymakers working on WAMZ and EAC integration should be approaching the adoption of a single monetary union with caution given the ongoing sovereign debt crisis in Europe. The report concludes by indicating the role that the development partners, including the African Development Bank Group, might play in this endeavour.

This report that describes research in progress within the Regional Integration and Trade Division is published to elicit comments and further debates.

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EXECUTIVE SUMMARY

Introduction

The African Regional Economic Communities (RECs) are committed to gradually establishing an economic union in their respective sub-regions in accordance with the objectives of the Abuja Treaty. The RECs pursue a gradual objective geared towards attaining the ultimate stage of economic and monetary union.

There is abundant economic literature on the costs and advantages of an economic and monetary union at the theoretical and empirical levels. Traditional literature on the Optimal Currency Areas (OCA) theory, developed by Mundell (1961) and McKinnon (1963), posit that member countries of a monetary union will benefit from lower transaction costs emanating from trading goods and assets in foreign currency. Recent empirical data highlight the significant positive impact of monetary unions on trade (Rose 2000, Glick and Rose 2001) and income (Frankel and Rose 2002). The other possible advantages in terms of macro-economic efficiency for joining a monetary union are the elimination of (or significant reduction in) nominal exchange rate volatility and hence lower interest rates, low real exchange rate volatility, greater financial integration. However, the advantages in terms of macro-economic efficiency of a monetary union may be offset by reduced macro-economic flexibility. Countries joining a monetary union lose their ability to stabilize production through an independent monetary policy and are constrained to relinquish the flexibility of their nominal exchange rate. To sum up, in accordance with the traditional approach to the OCA theory, it is more advantageous for countries with very close trading and financial ties with foreign countries to join an OCA than for countries with asymmetric business cycles (Artis and Toro 2000). However, it is widely admitted that the net advantages of belonging to a monetary union are not the same for all member countries.

This paper also highlights some findings of the reconsideration of Optimal Currency Areas (OCA) theory 50 years from its birth, in light of recent advances in open economy macro and monetary theory (see in particular Yoshimi 2014; Corsetti 2008, 2009; Gali 2008; Woodford 2003; Obstfeld and Rogoff 1995, 1996). Indeed, the OCA theory has been revisited and certain foundations have been challenged in the light of recent advances in open economy macro and monetary theory.

Furthermore, economic literature underscores the prerequisite conditions for establishing a monetary union. It is commonly admitted that the process of establishing a monetary union is long and complex. It requires the fulfillment of a certain number of pre-conditions, namely: (i) a strong political commitment, legal and institutional reforms as well as the adherence of economic operators thereto; (ii) sustained macro-economic convergence; (iii) effective fiscal oversight and discipline; (iv) monetary coordination; (v) significant integration of the financial sector; (vi) sustained commercial and economic integration; (vii) building the capacity of national and regional institutions involved in the process; and (viii) a well formulated strategy for transition towards a single currency.

Generally, the timeframes set by African RECs to complete the integration of their financial and monetary system seem to be too ambitious, the more so as the history of the EU shows that a very long period is needed to attain the ultimate stage of single currency.

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1. See Section II.
4. See Section II.
Likewise, the ASEAN countries, despite a more sustained commercial and economic integration than that observed in the various regions of the continent, consider that monetary integration is a long process and that they do not yet fulfil the conditions for an Optimal Currency Area or a Monetary Union.\footnote{Ong Keng Yong, Secretary-General of ASEAN at the Economic 2004 Conference, “Towards ASEAN Financial Integration”, University of Indonesia, Jakarta, 18 February 2004.}

The Euro Zone example reveals in particular that even though it is not absolutely necessary to fulfil all the conditions set forth by the OCA theory, some minimum prerequisite conditions (such as an adequate degree of trade and economic integration, a relative similarity of supply and demand shocks and business cycles, a relatively advanced financial system and market integration, and a synchronization of inflation rates) should precede the establishment of a monetary union and the introduction of a single currency. Beyond these minimum conditions, the Euro Zone example also shows that the establishment of a monetary union is facilitated when there is prior monetary coordination and a sufficient degree of regional financial integration. Therefore, the Euro Zone model should incite African RECs to adopt a cautious and gradual approach towards monetary union by fulfilling some minimum prerequisite conditions (such as a sufficient degree of trade and economic integration, a relatively advanced financial system and market integration, and an adequate level of monetary cooperation to provide a base for vibrant coordination of monetary and trade policies). Indeed, in the light of the experience of the Euro area, it has been shown that the adoption of a common currency has fostered European economic integration and given many European countries the benefits of low inflation and financial stability. It is well understood, however, that a single monetary policy cannot deliver efficient business cycle stabilization at national level, relative to an ideal benchmark in which region-specific monetary policy stabilizes domestic output gaps and marginal costs (Corsetti 2008). Moreover, more recent research also shows that it cannot generally be concluded that there is no cost of currency integration under labor mobility, as discussed in the classic Optimum Currency Area theory (Yoshimi 2014).

The present report has assessed the on-going monetary coordination and financial sector integration processes, as preliminary stages towards monetary union in both the West African Monetary Zone (WAMZ) and the East African Community (EAC) which actively engaged preparations with a view to building a monetary union, in light of theory and past experience. The two regions have been selected given the main following factors: (i) a limited number of Member States, which should facilitate the process, given the Euro Zone experience; (ii) the existence of strong political commitment, legal and institutional reforms; (iii) the existence of macro-economic convergence criteria; (iii) the significant integration of the financial sector; (iv) the existing degree of trade and economic integration; (v) the existence of regional institutions involved in the monetary integration process; and (vi) the existing strategy for transition towards a single currency.

The report did not analyse the overall monetary integration process in both regions. Specifically, the report dwelled on close linkages between monetary coordination and financial sector integration for sustaining the monetary integration process. Thereafter, the report made concrete proposals aimed at sustaining the monetary coordination and financial sector integration process with a view to building a monetary union in both sub-regions. The report also outlined potential areas for intervention by the African Development Bank and other key development partners.

\footnote{Liberia joined the WAMZ on 1st January 2010.}
\footnote{The new 2015 date was adopted at the 24th meeting of the Convergence Council of Ministers and Governors of the West African Monetary Zone in Abuja Monday June 22nd.}
West African Monetary Zone (WAMZ)

The establishment of an economic and monetary union has been a long-standing ambition of ECOWAS (Economic Community of West African States). In 1999, the ECOWAS adopted a two-pronged approach to the implementation of the ECOWAS integration programme. A second currency area in West Africa, known as the West African Monetary Zone (WAMZ), was established in 2000, with a view to achieving economic integration and a monetary union among the five non-member countries of the West African Economic and Monetary Union (WAEMU). This strategy has contributed to giving a fresh impetus to the implementation of the ECOWAS Monetary Cooperation Programme (EMCP).

The West African Monetary Institute (WAMI) was established by the Authority of Heads of State and Government of five West African Member States (The Gambia, Ghana, Guinea, Nigeria and Sierra Leone) in December 2000 and was launched in March 2001, to provide technical guidelines for conducting the integration process within the West African Monetary Zone (WAMZ).

However, the launch of the monetary union among WAMZ member countries was successively rescheduled three times (January 2003, July 2005 and December 2009) as a result of inadequate preparation. With respect to the revised plans, WAMZ hopes to adopt a single currency called “ECO” by 2015. This objective, like previous ones, may not be achieved if the member countries fail to establish effective monetary coordination and financial integration and other prerequisite conditions prior to the said date, in spite of progress recorded in other areas. While monetary union was yet to be actualised due to the challenges encountered by the Member States, some achievements were registered in the areas of policy harmonisation and institutional development in the zone (WAMZ 2013).

The inadequate preparation, inappropriate sequencing of reforms and unrealistic schedules, which inevitably led to successive postponements, have greatly undermined the credibility of the process towards monetary integration among WAMZ member countries. Therefore, the WAMI and other regional institutions should set priorities and adopt a pragmatic, gradual and realistic approach to facilitate and foster the adoption of reforms and gradually restore confidence in the process.

To do so, the capacity of WAMI should be strengthened to enable the Institute to play an effective role as a platform for intense cooperation between the central banks in the WAMZ. In addition, it is strongly recommended that technical cooperation ties between the Institute and national central banks in the region be strengthened.

East African Community (EAC)

The East African Community (EAC), established by a Treaty in 1999 between the founding members States (Kenya, Tanzania and Uganda) aimed at creating a customs union, a common market, a monetary union and ultimately a political federation. The EAC was expanded in 2007 to include Rwanda and Burundi, which undertook to implement measures relating to the Common External Tariff (CET) and internal customs duties in accordance with the membership schedule. The Community will eventually spread to include South Sudan and Somalia if they are admitted.

To foster regional economic and financial integration among EAC Partner States, an institutional framework and a range of policies have been put in place. Outstanding progress has been achieved towards economic integration. To attend the progress registered in the economic integration process, the EAC is also committed to realizing the successive stages of the establishment of a monetary union. In August 2007, the EAC Heads of State Summit decided to speed up...
the implementation of the monetary union, by bringing forward the initial launching date from 2015 to 2012.

However, progress in the monetary cooperation and financial integration process has been slow, thereby reflecting difficulties in the implementation of sub-regional programmes and initiatives, as well as major challenges to financial and monetary integration in the sub-region. In fact, the existence of political impetus and sub-regional institutions to buttress the economic and financial integration process did not lead to in-depth monetary coordination and financial integration within the EAC. However, significant progress has been recorded with a view to fostering the development of an integrated and competitive sub-regional financial system; the gradual implementation of coordinated monetary and financial policies and a cross-border financial infrastructure have contributed to the financial and monetary integration process. Furthermore, efforts made with a view to signing a monetary protocol tie with that process.

Moves toward deeper economic integration among the countries of the East African Community (EAC)—Burundi, Kenya, Rwanda, Tanzania, and Uganda—have gained new impetus from agreements sealed in November 2013. The signing of a Monetary Union Protocol by community heads of state in Kampala, Uganda, on November 30 is a milestone outlining a ten-year roadmap toward monetary union, which is a more realistic deadline. The formal launch of the East African Cross Border Payment System on November 25 is a significant operational step increasing monetary and economic integration (Mira 2013). The ratification of the monetary union, the third pillar of integration is set for July 2014 to pave way for the use of a common currency.

The current stage is considered as a preliminary phase of establishing financial and monetary integration. The degree of economic convergence, monetary coordination and integration of financial systems are still insufficient for launching an effective and sustainable monetary union within the stipulated timeframes.

The report under consideration lays emphasis on the need to strengthen monetary coordination and the integration of financial systems in order to strengthen on-going efforts at the sub-regional level and buttress on-going and scheduled assistance by the Bank and other development partners.

The report relies on the pivotal and primordial role played by central banks in the development, integration and stability of financial systems and proposes a pragmatic and gradual approach to monetary coordination and regional financial integration necessary for an effective and sustainable implementation of a monetary union. Furthermore, the report asserts that the basic prerequisites for financial integration and laying the groundwork for a sound and sustainable monetary union may only be achieved if human and institutional capacities are developed in a sustainable and coordinated manner.

The report also advocates that the very ambitious goals for launching a monetary union may prompt member States to speed up the implementation of requisite policies and reforms. However, they may also entail the risk of postponements and, consequently, undermine the credibility of the process, thereby considerably weakening the support of market participants and the general public, which is needed for the entire process. The EAC countries that are also engaged in the process of launching their monetary union in 2014 should learn from the failures of WAMZ.

While appreciating the roles currently played by the High Level Task Force (HLTF) in charge of negotiating the monetary protocol precedent to the establishment of EAMI and the EAC Secretariat which is coordinating this exercise, the report has suggested the establishment of a Permanent Technical Secretariat (PTS) as a technical team and a non-formal institution, which will provide and coordinate the necessary technical support and assistance to the national central banks given the primordial and pivotal role played by central banks in the monetary union process. The report did not suggest to replace the existing structure by the PTS.
but to reinforce this structure. Therefore, the PTS will work very closely with the existing institutions, namely the HLTF and the EAC Secretariat, in order to advance the monetary integration process in the EAC. The report has also suggested to coordinate capacity building in monetary and financial areas.

The Eurozone Crisis and Lessons for the Formation of the EAC and WAMZ Monetary Unions

The Eurozone crisis presents some critical lessons for developing countries, particularly in Africa. The Eurozone crisis has threatened to disorganize the European monetary integration model that Africa sought to imitate. The euro zone crisis is a vital case study for African RECs, in particular for the East African Community and West African Monetary Zone partner states as both regional blocs progressively move to unveil a monetary union.

Conclusions and Recommendations

The report’s overall assessment is that unrealistic schedules, which inevitably lead to the postponement of deadlines, may undermine the credibility of the monetary union, and considerably weaken the support of market participants and the public, which is necessary for the entire process. Consequently, both regions (EAC and WAMZ) should adopt a realistic, pragmatic and gradual approach to conducting the financial and monetary integration process. The report has suggested a few concrete solutions that contribute to fostering the integration process in both regions.

The above review has revealed various areas where donor assistance could advance monetary coordination and regional financial integration in the two regions studied here. These areas, which relate to monetary integration strategy in general, financial infrastructure, and financial institutions and policies, are categorized within four broad categories: (i) Policy Action Frameworks, (ii) Capacity Building /Governance, (iii) Advocacy, and (iv) Finance. Obviously, these areas will need further discussion among the Bank, the two sub-regions, member countries, and other development partners.
I. INTRODUCTION

1. BACKGROUND TO THE REPORT

The Abuja Treaty establishing the African Economic Community (AEC), which entered into force on 12 May 1994, laid down the phases and schedule for consolidating economic integration at the sub-regional level. The African integration strategy is based on the gradual integration of activities of Regional Economic Communities (RECs) - continental components of the AEC, committed to gradually establishing an economic union in their respective sub-regions in accordance with the objectives of the Abuja Treaty. Regarded as the building blocks of economic integration at the continental level, the RECs pursue a gradual objective geared towards attaining the ultimate stage of economic and monetary union.

2. OBJECTIVES OF THE REPORT

The purpose of the report is to assess the on-going monetary coordination and financial sector integration processes, as preliminary stages towards monetary union, both in the West African Monetary Zone (WAMZ) and the East African Community (EAC) which actively engaged preparations with a view to building a monetary union, in light of theory and past experience. The two regions have been selected given the main following factors: (i) a limited number of Member States, which should facilitate the process, given the Euro Zone experience; (ii) the existence of strong political commitment, legal and institutional reforms; (iii) the existence of macro-economic convergence criteria; (iv) the existing degree of trade and economic integration; (v) the existence of regional institutions involved in the monetary integration process; and (vi) the existing strategy for transition towards a single currency. The report does not analyse the overall monetary integration process in both regions. Specifically, the report dwells on close linkages between monetary coordination and financial sector integration for sustaining the monetary integration process. Thereafter, the report makes concrete proposals aimed at sustaining the monetary coordination and financial sector integration process with a view to building a monetary union in both sub-regions. The report also delineates potential areas for intervention by the African Development bank and other key development partners.

3. PLAN OF THE REPORT

To do so, the paper first examines how monetary coordination and regional financial integration address monetary integration challenges and how the Optimal Currency Area (OCA) theory could address these problems? (Section II). The third and fourth sections are devoted to the assessment of progress and challenges and the concrete proposals towards monetary coordination and financial integration within both regions respectively. Finally, the fifth and last section concludes the report in highlighting the main recommendations and areas for intervention by the African Development bank and other key development partners.
II. HOW COULD MONETARY COORDINATION AND REGIONAL FINANCIAL INTEGRATION ADDRESS MONETARY INTEGRATION CHALLENGES AND HOW THE OPTIMAL CURRENCY AREA (OCA) THEORY COULD ADDRESS THESE PROBLEMS?

1. MONETARY COORDINATION IN THEORY

It is important to specify the meaning of monetary coordination and regional financial integration as used in this report. Monetary coordination may be broadly defined to include, for instance, consultations between monetary authorities regarding the harmonization of monetary policies and exchange rates, and the sharing of information needed to support such harmonization. Cooperation is sometimes used interchangeably with the term coordination in the monetary field. However, (monetary) cooperation refers to policy measures implemented to facilitate cross-border trade and financial flows by removing frictions and obstacles. In this perspective, the definition of monetary coordination is more specific than that of monetary cooperation given above. Coordination implies the adoption of mutually agreed policy guidelines by various monetary authorities. Maintaining a distinction between cooperation and coordination, and adopting a broad definition of monetary cooperation contributes to explaining that the latter - like monetary integration - is an evolving process wherein lower levels of monetary cooperation may provide a base for vibrant coordination of monetary and trade policies.

2. REGIONAL FINANCIAL INTEGRATION IN THEORY

The measure of financial integration is both complex and multidimensional. Kawai and Motonishi (2005) use three aggregated measures for financial integration: measures are based on prices (interest rate parity, PER of stock markets), quantity-based measures (correlations between savings and investment, current account dynamics, trade and investment flows), and investment-based regulatory measures (financial infrastructure, trade control). As observed by Brouwer: “… market integration presupposes an increase in transactions on such markets and a price convergence trend in terms of single currency; integration may also radically alter the dynamics of this process. Financial integration is simply the application of this process to markets in financial instruments.” It is worth noting that such harmonization of prices is not as a result of set objectives, contrary to the case of convergence criteria where certain objectives have been set.

In other words, regional financial integration (RFI) refers to a process of broadening and deepening financial ties in a region. It refers to initiatives aimed at broadening and deepening financial systems within a region via the market or institutions, and at establishing an integrated financial system. RFI can be attained by removing obstacles to cross-border financial flows and investments and granting special concessions to investors in the region, and can also enable the harmonization of legal frameworks, policies and institutions, with a view to fostering the integration of national financial markets into an integrated regional financial market.

Given that most African financial markets are small and fragmented, their consolidation via RFI offers numerous theoretical advantages, including: (i) overcoming diseconomies caused by small financial markets (limited competition, innovation and efficiency of national financial systems; limited economies of scale; high costs of financial infrastructure, etc.); (ii) improving the supply of financial products and services; (iii) increasing savings and financial resources; (iv) developing larger-scale investment projects; and (v) expanding risk diversification opportunities. Furthermore, RFI may contribute to improving the efficiency of regulatory and

supervisory organs of the financial system, protecting central banks against domestic excesses, harmonizing legislations, and improving the efficiency of regional institutions.

3. MONETARY INTEGRATION IN THEORY

Monetary integration is a step above monetary coordination and financial integration, where Member States establish a single currency and central bank, and thus relinquish their sovereignty in monetary policy and trade policy which are currently determined by a “supranational” central bank. One of the fundamental issues consists in determining whether member States together form an area conducive to a single currency, and if other conditions precedents to a successful monetary union have been laid down.

4. DO MONETARY COORDINATION AND SUSTAINED FINANCIAL INTEGRATION IMPLY THAT A REGION IS CLOSER TO AN OCA OR DO THEY FOSTER MONETARY INTEGRATION?

Basically, monetary coordination and financial integration imply sustained capital mobility and a loss of autonomy over monetary policy and exchange rate flexibility. In such a case, the creation of a common regional currency cannot be very costly and may provide participants a certain number of micro-economic advantages. As asserted previously, these advantages should be attended by a drop in macro-economic costs and a higher degree of trade integration and symmetry of business cycles.

5. FINANCIAL INTEGRATION AS AN IMPORTANT ELEMENT OF ANY REGIONAL INTEGRATION PROCESS, AND PARTICULARLY FOR A MONETARY UNION

The financial sector should be adequately prepared to promote financial inclusion and foster the transition to a new currency. The financial sector itself is at the core of the market economy, given that it plays a key role in savings and investment intermediation. The depth and quality of an integrated financial market may also further widen the range of savings and investment choices, thereby facilitating economic growth in the monetary zone.

With the help of theoretical analyses developed in this section, the following two sections analyze the monetary coordination and regional financial integration process within the West African Monetary Zone (WAMZ) and the East African Community (EAC), respectively, and make recommendations with a view to deepening that process.

6. KEY FINDINGS OF THE REVIEW OF ECONOMIC LITERATURE ON THE COSTS AND ADVANTAGES OF AN ECONOMIC AND MONETARY UNION

There is abundant economic literature on the costs and advantages of an economic and monetary union at the theoretical and empirical levels, based particularly on the case of the European Economic and Monetary Union (EMU). Some of the findings from such literature are summarized below:

• Traditional literature on the Optimal Currency Areas (OCA) theory14, developed by Mundell (1961)15 and McKinnon (1963)16, posit that member countries of a monetary union will benefit from lower transaction costs emanating from trading goods and assets in foreign currency. Lower transaction costs should improve foreign trade and hence generate greater advantages that lead to economic specialization.

• Recent empirical data highlight the significant positive impact of monetary unions on trade (Rose 2000, Glick and Rose 2001) and income (Frankel and Rose 2002). However, other authors underscore the fact that such impact is obviously underestimated on account of the sample used and the absence of lineairties (Persson 2001), and the endogeneity of the decision to join the union (Tenreyro 2001).

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14. See Section II.
The other possible advantages in terms of macroeconomic efficiency for joining a monetary union are the elimination of (or significant reduction in) nominal exchange rate volatility and hence lower interest rates, low real exchange rate volatility, greater financial integration, and in the case of joining a zone with a dominant currency (such as the EURO), global acceptance of the single currency.

However, the advantages in terms of macroeconomic efficiency of a monetary union may be offset by reduced macroeconomic flexibility. Countries joining a monetary union lose their ability to stabilize production through an independent monetary policy and are constrained to relinquish the flexibility of their nominal exchange rate. To sum up, in accordance with the traditional approach to the OCA theory, it is more advantageous for countries with very close trading and financial ties with foreign countries to join an OCA than for countries with asymmetric business cycles (Artis and Toro 2000).

For countries seeking membership of a monetary union, the increase in macro-economic advantages is attended by a reduction in macro-economic costs, combined with an increase in the level of commercial integration and symmetry of business cycles. Empirical studies in the case of the EU show that countries with more closely integrated economies exhibit strongly correlated business cycles.

The OCA criteria are dynamic: the net advantages of integration into a monetary union for member countries increase upon joining the union, given that commercial integration and the correlation of business cycles are stronger as compared to the period prior to membership of the Union (Frankel and Rose 1998, 2002, Rose and Engel, 2001).

The modern reconsideration of the theory of Optimal Currency Areas (OCA) (see in particular Corsetti 2008 and 2009; Yohimi 2014)

However, it is widely admitted that the net advantages of belonging to a monetary union are not the same for all member countries.

Furthermore, economic literature underscores the prerequisite conditions for establishing a monetary union. It is commonly admitted that the process of establishing a monetary union is long and complex. It requires the fulfilment of a certain number of pre-conditions, namely: (i) a strong political commitment, legal and institutional reforms as well as the adherence of economic operators thereto; (ii) sustained macroeconomic convergence; (iii) effective fiscal oversight and discipline; (iv) monetary coordination; (v) significant integration of the financial sector; (vi) sustained commercial and economic integration; (vii) building the capacity of national and regional institutions involved in the process; and (viii) a well formulated strategy for transition towards a single currency.

Generally, the timeframes set for the various regions of the continent to complete the integration of their financial and monetary system seem to be too ambitious, the more so as the history of the EU shows that a very long period is needed to attain the ultimate stage of single currency. Likewise, the ASEAN countries, despite a more sustained commercial and economic integration than that observed in the various regions of the continent, consider that monetary integration is a long process and that they do not yet fulfil the conditions for an Optimal Currency Area or a Monetary Union.

17. See Section II.
Box 1: The realization of Economic and Monetary Union (EMU) in the European Union

June 1989: Political agreement by the EU Member States on the realization of EMU in three stages

July 1990 to end-1993: Stage 1 of EMU within the then existing institutional framework of the Community, focusing on completing the Single Market (introduced by the Single European Act of 1986), reducing disparities between Member States’ economic policies, removing all obstacles to financial integration and intensifying monetary cooperation

Nov 1990 to Feb 1992: Negotiation and eventual signing of the Treaty on European Union (the “Maastricht Treaty”) specifying the legal and institutional framework for EMU, the means and procedures for its achievement and the commitments made by the EU Member States in this respect

November 1993: Entry into force of the “Maastricht Treaty” following ratification by all EU Member States

January 1994: Start of Stage 2 of EMU and establishment of the European Monetary Institute (EMI)

June 1998: Establishment of the European Central Bank (ECB), forming, together With the NCBs of the participating EU Member States, the Eurosystem

1999: Start of Stage 3 of EMU (with 11 out of the 15 EU Member States participating), irrevocable fixing of conversion rates, conduct of a single monetary policy and introduction of the euro as scriptural money for monetary and financial purposes

January 2002: Introduction of euro banknotes and coins and legal changeover to the euro as the single currency of the euro area This means that in the case of the European Union it took: three years from the political agreement to realize EMU to the signing of the legal framework for EMU; seven years (1992 to 1999) from the signing of the legal framework for EMU to the start of Stage 3 of EMU; and 13 years from the political agreement to realize EMU to the final completion of the undertaking. These years were fully used by the EU Member States to reach the necessary degree of economic and legal convergence and by the Community bodies (in particular the EMI) to complete the necessary preparations for the start of EMU and the eventual changeover to the euro as the single currency of the euro area.


7. THE OPTIMAL CURRENCY AREA THEORY AND ITS RECONSIDERATION

a. Rationale for Optimal Currency Areas

The assessment of the soundness of a monetary union has been considered by economic theory and has been the subject of academic discussions. The dominant theory on the debate relating to monetary integration and the Optimal Currency Area (OCA) was developed in the 1960s, principally by Robert Mundell23, who deals with the central issue of knowing under what conditions a monetary union is ideal.

The Optimal Currency Area theory attempts to assess the soundness of a monetary union among different countries. Such monetary union is supposed to produce economic benefits, for instance the elimination of transaction costs. However, it implies that member countries will each forfeit their own individual monetary policy. Consequently, it presupposes that countries will relinquish the value-regulatory mechanism of their currency, particularly in such a manner as to influence the exchange rate between the latter and foreign currencies. Hence, member countries of a monetary union give up their instrument of adjustment to asymmetric shocks24 25. Consequently, the OCA theory will endeavour to lay down conditions under which a monetary union should be able to circumvent the adverse impacts of a fixed exchange rate, while benefitting from the benefits incidental to a single currency policy26.

The key (traditional and endogenous) criteria of the OCA theory are summarized below.

b. Traditional Criteria of an Optimum Currency Area

The theory of Optimum Currency Areas, in the traditional approach adopted in the 1960s with major contributions from Mundell (1961), McKinnon (1963)27 and Kenen (1969), endeavoured to model the cost-benefit calculation whereby countries could have decided whether or not to establish a monetary union.

24. Shock that does not affect countries of the same area the same way
Therefore, the countries should create a currency area with the expectation that current and future benefits will outweigh costs. In this approach, an OCA is defined as an optimum geographical area wherein there is a single currency, or several currencies, whose exchange rates are irrevocably pegged to one another. The single currency, or the various indexed currencies, may only fluctuate in unison against the rest of the world. Hence, the soundness of the decision whether or not to join a monetary union is assessed in light of three key criteria designed by the theory and which may be summarized as follows:

- Magnitude of asymmetric shocks;
- Efficiency of adjustment mechanisms;
- Structural characteristics of economies.

1) Mobility of Factors of Production

Mundell (1961) defined mobility of production factors, including labour, as the first criterion. He distinguishes a first case, wherein exchange rates are flexible, from that of the monetary union. In case of asymmetric shocks, if demand shifts from one country to another, it will entail unemployment in the first country and inflation in the second. Currency devaluation in the affected country will then allow for a readjustment of the situation. Under circumstances where currency devaluation is impossible, only a mobility of factors that is stronger within the monetary union than without will help counterbalance the absence of flexible exchange rates.

Furthermore, Mundell also underscored the importance of real political determination in successful monetary union building: “Of course, in the real world, currencies are mainly the expression of national sovereignty. Hence, monetary reorganization will only be possible if attended by profound political changes.”

2) Extent of Openness of Economies

The second criterion, emphasized by McKinnon (1963), is the extent of economic openness. McKinnon introduces a new concept, namely the ratio between tradable and non-tradable goods. Only the former are affected by import or export levels, whereas the prices of non-tradable goods depend on the domestic currency. However, in an open economy, where the ratio is high, any change in exchange rate results in an almost equivalent change in import or export prices, which therefore tend to be reflected on all prices (including those of non-tradable goods). McKinnon considers that the more countries are open to the outside world, the less they stand to lose by adopting a fixed exchange system, given that the extent of openness of an economy is measured by the share of tradable goods (exported goods + imported goods) in that economy’s total production. Consequently, the nominal exchange rate would be less useful as an instrument of adjustment for small open economies.

3) Specialization and Sector Diversification

The third criterion relating to the extent of specialization and sector diversification was proposed by Kennen (1969). He lays emphasis on the extent of diversification of the productive fabric of countries intending to establish a fixed exchange area. In his opinion, diversified economies may do without the exchange rate instrument and create an optimum currency area. The more diversified the economic fabric is, the lesser the risk of it being affected by a specific shock (internal or external). Hence, diversification reduces the need for changes in the terms of trade through the nominal exchange rate and constitutes a safeguard against all sorts of disruption. Highly diversified partner countries are more likely to find a single currency beneficial.

c. Endogenous OCA Criteria

The OCA theory, which had declined throughout the 1970s and 1980s, has been rethought since the late 1990s, obviously under the influence of the establishment of the EURO zone which is an instance of the application of economic doctrine. The new approach, labelled endogenous criteria, postulates that the monetary union auto-generates conditions for its optimization.

Indeed, traditional criteria may change over time. They are endogenous to the functioning of the monetary zone; it is important to assess them ex post. These secondary criteria may be defined as:

- Homogeneous preferences;
- Trade and economic integration;
- Price and salary flexibility;
- Similarity in supply and demand shocks and business cycles;
- Fiscal transfers;
- Financial market integration;
- Similarities in inflation rates;
- Etc.

1) Homogeneous Preferences

Cooper (1977) and Kindleberger (1986) developed the homogeneous preferences criterion. For both authors, a monetary union is primarily a social good which presupposes that its functioning is predicated on the convergence of the economic policy objectives of the various governments, particularly with respect to inflation.

2) Trade and Economic Integration

Frankel and Rose (1998) have demonstrated that the monetary union fostered trade integration among member countries, and hence their openness, and thereby reduced the risk of future asymmetric shocks. Furthermore, according to Fontagné and Freudenberg (1999), the economic integration of industrial countries essentially entails intra-industry specialization, which, in the Kenen tradition, is conducive to the monetary union.

3) Price and Salary Flexibility

Whenever nominal prices and salaries are flexible in and among countries envisaging a single currency, the transition to post-shock adjustment is less likely to be associated with lasting unemployment in a country and/ or inflation in another. This reduces the need for nominal exchange rate adjustment. In such a case, the loss of direct control on the nominal exchange rate instrument should not represent a cost. Price and salary flexibility is particularly important in the very short term, when the mobility of factors is partly limited, to facilitate the post-shock adjustment process.

4) Similarity in Supply and Demand Shocks and Business Cycles

Another essential criterion is the similarity in supply and demand shocks and business cycles in countries using a single currency. Monetary policy and exchange rate may not be used as a stabilization instrument if one member country is, for instance, affected by an asymmetric shock. Consequently, the business cycles of the countries considering the establishment of a currency area should be correlated to the maximum.

5) Fiscal Transfers

Fiscal transfers help to make up essentially for the absence of market-driven adjustments. The intention here is to redistribute financial resources mainly from richer to relatively poorer countries or from countries hit by a positive shock to those hit by a negative shock. Admittedly, both objectives could be incompatible: a

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country hit by a positive shock could be at the same time a relatively poorer country. Furthermore, the fiscal transfer system requires a certain degree of political integration.

6) Financial Market Integration

The integration of financial markets is an essential criterion which helps to reduce the need for exchange rate adjustment. It helps to moderate temporary adverse disturbances related to capital inflows (by borrowing from surplus areas or de-cumulating net foreign assets which could be reverted once the adverse shock is over). Under a high degree of financial integration, even slight interest rate adjustments could elicit equilibrating capital movements across partner countries. This would reduce differences in long-term interest rates, thereby easing the financing of external imbalance as well as fostering an efficient appropriation of resources.

7) Similarity in Inflation Rates

Similarity in inflation rates is also necessary for the establishment of an optimum currency area. External imbalances may ensue from persistent differences in national inflation rates, due especially to disparities in structural changes; diversity in labour market institutions, differences in economic policies and diverse social preferences. When inflation rates between the countries are relatively close over time, the terms of trade should also be relatively stable. This would foster a more balanced current account and trade among member countries, and should therefore curb the need for nominal exchange rate adjustment.

d. Application of the Optimum Currency Area Theory to the Euro Zone and lessons for the West African Monetary Zone (WAMZ) and the East African Community (EAC)

Economic opinions differ on the optimality of the Euro Zone. An analysis of the Euro Zone from the OCA theory point of view shows that it is not an Optimal Currency Area. Nevertheless, it possesses several mitigate elements that portend good tidings for its future.

European economies remain subject to asymmetric or regional shocks. Price and salary flexibility is deemed too weak. Similarly, labour mobility is also very weak and undermined by numerous restrictions. Inadequate budget transfers do not allow for a return to equilibrium and there is no federal budget that enables income transfers capable of mitigating asymmetric shocks.

Nevertheless, there are several elements in favour of the optimality of the Euro Zone as well as great potentials that augur well for its brighter future and subsequent attainment of optimality. Indeed, the Euro Zone will provide a strong incentive for cooperation among member countries. There is little absolute convergence, but rather conditional convergence, within the European Union. For instance, the Euro Zone implies the convergence of the economic results and policies of countries wishing to join the European single currency whose objective is to contribute to optimizing performance through price stability. In addition, it is worth noting that the economies of the six founding countries of the EEC (European Economic Community) develop in a relatively homogenous manner over time and their cycles are rather well inter-correlated. Hungary, Poland and Slovenia exhibit cycles that are better correlated with the core of the EU than those of some small countries already existing in the Euro Zone.

In comparison, the member countries of both sub-regions (West African Monetary Zone and East African Community) are far from achieving the above mentioned OCA Criteria, do not develop in a relatively homogenous manner over time and their cycles are not well inter-correlated.

However, the Euro Zone crisis, which began with the Greek crisis in 2010 and continued with the Irish crisis in the autumn of 2010, lays bare the limitations of Euro Zone governance and prompts both institutional innovations and numerous reform proposals that are under discussion.

The Euro Zone example reveals in particular that even though it is not absolutely necessary to fulfill all the conditions set forth by the OCA theory, some minimum prerequisite conditions (such as an adequate degree of trade and economic integration, a relative similarity of supply and demand shocks and business cycles, a relatively advanced financial system and market integration, and a synchronization of inflation rates) should precede the establishment of a monetary union and the introduction of a single currency. Beyond these minimum conditions, the Euro Zone example also shows that the establishment of a monetary union is facilitated when there is prior monetary coordination and a sufficient degree of regional financial integration.

Therefore, the Euro Zone model should incite the two sub-regions to adopt a cautious and gradual approach towards monetary union by fulfilling some minimum prerequisite conditions (such as a sufficient degree of trade and economic integration, a relatively advanced financial system and market integration, and an adequate level of monetary cooperation to provide a base for vibrant coordination of monetary and trade policies).

Furthermore, as observed by Kim (2007), it should be taken into account that the establishment of a monetary union with single currency is likely to stimulate trade integration and thus improve ex-post the conditions for a monetary union.

More recent work on the OCA (Corsetti, 2008 and 2009) posits that factors supporting monetary integration are financial sector integration (especially financial markets development and integration) and counter-cyclical fiscal policy, which are both high among priorities of the WAMZ and EAC policymakers.

e. The reconsideration of the Optimal Currency Areas (OCA) theory

In light of recent advances in open economy macro and monetary theory, some of the foundations of the Optimal Currency Areas (OCA) theory have been reconsidered 50 years from its birth. This reconsideration notably led to the main following conclusions:

- Aggregate welfare losses from monetary unification are found to be small — arguably smaller than the benefits from joining a disciplined currency area for countries without a stable and efficient macroeconomic policy (including fiscal policy) framework;

- Specialization in production and asymmetric cyclical shocks do not necessarily make a common monetary policy less efficient than nationally differentiated policies, for two reasons: (i) exchange rate movements do not necessarily perform the stabilizing role envisioned by the traditional theory, and most importantly, monetary unification may foster processes of convergence in the composition of spending at national level (see Corsetti 2008 and 2009);

- It cannot generally be concluded that there is no cost of currency integration under labor mobility, as discussed in the classic Optimum Currency Area theory (Yoshimi 2014).
III. WEST AFRICAN MONETARY ZONE

1. HISTORICAL BACKGROUND AND PROCESS OF MONETARY COORDINATION AND REGIONAL FINANCIAL INTEGRATION WITHIN THE WEST AFRICAN MONETARY ZONE

The establishment of an economic and monetary union has been a long-standing ambition of ECOWAS (Economic Community of West African States). The objective of the ECOWAS Treaty is “cooperation and integration leading to the establishment of an economic union in West Africa, with a view to raising the living standards of its people, while maintaining and enhancing economic stability, fostering relations among Member States and contributing to the progress and development of the African continent”\(^{40}\).

The ECOWAS programme for West African integration comprises: ECOWAS free trade scheme (EFTS), ECOWAS Monetary Cooperation Programme (EMCP); free movement of persons, development of regional transport and communication networks, strengthening the production base and harmonization of macro-economic policies of Member States.

However, the EMCP, set up in 1987 with the objective of establishing a single currency area in the sub-region, failed to achieve its set objective for numerous reasons, including political and economic difficulties faced by some Member States. The start-up of the EMCP was initially scheduled for 1992, but was postponed by the ECOWAS Heads of State and Government to 2000. Given also that the 2000 timeframe was obviously too ambitious, the regional authorities decided once more, during their meeting in Lomé, Togo, in December 1999, to adopt a two-pronged approach to the implementation of the ECOWAS integration programme. A second currency area in West Africa, known as the West African Monetary Zone (WAMZ), was established in 2000, with a view to achieving economic integration and a monetary union among the five non-member countries of the West African Economic and Monetary Union (WAEMU). This strategy has contributed to giving a fresh impetus to the implementation of the ECOWAS Monetary Cooperation Programme\(^{41}\).

Consequently, it is envisaged that the WAMZ single currency would run concurrently with the CFA Franc of the WAEMU within the ECOWAS for an interim period before the creation of a single currency for the entire region. The ambition of the region is to consider monetary union as a major step in the integration efforts in West Africa. Authorities anticipate that a single currency will offer greater economic efficiency and stronger growth in the long run.

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\(^{40}\) Article 3 (revised) of the ECOWAS Treaty of 24 July 1993

\(^{41}\) WAMI, 2009: Monetary and Financial Integration in West Africa, Accra.
Box 2: Role and Functions of the West African Monetary Institute

The West African Monetary Institute (WAMI) was established by the Authority of Heads of State and Government of five West African Member States (The Gambia, Ghana, Guinea, Nigeria and Sierra Leone) in December 2000 and was launched in March 2001, to provide technical guidelines for conducting the integration process within the West African Monetary Zone (WAMZ). Since its inception, the WAMI has played a pioneering and pivotal role in this process. WAMI shall have the responsibility to implement the fast track action plan for monetary unification and establishment of the common central bank within the WAMZ, known as the West African Central Bank (WACB).

In accordance with its Statute, the Institute shall be responsible for: (i) monitoring the status of macro-economic convergence; (ii) harmonizing policy design and regulatory frameworks; (iii) fostering a regional payments system; (iv) recommending an exchange rate mechanism and conversion rate mechanism; (v) organizing a sensitization drive for the introduction of the new currency; and (vi) design and technical preparation of the new currency.

The Institute would also be responsible for the establishment of the Common Central Bank, including the design of the central bank’s legal framework and ancillary institutions, proposals for the selection of the Headquarters, methods of share capital contribution, physical infrastructure and formulation of guidelines for the selection and hiring of key officers. The Institute should create conditions conducive to a smooth transition to the new common currency by ensuring that regulations in all countries are consistent with the introduction of a new currency; prices are quoted in the new currency as well as any other practical issues that would facilitate the smooth introduction of the new currency, and the withdrawal of old currencies.

WAMI’s initial two-year work schedule was expanded in 2002 to focus on multilateral surveillance of macroeconomic convergence. The other aspects of the work schedule include technical, institutional and policy harmonization issues that are to be implemented in order to set up the common Central Bank.

The main elements of the work schedule are as follows: Multilateral Surveillance involving quarterly monitoring and assessment of country performance with respect to the convergence criteria; statistical convergence and harmonization; development of the payments system; harmonization of legal frameworks; design of the monetary policy framework and other policies; undertaking effective sensitization and monitoring of activities at the national level; and supervision of all institutional, legal and administrative activities in preparation for the commencement of operations of the common central bank.

To implement its ambitious work schedule, WAMI designed a strategic plan for 2010-2015.

Hence, the programme to establish a monetary union among member countries of the West African Monetary Zone (WAMZ) (Nigeria, Ghana, The Gambia, Guinea, Sierra Leone and Liberia), is an integral part of the project to create a single currency among ECOWAS member countries (comprising WAMZ and WAEMU43 member countries and Cape Verde). The launching date of the WAMZ single currency, initially scheduled for 2003, was postponed to July 2005, and then to December 2009. During the ECOWAS Heads of State summit in June 2007, leaders requested that a feasibility study on the launching of a single currency among WAMZ and WAEMU member countries by 2009 be conducted, thus by-passing the intermediate stage of two parallel monetary unions. However, in June 2009, the WAMZ Heads of State, citing the global financial crisis, agreed to further postpone the starting date for the WAMZ single currency to 2015 (and thereby establish the ECOWAS single currency by 2020). Furthermore, this postponement is due to insufficient macro-economic convergence and failure to implement all the legal and institutional measures necessary for the establishment of a single central bank. As the proposed date of 2015 for the launch of the second regional currency moves closer, the ECOWAS Commission and the ECOWAS Authority of Heads of State and Government, like other stakeholders, are concerned about the state of preparedness of the six Member States of the West African Monetary Zone (WAMZ) for 201544.

Hence, the objective of the WAMZ is to create an integrated currency area characterized by the existence

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42. See Annex 1.
43. Benin, Burkina Faso, Cote d’Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo.
of a single central bank and a single currency that will substitute the six existing national currencies. The West African Monetary Institute (WAMI)\textsuperscript{45} is one of the organs of the WAMZ that plays a crucial and pivotal role in this process.

2. PROGRESS AND CHALLENGES OF MONETARY COORDINATION AND FINANCIAL INTEGRATION WITHIN THE WEST AFRICAN MONETARY ZONE

a. Progress

Substantial progress has been recorded by WAMI and considerable changes have been observed in respect of integration of the economies of the zone. Progress has been registered especially in the following areas: (i) preparation of the institutional framework for the establishment of a monetary union; (ii) macro-economic surveillance; (iii) development and integration of national payments systems with a view to gradually establishing a regional payments system; (iv) statistical harmonization to support the macro-economic surveillance process; and (v) convergence of business cycles.

1) Preparation of an Institutional Framework for the Establishment of a Monetary Union

In spite of limited political commitment, the WAMZ has scored relatively significant progress with respect to institutional, legal and regulatory preparation. The West African Monetary Institute (WAMI) has registered progress towards the development of the institutional framework necessary for the establishment of a monetary union: draft statutes for the WAMZ Secretariat, the future Regional Central Bank (WACB), the future West African Financial Surveillance Authority (WAFSA), payments systems, approval for single economic space, non-banking financial institutions, the regional banking system that would allow for the harmonization of the banking laws of the various member countries, were drafted and prepared.

2) Strengthening Macro-economic Surveillance

Macro-economic surveillance activity undertaken by WAMI was strengthened to include: an overall assessment of economic changes in member States; analysis of short-term prospects, including an in-depth discussion on risks and vulnerabilities, and recommendation of corrective measures to be implemented in respect of problems and shortcomings identified.

3) Regional Payments System

Substantial progress has been made in the development of national payments systems and the smooth introduction of a regional payments system in the WAMZ with the support of the African Development Bank. In July 2008, the ADB Board of Directors approved an ADF grant of about USD 23 million to finance the development and improvement of payments systems in The Gambia, Guinea and Sierra Leone. The main component of the payments system improvement process in the three different countries includes the development of a Real Time Gross Settlement (RTGS) system\textsuperscript{46}. In addition to the RTGS system, the project should help the three countries in computerizing the other components of the payments system. In the wake of Liberia joining WAMZ, a supplementary grant was awarded to WAMZ, the project executing agency, for the development and improvement of Liberia’s payments system. The project should help to harmonize the payments systems in the six member countries of WAMZ, with a view to facilitating the process of launching a monetary union in the zone. As outlined by the WAMZ report, the project would be completed ahead of the stipulated completion dates if the implementation momentum and the commitment of the beneficiary countries were sustained (WAMZ, 2013).

4) Statistical Harmonization

The Institute has had close cooperation ties with ECOWAS since 2004 on a WAMZ statistical harmonization programme, and has registered progress

\textsuperscript{45} WAMI was launched in March 2011.

\textsuperscript{46} Real Time Gross Settlement (RTGS) system of payment: Nigeria and Ghana have already developed RTGS systems.
especially with the adoption of a single IPC classification system by WAMZ countries.

The goal here is to achieve uniformity of good quality statistics from member States to support the performance surveillance and macro-economic policy convergence process. Two major activities were chosen for greater attention, namely the harmonization of national accounts (in collaboration with ECOSTAT) and the harmonization of statistical consumer prices.

With regard to statistics, WAMI partnered with the AfDB on the data dissemination system being constructed for adoption by all African central banks as well as regional integration institutions. To this end, the AfDB engaged the services of a solution provider to train staff of the Institute on the management of the data platform (WAMZ 2013).

5) Integration of Financial Markets

Efforts are underway for the integration of the Nigeria and Ghana Stock Exchanges, a crucial stage in capital markets integration.

The Ghana Stock Exchange (GSE) and the Nigeria Stock Exchange (NSE) have already considered procedures for harmonization and integration. In 2003, both stock exchanges signed an Aide-memoire on several areas of cooperation. Quite recently, a GSE-NSE joint committee decided to consider the option to harmonize both stock exchanges.

This process is part of the integration process for capital markets in the ECOWAS, which effectively took off with the inauguration of the West African Capital Markets Integration Council (WACMIC), in Abuja, Nigeria, by the President of the ECOWAS Commission. Subsequently, a Charter was signed and adopted by the different Stock Exchanges and Securities and Exchange Commissions, respectively, in Cote D’Ivoire, Ghana, Nigeria and Sierra Leone (WAMZ 2013).

6) Reduction of Economic Distance in the WAMZ

By and large, even though the costs of membership of a monetary union are currently high for countries such as Sierra Leone and Guinea, a comparison of two sets of data drawn up by WAMI reveals that the costs of a monetary union corresponding to the WAMZ programme tend to drop, compared to the period preceding the launching of the WAMZ. Basically, the WAMZ programme has contributed to reducing economic distance measured by the production and inflation gaps between the country of destination and applicant countries. The long-term costs of forming a monetary union between Nigeria and the applicant countries are likely to decrease as the WAMZ programme is implemented systematically.

b. Challenges

In spite of progress achieved towards the future establishment of a monetary union among WAMZ member countries, the process is still undermined by numerous constraints and challenges, including: (i) weak progress toward the fulfilment of the prerequisite conditions for the establishment of a monetary union; (ii) tough constraints on monetary coordination and regional financial integration; (iii) WAMI’s limited human resources and technical capacity; (iv) weak coordination between WAMI and the central banks of the region.

1) Slow Progress towards the Fulfilment of the Prerequisite Conditions for the Establishment of a Monetary Union

With regard to the criteria set forth by the OCA theory and its recent reconsideration as well as other prerequisite conditions commonly required for the establishment of a monetary union, the latter is undermined by significant shortcomings, namely:

- Weak political will characterized particularly by the existence of border controls which hinder the free movement of goods, and a weak commitment to implementing relevant political decisions and protocols;
- Persistent macro-economic instability and weak macro-economic governance;
- Severe asymmetric shocks (such as shocks related

47. WAMI, 2009, Monetary and Financial Integration in West Africa, Accra.
to fluctuations in world oil prices) and weak mobility of production factors, including labour;
• Quasi-absence of adjustment mechanisms;
• Significant structural differences among the economies of the zone;
• Very weak trade and economic integration among countries of the region (mainly explained by the weak development of regional infrastructure and existence of some barriers to intra-regional trade);
• Dissimilarity between supply and demand shocks and business cycles;
• Low degree of integration of the financial market;
• Weak convergence of economic conditions (despite the positive change observed at the level of economic distance among countries of the zone).

2) Tough Constraints on Monetary Coordination and Regional Financial Integration

Such tough constraints manifest as:

• Low degree of harmonization or the quasi-absence of harmonization of monetary policies;
• Existence of divergence in exchange rate regulations that undermined the effective coordination of regional exchange rate policies;
• Poor harmonization of exchange rate regulations, capital account liberalization (which is translated especially by the existence of capital account restrictions)\(^{48}\), etc.;
• Inadequate progress in the harmonization of policies and regulations relating to the legislation and surveillance of the banking system and non-banking financial institutions, despite the development of cross-border banking and financial activities; and
• Ineffective harmonization of legal and operational frameworks for financial markets (including the Sierra Leone Stock Exchange\(^{49}\)).

3) WAMI’s Limited Human Resources and Technical Capacity

With regard to the responsibilities entrusted to WAMI, the Institute’s human resources do not seem to be sufficient for it to fulfil its missions.

Notwithstanding a well-established organizational structure, WAMI does not perform its duties under optimal conditions, due to discrepancy between its capacity and resources, and the scope of the missions entrusted to it. The Institute is placed under the leadership of a Director-General and comprises five departments: (i) Research, (ii) Operations, (iii) Finance and Administration, (iv) Internal Audit, and (v) Legal Affairs. WAMI is supervised by a Convergence Council of Ministers and Central Bank Governors.

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\(^{48}\) The ECOWAS Treaty provides for the free movement of capital through the removal of all barriers to capital transfer among member States. It is worth noting that most member countries eased exchange controls during the 1980s and 1990s. However, controls still exist with respect to the movement of capital and money market instruments, direct investments, real estate and the movement of personal capital. The countries of the zone are at different levels of liberalization: The Gambia and Liberia have completely liberalized their capital account. Ghana and Nigeria have registered significant progress in 2006-2008: both countries have enacted new policy laws and measures as well as new laws with a view to liberalizing their exchange rate markets, and have announced the removal of a wide range of controls in the exchange rate markets, in particular, on the maintenance of foreign exchange accounts, capital operations, money market transactions, loan transactions, in-coming and out-going direct investments and real estate transactions. The other countries adopted a prudent approach. 

\(^{49}\) Sierra Leone Stock Exchange.
4) Weak Coordination between WAMI and the Central Banks of the Region

Compared with the European Monetary Institute (EMI) which was also responsible for coordinating the monetary policy of the central banks of participating member States within the European Central Banks System (ECBS) and thus preparing what was known as the third phase of the Economic and Monetary Union (establishment of the European single currency), WAMI does not play such a role.

This shortcoming ensues from WAMI’s weak capacity, financial, human and technical resources as well as the weak coordination of roles between WAMI and the central banks of the region.

3. REPORT PROPOSALS: REFOCUS ON A PRAGMATIC AND REALISTIC TIMING MONETARY COORDINATION AND FINANCIAL INTEGRATION PROGRAMME

The WAMZ monetary integration process is particularly undermined by a crucial credibility problem involving three groups of stakeholders, each of which needs to address the problem at its own level: (i) political authorities themselves; (ii) market participants (financial sector stakeholders and institutions, private sector, etc.) and the general public; and (iii) development partners.

Concerning inadequate preparation, inappropriate sequencing of reforms and unrealistic schedules, which inevitably led to successive postponements, have greatly undermined the credibility of the process. Setting priorities and adopting a pragmatic, gradual and realistic approach could facilitate and foster the adoption of reforms and gradually restore confidence in the process.

a. Redefining the Role and Strengthening the Capacity of WAMI

The capacity of WAMI should be strengthened to enable the Institute to play an effective role as a platform for intense cooperation between the central banks in the WAMZ.

Given the experience acquired by the Institute and considering its current and projected capacity, the Institute may concentrate, during a transition period, on the following major activities:

1. Surveillance of macro-economic convergence;
2. Harmonization of price statistics and capital account statistics;
3. Coordination of monetary and exchange rate policies (in close collaboration with national central banks);
4. Coordination of exchange rate policies and exchange regulation policies (in close collaboration with national central banks);
5. Coordination of financial infrastructure development (including payments systems) at the regional level;
6. Harmonization of regulations relating to the supervision and regulation of financial systems; and
7. Financial stability.

Institution building is indispensable for WAMI to achieve its set objectives. Such institution building may be conducted in the short term with the assistance of experts over a more or less extended period, so as to improve its capacity to implement the above activities.

b. Strengthening Technical Cooperation between WAMI and National Central Banks

To fulfill the key missions of WAMI and stay focussed on the major activities described above, it is strongly recommended that technical cooperation ties between the Institute and national central banks in the region be strengthened. The practicalities of such cooperation are predicated on the establishment of technical sub-teams in various fields mentioned, comprising officers from the Institute and national central banks. It has also been suggested that the position of technical coordinator be created within the Institute and placed under the aegis of its Director-General.
4. THE EUROZONE CRISIS AND LESSONS FOR THE FORMATION OF A WEST AFRICAN MONETARY ZONE AND AN EAST AFRICAN MONETARY UNION

The Eurozone crisis has broader impacts than just for countries of Europe. There are quite a few implications for Africa since closer economic integration in the continent has been touted as an important strategy to expand markets and the trade of goods between African countries. A common currency in Africa, such as the CFA franc, is supposed to enhance intra-African trade by eliminating exchange rate volatility, reducing transaction costs and facilitating capital flows within the region. The East Africa Community (EAC) is one of the regional economic blocs in the process of coming together. While a lot of progress has been made toward EAC integration, things have not been so straightforward. Policymakers working on EAC integration have been approaching the adoption of a single monetary union with caution given the ongoing sovereign debt crisis in Europe. There are certainly lessons from Europe that the East African countries can take to heart as they attempt to move toward a single monetary union.

Two main policy gaps in formation of the euro area have left it in its current state of instability. First, the design of the Eurozone did not provide a contingency plan or safety measures to deal with sovereign debt crises. There is no protocol for member states should they find it difficult to access markets to refinance their sovereign debt. Second, 17 sovereign fiscal authorities govern the euro, which means it takes a lot of coordination to get anything done. In addition, there are no compelling mechanisms to enforce the commitments of member states. Some clear lessons emerge from the Eurozone crisis that directly relate to the EAC and its path toward creating a single monetary union.

First, the process of further monetary integration of the EAC should not be expedited. Given the circumstances in Europe, it may be wise to wait and see how the euro-area crisis is handled. This will allow African policymakers to take stock of any lessons from Europe, which can help them decide whether move toward or away from the EAC shilling. Even before the Eurozone crisis, experts urged the EAC to move slowly regarding the monetary union and to be wary of inflation caused...
by volatile oil prices. With discovery of oil in Uganda, the threat of price volatility is certainly more eminent.

The second takeaway from the euro-area crisis is that fiscal and monetary policies are not enough to ensure sustainability against the lack of full-blown coordination of economic policies. Euro-area countries pursued different structural policies and as a result competitiveness differentials widened throughout the decade, leading to substantial imbalances within the euro area. For instance, Germany has been able to accumulate substantial current account surpluses while the peripheral economies in Europe were doing just the opposite and running current account deficits that resulted in higher debt. Had these imbalances been corrected earlier, the crisis would have been much less severe or may not have occurred at all. Even following the recent European Summit, there still seems to be no hint of coordination of macroeconomic policies. Instead, all European countries will retrench their budgets, which will set the pace for a deflationary adjustment by uniformly compressing aggregate demand throughout the euro-area.

Similarly, the EAC countries are pursuing differing structural policies even as they negotiate the deal for a currency union. While the EAC agreed upon the criteria for macroeconomic convergence, issues of fiscal sustainability have not been met by member countries. For example, the budget deficit level criterion is set not to exceed 5 percent of GDP. Yet, according to the August 2011 EAC Strategy Report, Kenya, Uganda, Tanzania and Rwanda all have deficits exceeding the recommended target. The upper inflation limit was also set at 5 percent, but the same five countries are grappling with high levels of inflation above 10 percent, coupled with high currency volatility. Reserve criterion and management have yet to even be decided upon. The rationale of choosing these criteria is that they are seen as attainable goals for members— high enough to encourage spending for development, but low enough to be sustainable in the long-term. Unless, the EAC wants to recreate the mistakes of Europe it should pay strict attention to the fiscal benchmarks and other macroeconomic convergence criterion requirements.

Finally, the euro-area crisis highlights the importance of an independent central bank for the region that will guide monetary policy formulation and implementation. In addition, the central bank must enforce prudential financial regulations for the financial sector of member countries. The East Africa Central Bank is planned to be formed along the lines of European Central Bank (ECB). Thus, one must consider the institutional deficiencies of the ECB in order to avoid falling into the same trap that the ECB is currently in. A crucial gap in the euro area is what to do when there is a run on government bonds since the ECB does not have a mandate to intervene. Nor is there a crisis management facility, such as an enhanced European Monetary Fund. The fiscal crisis has spilled over to the banking sector, for which there is no central supervision or a central or federal deposit insurance mechanism. In sum, the current treaty for the East African Community, unlike the one for the current EU euro area, needs to spell out safety measures and a bailout plan in case of debt or other fiscal problems among members.

The formation of the monetary union is a challenge given the great imbalance in individual national economic strengths of the EAC countries. They must be prepared to give up a degree of sovereignty and to converge politically to avoid collapse. The ideal integration situation is where the countries in the union share common monetary and fiscal policies, a common pool of foreign exchange reserves, and a common monetary authority or central bank. Otherwise, trying to operate a single currency without social, economic and political integration is likely to fail as evidenced by Eurozone crisis.

For the time being, the EAC is better off slowing down the integration process. The 2024 monetary union launch is only feasible if all of the macroeconomic convergence
criteria are met and harmonization of all fiscal, financial and monetary policies is complete. Instead of rushing to move into a currency union, regional integration in the East African Community should focus more on trade expansion and infrastructure coordination. Whatever the EAC countries decide, the process of forming a single monetary union should be carefully considered given the ongoing turmoil in Europe and the EU’s failure to resolve the problem.

5. Conclusions and Recommendations

The launch of the monetary union among WAMZ member countries was successively rescheduled three times (January 2003, July 2005 and December 2009) as a result of inadequate preparation. The WAMZ Heads of State and Government had decided in December 2009 that it was not feasible to introduce a single currency in the five WAMZ member countries on that date. With respect to the revised plans, WAMZ hopes to adopt a single currency called “ECO” by 2015. This objective, like previous ones, may not be achieved if the member countries fail to establish effective monetary coordination and financial integration prior to the said date, in spite of progress recorded in other areas. Indeed, as the proposed date of 2015 for the launch of the second regional currency moves closer, the ECOWAS Commission and the ECOWAS Authority of Heads of State and Government, like other stakeholders, are concerned about the state of preparedness of the six Member States of the West African Monetary Zone (WAMZ) for 2015 (WAMZ 2013).

The inadequate preparation, inappropriate sequencing of reforms and unrealistic schedules, which inevitably led to successive postponements, have greatly undermined the credibility of the process towards monetary integration among WAMZ member countries. The WAMI and other regional institutions should set priorities and adopt a pragmatic, gradual and realistic approach to facilitate and foster the adoption of reforms and gradually restore confidence in the process.

To do so, the capacity of WAMI should be strengthened to enable the Institute to play an effective role as a platform for intense cooperation between the central banks in the WAMZ. In addition, it is strongly recommended that technical cooperation ties between the Institute and national central banks in the region be strengthened.

51. The new 2015 date was adopted at the 24th meeting of the Convergence Council of Ministers and Governors of the West African Monetary Zone in Abuja Monday June 22nd.
IV. EAST AFRICAN COMMUNITY

1. HISTORICAL BACKGROUND TO THE EAST AFRICAN COMMUNITY AND THE ECONOMIC AND MONETARY INTEGRATION PROCESS

In the past, Kenya, Tanzania and Uganda have enjoyed a long history of co-operation under successive regional integration arrangements. The Treaty establishing the EAC, signed on 20 November 1999 between the founding members States (Kenya, Tanzania and Uganda), officially went into force on 7 July 2000. In accordance with Article 5 of the Treaty, member States undertake to establish among themselves “a customs union, a common market, a monetary union and ultimately a political federation”. Furthermore, Article 82 of the treaty urges member States to “cooperate in monetary and financial matters and maintain the basic convertibility of their currencies as a basis for the establishment of a monetary union”.

More specifically, Article 82 (1) stipulates that “…the Partner States undertake to cooperate in monetary and fiscal matters in accordance with the approved macro-economic policies, harmonization programmes and convergence framework of the Community in order to establish monetary stability within the Community aimed at facilitating economic integration efforts and the attainment of sustainable economic development of the Community. To this end, the Partner States shall: (a) co-operate in monetary and financial matters and maintain the convertibility of their currencies as a basis for the establishment of a Monetary Union; (b) harmonize their macro-economic policies especially in exchange rate policy, interest rate policy, monetary and fiscal policies; and (c) remove obstacles to the free movement of goods, services and capital within the Community”.

Furthermore, in accordance with Article 83 (2), “Partner States undertake to: (a) remove all exchange restrictions on imports and exports within the Community; (b) maintain free market determined exchange rates and enhance the levels of their international reserves; (c) adjust their fiscal policies and net domestic credit to the government to ensure monetary stability and the achievement of sustainable economic growth; (d) liberalize their financial sectors by freeing and deregulating interest rates with a view to achieving positive real interest rates in order to promote savings for investment within the Community and to enhance competition and efficiency in their financial systems; and (e) harmonize their tax policies with a view to removing tax distortions in order to bring about a more efficient allocation of resources within the Community”.

In order to achieve these objectives, integrate their economies and establish a monetary union, the Partner States have drawn up the following macro-economic convergence criteria:

- Reducing and stabilizing Inflation rate below 5%;
- Achieving robust and sustainable real GDP growth rate of at least 7% per annum;
- Reducing current account deficit with respect to GDP to a sustainable level;
- Reducing budget deficit-to-GDP ratio (excluding grants) to less than 5%;
- Increasing national savings-to GDP ratio to at least 20%, in the medium term;
- Accumulating gross exchange reserves equivalent to six months of imports in the medium term;
- Maintaining reduced market-determined interest rates;
- Maintaining stable market-determined interest rates;
- Implementing initiatives aimed at reducing the internal and external debt; and
- Applying prudential banking regulation standards and stringent surveillance, and improving business governance and transparency in all financial transactions.

The primary stage of the integration process was achieved with the establishment of a customs union. During their summit of 2004, the Heads of State of EAC member countries adopted the Protocol to establish a Customs Union. This protocol went into force on 1 January 2005 and became fully effective on 1 January 2010, following a period of gradual implementation.
The EAC was expanded in 2007 to include Rwanda and Burundi, which undertook to implement measures relating to the Common External Tariff (CET) and internal customs duties in accordance with the membership schedule.

During the EAC Heads of State Summit of 2009, five Heads of State adopted a Protocol to establish the EAC Common Market, which should facilitate the free movement of goods, services, labour and capital. This protocol should enter into force on 1 July 2010 and should be fully effective by 1 January 2015, following a period of gradual implementation.

To attend the progress registered in the economic integration process (including the progressive development of regional infrastructure and the establishment of the EAC Customs Union to boost intra-regional trade), the EAC is also committed to realizing the successive stages of the establishment of a monetary union. In August 2007, the EAC Heads of State Summit decided to speed up the implementation of the monetary union, by bringing forward the initial launching date from 2015 to 2012. On 30 June 2008, the EAC initiated the negotiation procedure with the European Central Bank (ECB), which culminated in the signing of a contract by both parties on 2 June 2009, for the preparation of a study on the creation of a monetary union within the EAC. More recently, this deadline has been revised and replaced by a realistic deadline. Indeed, in November 2013, EAC signed Monetary Union Protocol in Kampala, outlining ten-year road map towards monetary union. The EAC single currency would be introduced in 2024. The EAC Monetary Institute is planned to be established in 2015 to direct preparatory work for monetary union. An East African Surveillance, Compliance and Enforcement Commission to monitor and enforce convergence will be created by 2018. From that point on, monetary and exchange rate policies will be coordinated and harmonized (Mira 2013). As outlined by Mira (2013), the launch of the East African Cross Border Payment System, an integrated payment and settlement system within the EAC, is a concrete operational step that will help toward monetary, financial, and economic integration. The system is so far operational in three EAC members—Kenya, Tanzania, and Uganda; two additional members—Rwanda and Burundi—are working on the preparation of their systems.

A road map for the establishment of the East African Monetary Union (EAMU) is already in place, and all works should be completed prior to the 2024 deadline recently set by the Heads of State of EAC member countries. This is the third phase of integration of the economies of Kenya, Uganda, Tanzania, Rwanda and Burundi.

2. KEY PROGRESS AND CHALLENGES IN MONETARY COORDINATION AND FINANCIAL INTEGRATION WITHIN THE EAST AFRICAN COMMUNITY

The report of the Monetary Affairs Committee (MAC) of the EAC Secretariat, “Achievements, Challenges and Way Forward (1998-2008)”\(^{52}\), comprising governors of central banks whose mandate is to strengthen monetary and financial cooperation within the Community, presents the numerous achievements recorded over the ten-year period, which have had an impact on the integration process. Similarly, the report of the 13th EAC Monetary Affairs Committee Meeting\(^{53}\) underscores on-going progress in the area of monetary and financial cooperation within the Community and challenges to the establishment of a monetary union in accordance with the adopted schedule. The progress recorded and on-going challenges are described in the key areas below.

**a. Prerequisite Conditions for the Establishment of a Monetary Union**

1) Monetary Policy Frameworks, Targets and Instruments

Henceforth, the monetary policy framework for all central banks uses a Reserve Money Programme (RMP). In accordance with this programme, the formulation of monetary policy is based on the currency quantitative theory. In the RMP, the monetary base is
used as operating target, while money, in broad terms, serves as intermediate target. The RMP hinges on the assumption that the demand for money, monetary multiplier and the speed of money circulation are stable and predictable. Similarly, all central banks use open-market operations as the key instrument for monetary policy implementation. Lastly, central banks use permanent facilities, mandatory reserves and exchange rate operations for monetary policy purposes.

However, in practice, central banks are still facing almost similar challenges in implementing the RMP. Such challenges include in particular: (i) narrow and shallow financial markets; (ii) unpredictable capital flows; (iii) weak monetary policy transmission mechanisms; (iv) existence of a segmented and concentrated banking system; (v) high proportion of money in circulation in the monetary base; (vi) external shocks on supply such as basic commodity prices, drought and food commodity prices; (vii) volatility of the monetary multiplier and the speed of money circulation; (viii) the high degree of government deposits with commercial banks in some countries of the sub-region is an on-going challenge to the conduct of the monetary policy; (ix) government’s overarching influence on central banks in some countries, sometimes leads to a freeze in money market funding; (x) the volatility of foreign exchange inflows in the sub-region also has repercussions on the conduct of monetary policy; while it is true that capital flows are beneficial to economic development, it is worth acknowledging that the sharp increase in portfolio investments complicates the conduct of monetary policy.

2) Monetary Policy Communication Strategy

Central banks in the Community have gradually become aware of the importance of transparency and communication for the credibility of monetary policy. Generally, however, central banks are still at an initial stage of institutionalization and implementation of monetary policy communication strategies.

b. Liberalization of Capital Account

The report particularly underscores the fact that most restrictions on the movement of capital have been removed. In the aftermath of such liberalization, it has been observed that EAC member countries have been receiving increasingly large volumes of capital with the attendant adverse and beneficial consequences for the region. Such capital inflow, especially in the form of short-term capital, raises challenges for the implementation of monetary policy.

c. Currency Convertibility

EAC member countries continue to foster the convertibility of their currency with respect to other currencies in the sub-region. However, this convertibility is far from being real and effective54, and member States acknowledge that this issue should be resolved within reasonable deadlines by the competent sub-committee of the Monetary Affairs Committee.

d. Capacity Building in Economic Modelling and Forecast

The EAC central banks recently undertook to build their capacity in economic modelling and forecast, with a view to improving efficiency in the formulation and implementation of their monetary policies55. However, tremendous shortcomings persist and central banks still face very huge challenges to building their liquidity forecast capacity.

e. Harmonization of Price Statistics

The central banks of the Community have registered significant progress in harmonizing the definition of underlying inflation, excluding articles whose prices will likely be influenced by exogenous factors such as climate and fluctuations in world oil prices. However, some banks have not adopted this definition of underlying inflation excluding food and energy prices and most banks are still at the stage of introducing cooperation with National Statistics Institutes for the quarterly production of disaggregated price statistics.

f. Harmonization of Monetary and Financial Statistics and Financial Stability Indicators

The harmonization of definitions, concepts and statistical methodologies and indicators of various

54. Conclusions collected following discussions between the author and some central banks of the sub-region in June 2010.
55. This priority has also been underscored by the central bank officials met during our mission in June 2010.
financial sectors is underway. It is expected that a series of indicators of financial stability be posted on the official website of the EAC Secretariat. However, there is still no complete and comprehensive base of stability indicators for the entire financial system in various countries of the Community. The central banks, financial market authorities, pension funds, national insurance commissions and the NIS discussed issues relating to cross-cutting financial data.

**g. Supervision and Regulation of the Banking System**

Furthermore, the report reveals that significant progress has been achieved in harmonizing banking legislation, licence issuance procedures, prudential guidelines for and regulation of cross-border activities of financial institutions. However, there is no enabling arrangement for an institution authorized to operate in one State of the Community to do so in another State of the Community without authorization from the latter country (that is, there is no single “authorization” in the sub-region). As regards banking supervision, the EAC central banks also intend to implement Basel II.

The Basel Core Principles represent the internationally accepted standards and reference points for assessing the efficiency of banking supervision and regulation. The Report of the 13th EAC Monetary Affairs Committee (MAC) Meeting and the financial systems appraisals conducted by the IMF and the World Bank show that member countries comply with the Basel Core Principles at varying degrees. For the same reason, there are differences between prudential regulations and IFRS standards in some member countries.

**h. Payments Systems**

The report states that more significant progress has been recorded in the payments systems. While it is true that some EAC countries have adequate payments systems, it is worth acknowledging also that much still has to be done to globalize, within the sub-region, payments systems that are efficient, effective and compliant with international best practices. For instance, all countries have not yet integrated the Real Time Gross Settlement (RTGS) module into their payments system. Member States have proposed to introduce or strengthen modern payments systems nationwide (and with some arrangements regarding the interoperability of card systems at the Community level). Kenya, Tanzania and Uganda have incorporated central depositories of government securities into the RTGS modules of their national systems. The two additional members—Rwanda and Burundi—are working on the preparation of their systems. The same report also reveals that the harmonization of payments systems at the regional level should be implemented at end-2009 (such harmonization is ongoing with the formal of the East African Cross Border Payment System, an integrated payment and settlement system within the EAC in November 2013). Experience has shown that linking up payments systems within a regional group (such as the EU's TARGET system) may be a powerful instrument to buttress financial integration and supplement efforts aimed at fostering regional trading arrangements. During the 13th EAC Monetary Affairs Committee Meeting, the central banks also recommended that the Sub-committee in charge of harmonization of payments systems analyse the impact of currency convertibility on such harmonization.

**i. Convergence of Financial Services**

There is currently a global trend towards the convergence of financial services, with the emergence of a “single window for financial services”. According to this model, clients may access various financial services, including insurance, brokerage and counselling on financial products and services from a single financial services provider (generally a bank). Within the EAC in recent years, banks have expressed interest in providing their clients a wide range of financial services in addition to

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56. A Regional Workshop on Cross-Border Banking and Consolidated Supervision has been organized by the African Development Bank (AfDB), partnering with the Central Bank of Kenya (CBK) and in collaboration with the Central Banks of AMU, CEMAC, COMESA, EAC regions and the International Monetary Fund (IMF) in Nairobi on December 6-10, 2010. The main objectives were: (i) to give the contours of cross-border banking supervision and advanced issues relating to cross-border banking supervision; (ii) to raise awareness of the concept, practice and relevance of cross-border banking supervision in the context of concentration and internationalization of the banks and the challenges faced by the supervisors in Africa; and (iii) to develop proposals regarding the cross-border banking supervision in the targeted proposed regions.


58. The AfDB, in conjunction with USAID, is currently organizing a workshop on payments systems in the EAC to discuss options for the development of payments systems in the sub-region and their integration.
banking products and services, particularly insurance services (bank insurance). This recent trend is translated by the incorporation of specialized subsidiaries or the development of partnerships with other financial services partners such as insurance companies and capital market stakeholders. The current banking regulation in all EAC member countries does not authorize banks to provide financial services other than banking services. In order to meet increasing client demand for a wider range of financial products and services, and to deepen access to financial services within the Community, the EAC Monetary Affairs Committee\textsuperscript{59} had recommended the creation of a conducive legal and regulatory framework and the conduct of a detailed risk assessment for institutions. The process is underway in various EAC countries.

\textbf{j. Integration of Financial Markets}

Article 86 of the Treaty stipulates that: “Member States shall, in accordance with timetable to be determined by the Council, permit the free movement of capital within the Community, develop, harmonize and eventually integrate their financial systems. In this regard, the Partner States shall: (a) ensure the unimpeded flow of capital within the Community through the removal of controls on the transfer of capital among the Partner States; (b) ensure that citizens of and persons resident in a Partner State are allowed to acquire stocks, shares and other securities or to invest in businesses in the other Partner States; and (iii) encourage cross-border trade in financial instruments.

However, it is observed in the report\textsuperscript{60} that, in general, the financial systems and markets of the sub-region are narrow and under-developed, and numerous difficulties and challenges still need to be addressed. Indeed, the central banks of the sub-region face huge challenges in conducting financial market operations, as equally underscored in the 13th Report of the Monetary Affairs Committee\textsuperscript{61}. These difficulties are due mainly to weak institutional, legal and regulatory frameworks, and poor financial infrastructure development.

The analysis of financial market integration in the EAC has also been the subject of a recent IMF report entitled “Progress towards Harmonization of Capital Account Regulations and Capital Market Integration in the East African Community” (IMF Country Report No. 09/37). The report covers Kenya, Tanzania and Uganda. Among the three countries analysed, Kenya has by far the largest capital market in the sub-region in terms of market capitalization, the number of listed corporations and turn-over. Their common legal tradition has allowed for the harmonization, to a certain extent, of the legal and regulatory frameworks of markets in Tanzania and Uganda as well as that of Kenya with the objective of bridging the gap with respect to the Kenyan law on securities, while bearing in mind the regional integration of the various markets.

All EAC member States are currently implementing five-year financial market development plans under the aegis of the Monetary Affairs Committee and the EAC Secretariat. The Capital Markets, Insurance and Pension Committee (CMIPC) (formerly known as Capital Markets Development Committee) was set up to foster the harmonization of legal regimes, regulatory frameworks, fiscal regimes (given that these reforms pertain to regional financial market development within the EAC), disclosure rules and financial and accounting standards. The committee actively encourages member States to implement its recommendations (including Burundi and Rwanda, as new members of the EAC). However, as underscored in the IMF report, financial markets in the sub-region are not yet well integrated. One of the reasons for such poor performance is obviously the fact that the approach to the liberalization of capital account regulation was more gradual than financial market reform, and was not conducted in a harmonized manner in all the three countries. While Uganda completely opened up its capital account in the late 1990s, Kenya’s capital account is at present almost completely liberalized. Conversely, Tanzania maintained a certain measure of control on capital account, and intends to do so until end-2015.

The Cadogan Financial Report on developing an EAC regional securities market (January 2009) also concludes that there is currently little cross-border capital market business. The report identifies various

\textsuperscript{59} EAC Secretariat: Report of the 13th EAC Monetary Affairs Committee (MAC) Meeting, 10 May 2010, Arusha, Tanzania.

\textsuperscript{60} MAC report “Achievements, challenges and way forward (1998-2008)”, Arusha, Tanzania.

\textsuperscript{61} EAC Secretariat: Report of the 13th EAC Monetary Affairs Committee (MAC) Meeting, 10 May 2010, Arusha, Tanzania.
barriers to the regionalization of securities markets, including legal and fiscal, regulatory, operational and political barriers (in the form of preservation of vested interests or insufficient commitment). The report recommends, where possible, a harmonized approach to accommodate more easily different speeds of progress. In the area of market infrastructure, the report recommends the retention of individual national exchanges, using a single trading platform to achieve economies of scale, and with its own stock market price index and investor information system. In the area of clearing and settlement, the report proposes that the securities depository function be separated from national exchanges and merged into a single EAC-wide company using the linked national RTGS systems for cross-border settlement. Furthermore, the report proposes that institutions licensed in one EAC country should be able to operate in all Partner States without further regulatory approval (i.e. a “regional passport arrangement”). These recommendations and some proposals made in the IMF report are compatible with the recommendations of this report (refer to the Section V).

The East African Securities Exchange Association (EASEA), a body that puts together the stock exchanges of Kenya, Uganda, Tanzania and Rwanda, has put forward a policy that will require Initial Public Offers (IPO) within the East African Community to be cross listed on all the regional stock exchanges. Through interconnectedness and collaboration of the regional stock exchanges, EASEA hopes to increase efficiency and market liquidity in the region. The body also plans to create guidelines on how stockbrokers can operate across the region as well as establishment of inter-depository transfers for cross listed securities.

EASEA has come a long way and made good achievements thus far with regards to harmonizing development within the regional capital markets.

**k. Financial Education and Access to Financial Services**

The levels of financial education and access to financial products and services have improved but are still low in the EAC. Data published by Finscope in the case of a sample of African countries, shows that for EAC countries, the rate of access to formal financial services is very low (even though in progress) and fall below the rate of access to informal financial services. On the contrary, the rate of financial exclusion is high. For purposes of illustration, in Kenya, the rate of access to formal financial services increased from 26.4% in 2006 to 40.5% in 2009, whereas 26.8% of the population continues to use informal financial services. The report goes further to reveal that in Tanzania, the rate of access to formal financial services increased from 11.2% to 16.7%, and 27.3% of the population resort to informal financial services. The 2007 Finscope report shows that the rate of access to formal and informal financial services in Uganda is the lowest in the sub-region (21% and 17%, respectively). The situation in Rwanda as presented by the 2008 Finscope survey is almost similar to that of Uganda with relatively close figures (21% and 26% respectively). However, the rate of access to formal financial services in Burundi is very critical, with a level in the region of 1.9%. Furthermore, the financial integration process within the EAC is undermined by the absence of harmonization of financial education curricula in the sub-region and lack of coordination of actions undertaken in this area by the various member countries.

The general impression from the foregoing is that, despite the ratification of the Common Market Protocol and the efforts of the Monetary Affairs Committee and sub-committees (CMIPC, etc.), through their regular meetings, decisions and recommendations made at the end of such meetings, monetary coordination and financial integration within the EAC are still very limited. In fact, the adoption of the Common Market Protocol is a crucial stage in the monetary coordination and financial integration process. The protocol aims at facilitating the free movement of goods, services, persons and capital and should foster the emergence and development of cross-border financial institutions. However, the effective implementation of the Protocol is undermined by huge constraints, particularly the coordination and harmonization, by Partner States, of their financial sector policies, legislative and regulatory...
frameworks to foster the development and stability of their financial systems as well as the development of their financial infrastructure (particularly financial norms and standards as well as payments and settlement systems) at sub-regional level. These arrangements are fundamental for economic and financial integration which, together with monetary coordination, constitute a prerequisite condition for the establishment of an effective monetary union.

To support this process, a number of initiatives intended to buttress the development and integration of financial systems and monetary coordination, have been developed by key development partners in conjunction with the EAC Secretariat.

Very intense initiatives to strengthen human capacity are currently undertaken and scheduled by national and regional institutions as well as key development partners to support the financial systems development and integration process, and monetary coordination in EAC countries. The report underscores the need for heightened coordination and sustainability of human capacity building activities. Accordingly, the report proposes that sub-regional training institutions play a greater role in monetary and financial matters in order to develop and harmonize capacity as well as implement capacity building programmes.

3. REPORT PROPOSALS TO SUPPORT THE MONETARY COORDINATION AND REGIONAL FINANCIAL INTEGRATION PROCESS AND ON-GOING EFFORTS BY KEY DEVELOPMENT PARTNERS

It is clear from the above developments on achievements and challenges to financial systems development and integration, and monetary coordination in EAC countries that the efforts of national, sub-regional and international institutions should be well coordinated. Likewise, the implementation of on-going and scheduled actions and policies is undermined by the low development and harmonization of institutional and human capacity at the national and regional levels.

Given the primordial and pivotal role played by central banks in the development, integration and stability of financial systems, the report proposes the establishment, within the Monetary Affairs Committee bringing together the central bank governors of the sub-region, of a Permanent Technical Secretariat hosted in one of the central banks. The following paragraph summarizes the role and composition of the said secretariat.

a. Establishment of a Permanent Technical Secretariat within the Monetary Affairs Committee of the EAC Secretariat hosted in one of the Central Banks of the Sub-Region

To support the regional financial integration and monetary union process, and given the complexity of the technical coordination of the prerequisite stages of the establishment of EAMI, particularly the implementation of the recommendations of the Monetary Affairs Committee and the conduct of negotiations under the Monetary Protocol, the establishment of a Permanent Technical Secretariat within the Monetary Affairs Committee is hereby proposed.

1) Establishment

The Permanent Technical Secretariat (PTS) would be established without a legal status different from that of the MAC and without decision-making power. It will be based in one of the central banks of the EAC (to be chosen by the Committee of Central Bank Governors). The PTS would be established with a view to undertaking the preparatory work needed for MAC and sub-committee meetings, monitoring recommendations and their coordinated implementation prior to the establishment of EAMI. The PTS, as a technical instrument within the MAC, should carry out activities under the supervision of the Committee and without interfering with the activities of national central banks regarding monetary policy, exchange rate policy and other areas.

63. The start-up expenses of the PTS may be partly defrayed by development partners.
64. These meetings are prepared by the central bank of the country of origin of MAC’s current chairman.
2) Objective and Mission

The PTS’s key missions are three-fold:

- Institution building of MAC and sub-committees by assisting in the analytical and technical preparation of MAC meetings, as well as the coordinated monitoring and implementation of MAC and sub-committee recommendations.
- Ensuring technical monitoring and coordination of external technical assistance for MAC in its area of jurisdiction.
- Providing technical assistance to member countries for negotiations with a view to signing the “Monetary Protocol” precedent to the establishment of EAMI.

Against such a backdrop, the mission of the PTS would consist especially in conducting preparatory works for laying the technical foundations for the establishment of EAMI.

3) Organization

The organization of the PTS should be designed in such a manner as to ensure that it effectively plays its role. It would comprise a limited number of full-time senior staff seconded from central banks and appointed by MAC. Furthermore, the PTS should receive assistance from long-term external consultants (from institutions like the IMF and/or the ECB). The administrative duties of the PTS may be performed by the host central bank.

The PTS may comprise a coordinator assisted by a deputy coordinator - responsible for reporting PTS activities to the MAC - and five technical units covering specific areas and comprising two experts each. In addition, the PTS may be supported by two to four Secretaries/Assistants.

The project may cover four key areas, namely: (i) Statistics and modelling; (ii) Monetary and financial policies; (iii) Exchange rate policy and exchange regulation; (iv) Supervision and regulation of financial systems and financial stability; (v) Financial infrastructure.

65. Monitoring of recommendations initially entrusted to the various central banks.
4) Obligation to Report

As a technical instrument of the MAC and in accordance with set objectives, the PTS shall submit regular progress reports to the MAC, which should assess the extent to which the PTS is achieving its objectives. These reports may be drawn up on a monthly basis to facilitate the monitoring of assigned activities. In addition, summary reports should be prepared on a quarterly, half-yearly and yearly basis.

The PTS reports, validated by the MAC, should also be used in informing partner countries, national financial institutions as well as sub-regional institutions involved in the financial integration and monetary union process (professional banking associations, professional insurance associations, financial market associations, etc.), to keep them abreast of the progress achieved in the financial and monetary integration process and to help them prepare for the process. These reports, validated by the MAC, should be published for wider circulation.

5) Coordination with the EAC Secretariat and the HLTF

While appreciating the roles currently played by the High Level Task Force (HLTF) in charge of negotiating the monetary protocol precedent to the establishment of EAMI and the EAC Secretariat which is coordinating this exercise, the PTS as a technical team and a non-formal institution will provide and coordinate the necessary technical support and assistance to the national central banks given the primordial and pivotal role played by central banks in the monetary union process. The report does not suggest to replace the existing structure by the PTS but to reinforce this structure. Therefore, the PTS will work very closely with the existing institutions, namely the HLTF and the EAC Secretariat, in order to advance the monetary integration process in the EAC. As suggested by the Central bank of Kenya, the PTS as a precursor of EAMI needs to work closely with relevant stakeholders including statistical bureaus while undertaking preparatory work.

Therefore, there is no overlapping roles between the existing, namely the HLTF and the EAC Secretariat, and the PTS. The purpose of the PTS is to complement the work being done by the HLTF and the EAC Secretariat.

6) Dissolution of the PTS and Transition to the EAMl

The PTS should be dissolved upon the establishment of the EAMI with broader duties and its own legal status. The EAMI could benefit not only from the work done by the PTS, but also from its experience and human resources.

b. Coordinated Capacity Building in Monetary and Financial Areas

The monetary and financial integration process may only be completed effectively if human resources are developed in a harmonious, coordinated and sustainable manner within the community. Such development can be achieved through the implementation of common capacity building programmes in various areas covered by the process, namely: (i) macro-economic analysis and forecast, statistics and modelling; (ii) monetary and financial policies; exchange rate policies and exchange regulations; supervision and regulation of financial systems; financial stability; payments systems, financial information systems; financial markets; insurance, etc.

Several options can be considered for implementing this proposal. A first option would consist in designing training modules in the above areas on a permanent basis in sub-regional training institutions (Kenya School of Monetary Studies, Training Institute for Financial Markets Operators based in Kampala, Uganda, etc.) sanctioned by end-of-course certificates and diplomas. A second option would consist in incorporating these modules in the university curricula of various Partner States and taught in the above sub-regional institutions. A third option would consist in designing common curricular in monetary and financial disciplines at the

66. However, the Central Bank of Kenya has raised the concern of a duplication of efforts and the issue how the proposed PTS will fit in under the current arrangements in the negotiations of EAMU; on one hand there is a HLTF to negotiate the protocol and on the other there is the EAC Secretariat coordinating the exercise. Thus, the Central Bank of Kenya has suggested considering a proposal of first strengthening the EAC Secretariat’s capacity to carry out some of the critical tasks, with the assistance of partner states, before setting up the proposed PTS.

67. Kenya School of Monetary Studies (KSMS)

68. The Training Institute for Financial Markets Operators
sub-regional level, which should be taught by national universities and schools with the support of external partners. To attract talents in the sub-region, partnership and sponsoring agreements could be established with foreign training institutions of international repute.

4. CONCLUSIONS AND RECOMMENDATIONS

To foster regional economic and financial integration among EAC Partner States, an institutional framework and a range of policies have been put in place. Outstanding progress has been achieved towards economic integration. However, progress in the economic convergence as well as monetary, financial and exchange rate policy coordination process has been slow, thereby reflecting difficulties in the implementation of sub-regional programmes and initiatives, as well as major challenges to economic, financial and monetary integration in the sub-region.

In fact, the existence of political impetus and sub-regional institutions to buttress the economic and financial integration process did not lead to in-depth monetary coordination and financial integration within the EAC. Nevertheless, significant progress has been recorded with a view to fostering the development of an integrated and competitive sub-regional financial system; the gradual implementation of coordinated monetary and financial policies and a cross-border financial infrastructure have contributed to the financial and monetary integration process. Furthermore, efforts made with a view to signing a monetary protocol tie with that process.

At this stage, the EAC is at the preliminary phase of establishing financial and monetary integration. The degree of economic convergence, monetary coordination and integration of financial systems are still inadequate for launching an effective and sustainable monetary union within the stipulated timeframes. The report under consideration lays emphasis on the need to strengthen monetary coordination and the integration of financial systems in order to bolster on-going efforts at the sub-regional level and buttress ongoing efforts and scheduled assistance by the various development partners.

Against the backdrop of the EAC and the existence of various currencies, the report relies on the pivotal and primordial role played by central banks in the development, integration and stability of financial systems, to propose a pragmatic and gradual approach to monetary coordination and regional financial integration necessary for an effective and sustainable implementation of a monetary union. Furthermore, the report asserts that the basic prerequisites for financial integration and laying the groundwork for a sound and sustainable monetary union may only be achieved if human capacity is developed in a sustainable and coordinated manner.

In addition, the report upholds that the very ambitious goals for launching a monetary union may prompt member States to speed up the implementation of requisite policies and reforms. However, they may also entail the risk of postponements and, consequently, undermine the credibility of the process, thereby considerably weakening the support of market participants and the general public, which is needed for the entire process. The EAC countries that are also engaged in the process of launching their monetary union in 2024 should learn from the failures of WAMZ.
V. THE EUROZONE CRISIS AND LESSONS FOR THE FORMATION OF THE EAC AND WAMZ MONETARY UNIONS

The Eurozone crisis presents some critical lessons for developing countries, particularly in Africa. The Eurozone crisis has threatened to disorganize the European monetary integration model that Africa sought to imitate. The euro zone crisis is a vital case study for African RECs, in particular for the East African Community (EAC) and West African Monetary Zone (WAMZ) partner states as both regional blocs progressively move to unveil a monetary union.

1. BACKGROUND

The European sovereign debt crisis is the current financial crisis that reflects the difficulties for some Eurozone member countries (e.g. Greece) to re-finance their government debt without the assistance of third parties (including the IMF). The European sovereign debt crisis resulted from a combination of intricate factors, including the financial globalization; strong liquidity and easy credit conditions during the 2002-2008 period that encouraged high-risk lending and borrowing practices; fiscal policy choices related to government revenues and expenses; the 2007-2008 global financial crisis; and approaches used by nations to bail out exposed banks and private bondholders, assuming private debt burdens or socializing losses. However, causes of the crisis varied by country. For instance, In Greece, unsustainable public sector wage and pension commitments drove the debt increase.

In 2009, fears of a sovereign debt crisis surged among institutional investors as a result of the movement of downgrading of government debt by rating agencies for some European countries. In several countries, private debts arising from a property bubble were transferred to sovereign debt as a result of banking system bailouts and government responses to boost economies post-bubble. The structure of the Eurozone as a monetary union without fiscal union contributed to the crisis and harmed the ability of European leaders to respond. European banks own a significant amount of sovereign debt, such that fears regarding the solvency of banking systems or sovereigns are negatively reinforcing.

Concerns intensified in early 2010 and thereafter, leading Europe’s finance ministers in May 2010 to create the European Financial Stability Facility (EFSF) aiming at ensuring financial stability across Europe. In October 2011 and February 2012, the Eurozone leaders agreed to reinforce measures designed to prevent the collapse of member economies (e.g. an agreement whereby banks would accept a certain percentage write-off of Greek debt owed to private creditors, an increase of the EFSF to about €1 trillion, and the requirement for European banks to achieve their capitalisation). In addition of these measures, EU leaders also agreed to create a European Fiscal Compact including the commitment of each member country to introduce a balanced budget amendment. European policy makers have also proposed greater integration of EU banking management with euro-wide deposit insurance, bank oversight and joint means for the recapitalization or resolution of failing banks. The European Central Bank (ECB) has taken measures to maintain money flows between European banks by lowering interest rates and providing weaker banks (mostly from crisis countries) with cheap loans of more than one trillion Euros.

While sovereign debt has risen substantially in only a few Eurozone countries, it has become a perceived problem for the area as a whole, leading to continuous speculation of a possible disintegration of the Eurozone.
2. LESSONS OF THE EUROZONE CRISIS FOR THE FORMATION OF THE WAMZ AND EAC MONETARY UNIONS

There are certainly lessons from Europe that the West Africa and East African countries can take to heart as they attempt to move toward a single monetary union. Ongoing developments in Europe are giving policy makers within Africa in general and in both regions in particular an opportunity to rethink earlier perceptions about monetary integration issues.

In fact, the euro zone is a case study about the prominence of surveillance, harmonization and coordination of fiscal policies in the economic and monetary union and the optimal of macroeconomic framework.

Two main policy gaps in formation of the euro area have left it in its current state of instability. First, the design of the Eurozone did not provide an eventuality plan or safety measures to find appropriate solutions to sovereign debt crises. There is no protocol for member countries should they find it difficult to access markets to refinance their sovereign debt. Second, 17 sovereign fiscal authorities govern the euro, which means it takes a lot of coordination to get anything done. In addition, there are no persuasive mechanisms to enforce the commitments of member countries.

Some clear lessons emerge from the Eurozone crisis that directly relate to the WAMZ and EAC and its path toward creating a monetary union. Policymakers working on WAMZ and EAC integration should be approaching the adoption of a single monetary union with caution given the ongoing sovereign debt crisis in Europe.
First, the process of further monetary integration of the WAMZ and EAC should not be rushed. Given the circumstances in Europe, it may be wise to wait and see how the euro-area crisis is handled. This will allow policymakers in both regions to take stock of any lessons from Europe. Even before the Eurozone crisis, experts urged the WAMZ and EAC to move slowly towards the monetary union and to adopt a gradual and cautious approach.

The second takeaway from the euro-area crisis is that fiscal and monetary policies are not enough to ensure sustainability against the lack of full-blown coordination of economic policies. Euro-area countries pursued different structural policies and as a result competitiveness differentials widened throughout the decade, leading to substantial imbalances within the euro area. For instance, Germany has been able to accumulate substantial current account surpluses while the peripheral economies in Europe were running current account deficits that resulted in higher debt. Had these imbalances been corrected earlier, the crisis would have been much less severe or may not have occurred at all.

Similarly, the WAMZ and EAC countries are pursuing differing structural policies. While the WAMZ and EAC agreed upon the criteria for macroeconomic convergence, issues of fiscal sustainability have not been met by member countries. Unless, the WAMZ and EAC want to recreate the mistakes of Europe it should pay strict attention to the fiscal benchmarks and other macroeconomic convergence criterion requirements.

Finally, the euro-area crisis highlights the importance of an independent central bank for the region that will guide monetary policy formulation and implementation. In addition, the central bank must enforce prudential financial regulations for the financial sector of member countries. The West African Central Bank (WACB) and the East Africa Central Bank are planned to be formed along the lines of European Central Bank (ECB). Thus, one must consider the institutional deficiencies of the ECB in order to avoid falling into the same trap that the ECB is currently in. A crucial gap in the euro area is what to do when there is a run on government bonds since the ECB does not have a mandate to intervene. Nor is there a crisis management facility, such as an enhanced European Monetary Fund. The fiscal crisis has spilled over to the banking sector, for which there is no central supervision or a central or federal deposit insurance mechanism. In sum, both regions need to spell out safety measures and a bailout plan in case of debt or other fiscal problems among members.

The formation of the monetary union is a challenge given the great imbalance in individual national economic strengths of the WAMZ and EAC countries. They must be prepared to give up a degree of sovereignty and to converge politically to avoid collapse. The ideal integration situation is where the countries in the union share common monetary and fiscal policies, a common pool of foreign exchange reserves, and a common monetary authority or central bank. Otherwise, trying to operate a single currency without social, economic and political integration is likely to fail as evidenced by Eurozone crisis.

Instead of rushing to move into a currency union, regional integration in the WAMZ and EAC should focus more on economic integration including regional trade expansion and infrastructure coordination. Both regions should take appropriate steps and undertake more technical preparations prior to the expected implementation date to ensure that member countries will not suffer the same difficulty as those in the Eurozone. The ten-year roadmap toward monetary union recently adopted by the EAC heads of state in November 2013 is online with these recommendations.

Fiscal discipline is important as it is one key lesson that can be learnt from the Greek crisis. One key lesson that stands tall is the need for individual countries aspiring to join monetary unions to be fiscally disciplined, transparent with their economic data with their peers and committed to converging to the agreed criteria. For the EAC, an East African Surveillance, Compliance and Enforcement Commission to monitor and enforce convergence will be created by 2018 (Mira 2013).
VI. GENERAL CONCLUSION, RECOMMENDATIONS AND AREAS OF INTERVENTION BY THE AFRICAN DEVELOPMENT BANK AND OTHER DEVELOPMENT PARTNERS

As of necessity, monetary coordination and financial sector integration involve a wide range of structural and institutional measures and reforms. Given the huge number of actions and operational reforms to be implemented, the following question naturally comes to mind: which principles and criteria must be taken into consideration when setting priorities between various institutional policies and reforms?

The sequencing of priorities among measures to be taken in the financial sector, appropriate reforms scheduling and coordination are important for the following reasons: (i) an inappropriate sequencing of reforms may engender excessive risk-taking, financial instability and other adverse consequences; (ii) limited institutional capacity and human and financial resources necessarily require a prioritization of reforms; (iii) setting priorities may facilitate and foster the adoption of reforms; (iv) rushing prematurely into a monetary union without the prerequisite monetary coordination and financial integration may ultimately lead to an ineffective monetary integration. The Bank’s69 study revealed that the financial integration process in regions with different currencies has also been undermined by the lack of monetary coordination or very poor coordination.

1. COMMON CHARACTERISTICS AND KEY RECOMMENDATIONS

The report particularly asserts that unrealistic schedules, which inevitably lead to the postponement of deadlines, may undermine the credibility of the monetary union, and considerably weaken the support of market participants and the public, which is necessary for the entire process. The launch of the monetary union among WAMZ70 member countries was successively rescheduled three times (January 2003, July 2005 and December 2009) as a result of inadequate preparation. The WAMZ Heads of State and Government had decided in December 2009 that it was not feasible to introduce a single currency in the five WAMZ member countries on that date. With respect to the revised plans, WAMZ hopes to adopt a single currency called “ECO” by 201571. This objective, like previous ones, may not be achieved if member countries fail to establish effective monetary coordination and financial integration prior to the said date, in spite of some progress recorded in other areas (such as macro-economic convergence).

Similarly, in the case of the EAC, the ECB72 Staff Study also lays emphasis on the close link between monetary coordination and financial integration for sustaining the monetary union process. Hence, EAC countries which are also engaged in the process of launching their monetary union in 2024 should learn from the failures of WAMZ.

Consequently, both regions (EAC and WAMZ) should adopt a realistic, pragmatic and gradual approach to conducting the financial and monetary integration process. The report suggests a few concrete solutions that contribute to fostering the integration process in both regions.

2. Supporting the Process of Monetary Coordination and Regional financial integration: Areas of Intervention by the African Development Bank and other Development Partners

The above review has revealed various areas where donor assistance could advance monetary coordination and regional financial integration in the two regions studied here. These areas, which relate to monetary integration strategy in general, financial infrastructure, and financial institutions and policies, are categorized in Table 6 below within four broad categories: (i) Policy

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70. Nigeria, Ghana, Guinea, Gambia, Sierra Leone. Liberia joined WAMZ starting 1 January 2010.
71. The new 2015 date was adopted at the 24th meeting of the Convergence Council of Ministers and Governors of the West African Monetary Zone in Abuja, Monday June 22nd, 2009.
72. ECB, Study on the Establishment of a Monetary Union among the Partner States of the East African Community, ECB Staff Study, February 2010.
Action Frameworks, (ii) Capacity Building /Governance, (iii) Advocacy, and (iv) Finance. As mentioned in individual regional reviews above, these areas will need further discussion among the Bank, the two RECs, member countries, and other development partners.

The annex 3 provides some on-going and planned projects of Key Development Partners (including the African Development Bank) to support the Monetary Coordination and Financial Sector Integration Process in the East African Community.

<table>
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<tr>
<th>Proposal</th>
<th>Policy Action Frameworks</th>
<th>Capacity Building/Governance</th>
<th>Advocacy</th>
<th>Finance</th>
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<tr>
<td>Monetary Coordination (MC) &amp; Regional financial integration (RFI) Framework</td>
<td>Sharpen Regional Action Plans</td>
<td>Strengthen regional secretariats’ and other regional institutions capacity (WAMI, EAC Secretariat, PTS, etc.)</td>
<td>Policy dialogue</td>
<td>Financial assistance (consultants, experts, etc.)</td>
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<td></td>
<td>Coordinated national Action Plans</td>
<td>Strengthen national coordinating body</td>
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<td></td>
<td>Coordination of MC &amp; RFI programs</td>
<td>Institution building for Central Banks to improve the efficiency of monetary and exchange rate policies</td>
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<td>Financial Infrastructure</td>
<td>RISPs/ CSPs/FSAPs</td>
<td>Supervisory bodies, central banks, national governments, development of the payments systems at the regional and country levels</td>
<td>Policy dialogue</td>
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<td>Supervision &amp; regulation</td>
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<td>Financial assistance (consultants, experts, etc.)</td>
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<td>Legal systems, property rights, judiciary</td>
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<td>Loans &amp; grants</td>
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<td>Financial Institutions</td>
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<td>Strengthen central banks’ capacity</td>
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<td>Monitoring &amp; Evaluation mechanisms</td>
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<td></td>
<td>Strengthen financial markets</td>
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<td>Workshops/training institutions</td>
<td>Financial assistance (consultants, experts, etc.)</td>
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<td></td>
<td>Link/merge financial markets</td>
<td>e.g.: technical assistance to be provided to the Training Institute for financial markets operators based in Kampala (Uganda)</td>
<td>Equity, loans &amp; grants</td>
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<td></td>
<td>Link the different financial markets with the national payments systems</td>
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<td>Capacity building of the markets operators</td>
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<td>Implement regional &amp; national credit bureaus/ information systems</td>
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<td></td>
<td>Strengthen other financial institutions’ capacity</td>
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<tr>
<td>Financial Policies</td>
<td>Harmonization and coordination of monetary and exchange rate policy frameworks</td>
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<td>Workshops/training institutions</td>
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<td></td>
<td>Harmonization of banking supervision</td>
<td>e.g.: technical assistance to be provided to the Training Institute for financial markets operators based in Kampala (Uganda)</td>
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<td>Implementation of cross-border banking and consolidated supervision</td>
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<td>Harmonization of regulatory frameworks for other institutions (Pension funds &amp; Insurance, MFI s, etc.)</td>
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<td></td>
<td>Harmonization of statistical concepts, methods, and definitions</td>
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<td></td>
<td>Liberalization of exchange controls</td>
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<td></td>
<td>Region-wide policies for cross-border financial transactions</td>
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</table>
VI. ANNEXES

ANNEX 1. Stages towards the Economic and Monetary Union (EMU) in the European Community

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<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>• Launching of the European Monetary System (EMS) in 1979 as a forerunner of the Economic and Monetary Union (EMU)</td>
<td>• Complete freedom for capital transactions</td>
<td>• Establishment of the European Monetary Institute (EMI) in 1994</td>
<td>• Irrevocable fixing of conversion rates</td>
</tr>
<tr>
<td>• Signature of the Maastricht Treaty in 1992</td>
<td>• Increased co-operation between central banks</td>
<td>• Ban on the granting of central bank credit to the public sector</td>
<td>• Introduction of the euro</td>
</tr>
<tr>
<td></td>
<td>• Free use of the ECU (European Currency Union, forerunner of the Euro)</td>
<td>• Increased co-ordination of monetary policies</td>
<td>• Conduct of the single monetary policy by the ESCB</td>
</tr>
<tr>
<td></td>
<td>• Improvement of economic convergence</td>
<td>• Strengthening of economic convergence</td>
<td>• Entry into effect of the intra-EU exchange rate mechanism (ERM II)</td>
</tr>
<tr>
<td></td>
<td>• Full achievement of a single European market through the dismantling of all internal barriers to the free movement of persons, goods, capital and services within Europe.</td>
<td>• Process leading to the independence of the national central banks, to be completed at the latest by the date of establishment of the European System of Central Banks (ESCB) and the European Central Bank (ECB)</td>
<td>• Entry into force of the Stability and Growth Pact</td>
</tr>
</tbody>
</table>

Source: www.ecb.int.

ANNEX 2. WAMZ Strategic Plan: 2010-2015

WAMI’s Strategic Plan for 2010-2015 is based on five pillars corresponding to current and future major challenges of the zone and covering the key functions of the Institute. The key components of the Plan are as follows:

• Macro-economic convergence and statistical harmonization;
• Regional trade and integration;
• Financial integration;
• Payments system infrastructure; and
• Institutional capacity building.
### PILLAR I: MACROECONOMIC CONVERGENCE AND STATISTICAL HARMONIZATION

<table>
<thead>
<tr>
<th>Objective</th>
<th>Strategies</th>
<th>Measures</th>
<th>Time Frame</th>
<th>Indicators</th>
<th>Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Monetary Policy Strategy</strong></td>
<td>Design a monetary policy framework</td>
<td>Review monetary policy framework from other region/countries and analyse the monetary and inflation targeting framework</td>
<td>2010-2014</td>
<td></td>
<td>WAMI and Expert Group</td>
</tr>
<tr>
<td><strong>Framework for the harmonization of money and banking statistics in the WAMZ.</strong></td>
<td>Design the framework</td>
<td>1. Submit proposed framework for the Consideration and validation by the WAMZ Experts Committee on harmonization of money and banking statistics in the WAMZ. 2. Implement Harmonized Framework in the WAMZ Multilateral Surveillance System</td>
<td>2010-2013</td>
<td>Harmonized banking statistics</td>
<td>WAMI and member Countries</td>
</tr>
<tr>
<td><strong>WAMZ Statistical Database</strong></td>
<td>Preparation of statistical Tables to Country Reports and Zonal Macroeconomic Convergence Reports</td>
<td>1. Undertake an exercise to extend existing WAMZ country data sets (2000-2015) going as far back to at least 1980 for the and on selected economic indicators. 2. Continue to pursue collaboration with ECOWAS/ ADB/ World Bank on Statistical Harmonization and Database Development:</td>
<td>2010-2014</td>
<td>Accurate and updated database</td>
<td>WAMI and other Institutions</td>
</tr>
</tbody>
</table>
### PILLAR II: TRADE AND REGIONAL INTEGRATION

<table>
<thead>
<tr>
<th>Objective</th>
<th>Strategies</th>
<th>Measures</th>
<th>Time Frame</th>
<th>Indicators</th>
<th>Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promotion of good trade governance</td>
<td>Promote compliance with bilateral, regional and multilateral trade agreements and decisions</td>
<td>Advocacy-meetings with countries relevant authorities Streamlining record keeping of agreements Publicizing agreements Making agreements accessible to the public Build capacity in trade negotiations and implementation of agreements/decisions</td>
<td>Jan. 2010 Dec. 2012</td>
<td>Agreements are domesticated Reports Reduction in incidence of non-compliance</td>
<td>Member countries/ WAMI</td>
</tr>
<tr>
<td></td>
<td>Set up rules of origin sub-committee</td>
<td>Inaugurate sub-committee Source funding</td>
<td>Jan. 2010 Dec. 2010</td>
<td>Sub-committee is operational</td>
<td>Ministry of Trade/WAMI/ ECOWAS Expert Working Group</td>
</tr>
<tr>
<td></td>
<td>Sensitisation of stakeholders on good trade practice</td>
<td>Country -wide sensitization</td>
<td>Jan. 2010 Dec. 2014</td>
<td>Agreed document on what good trade practice is Number of sensitisation activities held</td>
<td>WAMI/Ministry of Trade</td>
</tr>
<tr>
<td></td>
<td>Promote hosting of website in member countries for public education on cross-border trade and investment rules and initiatives</td>
<td>Member countries to provide facilities for purpose Seek assistance from partners</td>
<td>Jan. 2010 Dec. 2014</td>
<td>Website for purpose hosted</td>
<td>WAMI/Ministry of Trade</td>
</tr>
<tr>
<td></td>
<td>Publish records of member countries progress on compliance with decisions</td>
<td></td>
<td>Jan. 2010 Dec. 2011</td>
<td>Records published</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td>Facilitate implementation of consumer protection policies</td>
<td>Countries given guidelines on policy Sensitise public on importance of such a policy and feature it in newsletter</td>
<td>Jan. 2010 Dec. 2012</td>
<td>Competition policy introduced Policy features in newsletter</td>
<td>WAMI/Ministry of Trade</td>
</tr>
<tr>
<td>Objective</td>
<td>Strategies</td>
<td>Measures</td>
<td>Time Frame</td>
<td>Indicators</td>
<td>Responsibility</td>
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<tr>
<td>Capital Market Development and Integration</td>
<td>Set up a Regional Capital Market Development Committee (RCMDC)</td>
<td>Advocacy and invitation to formal inaugural meeting of the Regional Capital Market Development Committee (RCMDC)</td>
<td>Jan. 2010 Dec. 2010</td>
<td>RCMDC owns and interact with Stakeholder Committees</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td>Promote deepening of the bonds market</td>
<td>Broaden and deepen the domestic market for government securities - grow market for fixed incomes</td>
<td>Jan. 2010 Dec. 2014</td>
<td>developed new financial instruments such as fixed income securities</td>
<td>Central Banks Expert Working Group Meetings, Convergence Council</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lengthen maturity of government instruments and promote the issuance of corporate bonds by the private sector</td>
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<td>Ministry of Finance</td>
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<td>Central Bank</td>
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<td>Ministry of Finance</td>
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<td>Central Bank</td>
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PILLAR III: FINANCIAL SECTOR INTEGRATION
<table>
<thead>
<tr>
<th>Objective</th>
<th>Strategies</th>
<th>Measures</th>
<th>Time Frame</th>
<th>Indicators</th>
<th>Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Integrating the Banking Sector</td>
<td>Harmonization of regulatory and supervisory frameworks</td>
<td>Promote cross-border financial services</td>
<td>Jan. 2010</td>
<td>MoU signed and implemented on cross-border supervision</td>
<td>Expert Working Group Meetings, Convergence Council</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Strengthen cross-border supervision</td>
<td>Dec. 2010</td>
<td>Reports on harmonization of regulatory and supervisory practices</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Promote Credit Bureau and Credit Rating systems</td>
<td>Regional credit reporting system and information sharing for soundness of the financial sector</td>
<td>Jan. 2010</td>
<td>Regional credit information sharing platform</td>
<td>Central Banks</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Dec. 2010</td>
<td>Reports on harmonized reporting and accounting framework</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Promote and harmonize reporting frameworks and accounting practices</td>
<td></td>
<td>Jan. 2010</td>
<td></td>
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</tr>
<tr>
<td></td>
<td>Improve the Interbank and Deepen the Money Market</td>
<td>Deepen the market with more instruments</td>
<td>Jan. 2010</td>
<td>Increase in the number of bank supervisors with additional skills</td>
<td>Expert Working Group Meetings, Convergence Council</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Maintain liquidity and marketability of instruments</td>
<td>Dec. 2014</td>
<td></td>
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</tr>
<tr>
<td></td>
<td>Promote Capacity Building of bank supervisors</td>
<td>Promote Trade in cross border insurance services</td>
<td>Jan. 2010</td>
<td></td>
<td>Expert Working Group Meetings, Convergence Council</td>
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<td></td>
<td></td>
<td></td>
<td>Dec. 2014</td>
<td></td>
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<tr>
<td></td>
<td>Set up Regional Forum for Insurance Supervisors</td>
<td></td>
<td>Jan. 2010</td>
<td>Records published</td>
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<td></td>
<td></td>
<td></td>
<td>Dec. 2014</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Harmonization of regulatory and supervisory frameworks</td>
<td></td>
<td>Jan. 2010</td>
<td>Competition policy introduced Policy features in newsletter</td>
<td>Expert Working Group Meetings, Convergence Council</td>
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<td></td>
<td></td>
<td></td>
<td>Dec. 2010</td>
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<tr>
<td></td>
<td>Promote Capacity Building for Insurance Supervisors</td>
<td></td>
<td>Jan. 2010</td>
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<td></td>
<td></td>
<td></td>
<td>Dec. 2014</td>
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**Integrating the Insurance Sector for Cross Border Services**
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<thead>
<tr>
<th>Objective</th>
<th>Strategies</th>
<th>Measures</th>
<th>Time Frame</th>
<th>Indicators</th>
<th>Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regional Currency Convertibility/Quoting and trading of regional currencies</td>
<td>Sensitization of Operators on currency convertibility arrangement</td>
<td>Seek Central Bank Support or guarantee as buyer of last resort</td>
<td>Jan. 2010 Dec. 2014</td>
<td></td>
<td>Central Banks</td>
</tr>
<tr>
<td></td>
<td>Framework on Design, Demand and Supply Issues</td>
<td>Draw up a sequencing of activities leading to introduction of Eco Physical Currency</td>
<td>July 2010 Sept. 2011</td>
<td>Documented sequencing paper</td>
<td>WAMI</td>
</tr>
<tr>
<td>Preparation Towards the introduction of the Eco</td>
<td></td>
<td>Determine the volume of the Eco bank notes and coins to be printed in number and column of the denomination and the boundary between coins and banknotes</td>
<td>Jan. 2010 Oct. 2010</td>
<td>Policy paper approved by Convergence Council</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Select themes on which to base design of the Eco Physical currency</td>
<td>Dec. 2010 Jun. 2011</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>Set up and Inaugurate National Steering Committee</td>
<td>Sept. 2010 Dec. 2011</td>
<td>Prepare position paper on themes to be approved by Convergence Council</td>
<td></td>
</tr>
<tr>
<td>Objective</td>
<td>Strategies</td>
<td>Measures</td>
<td>Time Frame</td>
<td>Indicators</td>
<td>Responsibility</td>
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<tr>
<td>Preparation Towards the introduction of the Eco (Contd.)</td>
<td>Framework on Design, Demand and Supply Issues (Contd.)</td>
<td>Provide alternate design themes and features of the Eco banknotes and coins through a competitive process</td>
<td>Jan. 2010 - Jun. 2011</td>
<td>Approved by Convergence Council</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Evaluate proposals to select winning designs</td>
<td>Jan. 2010 - Oct. 2010</td>
<td>TOR and Bid process concluded</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Identify Steps and procedures for Smooth Changeover from National Currencies to Eco Currency</td>
<td>Undertake scenario analysis on the appropriateness of time</td>
<td>July 2010 - Sept. 2011</td>
<td>Change over plan document</td>
<td>WAMI, Convergence Council</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Assess logistics and banking and financial community changeover plan for the virtual currency</td>
<td>July 2011 - Dec. 2011</td>
<td></td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Determine the bilateral exchange rates of the WAMZ currencies and the Eco - unit of account and implement ERM III</td>
<td>Jan. 2010 - Dec. 2014</td>
<td>Approve new ERM</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Determine the external value of the Eco currency against internal currencies</td>
<td>July 2011 - Dec. 2011</td>
<td></td>
<td>WAMI</td>
</tr>
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</table>
PILLAR IV: PAYMENTS SYSTEM INFRASTRUCTURE

<table>
<thead>
<tr>
<th>Specific Objectives</th>
<th>Strategies</th>
<th>Activities</th>
<th>Timeframe Commencement</th>
<th>Timeframe Completion</th>
<th>Indicators</th>
<th>Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Development of the basic infrastructure of the financial sector, through the modernization of the payment systems of The Gambia, Guinea and Sierra Leone.</td>
<td>Harmonize technology platform and protocols</td>
<td>(i) Set up a sub-committee to investigate the following: • Industry technical standards • Rules and regulations/guidelines • Interconnection and interoperability between different infrastructure, systems and products (ii) Engage a single Solution Provider for each component in the three countries</td>
<td>January 2010</td>
<td>December 2011</td>
<td>(i) Modernized payment systems in The Gambia, Guinea and Sierra Leone (ii) Same day funds transfer (iii) Published list of approved payments standards for the WAMZ (iv) the percentage of citizens of WAMZ with access to the financial sector increase to 15% by 2011, from 8%</td>
<td>(i) WAMI, (ii) Standards &amp; IT Tech Sub-Committee (iii) Regulation, legal, &amp; Institutional Framework Tech. Sub. Committee</td>
</tr>
<tr>
<td>2. Acquisition and Installation of ECOWAN73</td>
<td>Integrate ICT information processing channels in WAMZ sub-region</td>
<td>(i) conduct systems engineering and integration (ii) Build WACB-Net Point of Service infrastructure (iii) Initiate content development and procurement (iv) Connect all participants on payment systems to ECOWAN (v) Organise workshops and seminars for the stakeholders</td>
<td>2010</td>
<td>2015</td>
<td>(i) Integrated regional payments system (ii) Real-time mirroring of transactions between two sites (iii) Real-time capturing of statistical information and computation of bank reserves (iv) Cross-border fund transfers on real-time basis.</td>
<td>(i) WAMI (ii) Standard and IT Tech. Sub-Committee (iii) Retail and Wholesale Tech. Sub-Committees</td>
</tr>
<tr>
<td>3. Creation of the necessary enabling environment for the financial system.</td>
<td>Domesticate the WAMZ Payments System Statute</td>
<td>(i) Hold stakeholders Meetings (ii) Sensitize the WAMZ member countries</td>
<td>January 2010</td>
<td>December 2010</td>
<td>Codified WAMZ payments system law.</td>
<td>(i) WAMI (ii) Regulatory, legal &amp; Institutional Framework Sub-Committee</td>
</tr>
<tr>
<td></td>
<td>Rules and regulation for all payment streams</td>
<td>(i) Review international best practices regarding rules and regulations governing payment instruments/products, and private systems (ii) Sensitize the stakeholders</td>
<td>January 2010</td>
<td>September 2011</td>
<td>(i) Codified Rules and Regulations</td>
<td>-idem-</td>
</tr>
</tbody>
</table>

73. ECOWAS Wide Area Network.
<table>
<thead>
<tr>
<th>Specific Objectives</th>
<th>Strategies</th>
<th>Activities</th>
<th>Timeframe commencement</th>
<th>Timeframe Completion</th>
<th>Indicators</th>
<th>Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>4. Development of an integrated regional platform for card transactions</td>
<td>Promote regional platform for card transactions</td>
<td>(i) Develop a framework for card payments and settlements in the WAMZ (ii) Review international best practices (iii) Inter-connect the national switches for interoperability</td>
<td>June 2010</td>
<td>December 2013</td>
<td>(i) Integrated regional platform for cross-border card transactions (ii) Share of intra-trade to total trade among WAMZ countries increase to 10% by 2014, from a low of 2.3%</td>
<td>WAMI (i) Retail Payments System Sub-Committee (ii) Standard and IT Sub-Committee (iv) Regulatory &amp; Legal Framework Committee</td>
</tr>
<tr>
<td>6. Development of WACB payment System infrastructure and Common database for the WAMZ</td>
<td>(i) Promote the development of WACB Payment Mechanism (Computer Centre, GL system, CBA, RTGS central hub, CSD, LAN, MAN, etc.) (i) Seek tech. and financial assistance (i) Build the computer centre of the WACB (ii) Conduct Systems engineering and integration (ii) Link the RTGS of the NCBs to the WACB Central hub (ii) Country-wide sensitisation/ workshops</td>
<td>December 2013</td>
<td>January 2015</td>
<td>(i) Integrated regional Payments system (ii) The share of formal trade to total trade increase to 20% from 10% in 2014. (iii) Consumer framework (iv) Increased use of electronic modes of payment (v) Fast and reliable cross-border transfers</td>
<td>WAMI (i) Retail Payment Sub. Committee (ii) Standard &amp; IT Sub-Committee (iii) Regulatory and Legal Committee</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(ii) Promote the development of Database for the WAMZ</td>
<td>(i) Investigate the industry technical standards (ii) Seek tech. and financial assistance (iii) Establish WAMZ database</td>
<td>December 2013</td>
<td>January 2015</td>
<td>(i) Consumer protection framework in the zone (ii) Information sharing on end-users of the financial system</td>
<td>WAMI (i) Standard &amp; IT Sub-Committee (ii) Retail Payment Sub. Committee (ii) Regulatory and Legal Committee</td>
</tr>
</tbody>
</table>
## PILLAR V: INSTITUTIONAL AND CAPACITY BUILDING:

<table>
<thead>
<tr>
<th>OBJECTIVES</th>
<th>STRATEGIES</th>
<th>MEASURES</th>
<th>TIMEFRAMES</th>
<th>INDICATORS</th>
<th>RESPONSIBILITY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal framework for introduction of the eco</td>
<td>Strengthen capacity by organizing study visits to monetary institutions / organizations to learn from their experiences</td>
<td>Draft legal instruments for the introduction of the eco</td>
<td>2010 - 2012</td>
<td>Legal instruments for the introduction of the eco</td>
<td>WAM/LIC</td>
</tr>
<tr>
<td>Legal framework for Accounting and Statistics</td>
<td>Strengthen capacity by organizing study visits to monetary institutions / organizations to learn from their experiences. Organise meeting of Member States to develop legal framework.</td>
<td>Draft legal instruments to Accounting and Statistics</td>
<td>2010 - 2012</td>
<td>Legal instruments for Accounting and Statistics</td>
<td>WAM/ Member States</td>
</tr>
<tr>
<td>Build support for the WAMZ programme</td>
<td>Create awareness, in the stakeholders, of the progress of the WAMZ programme</td>
<td>Distribute brochures, pamphlets, leaflets and posters on the WAMZ programme</td>
<td>2010 - 2014</td>
<td>Evaluation results show support for the WAMZ programme</td>
<td>WAM/NSCs</td>
</tr>
<tr>
<td></td>
<td>Publicize the benefits of the WAMZ programme to stakeholders through different media</td>
<td>Distribute sensitization materials on the benefits of the WAMZ programme</td>
<td>2010 - 2014</td>
<td>Evaluation results indicate stakeholders know the benefits of the WAMZ programme</td>
<td>WAM/NSCs</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Hold interviews on radio and television on the benefits of the WAMZ programme</td>
<td>2010 - 2014</td>
<td>Level of response to interview programmes</td>
<td>WAMI</td>
</tr>
<tr>
<td>Make National Sensitization Committees (NSCs) effective implementers of the sensitization programme</td>
<td>Build capacity in the NSCs to plan and implement sensitization activities</td>
<td>Hold training workshops for NSCs at WAMI and in member countries</td>
<td>2010</td>
<td>Number of training workshops run for NSCs</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Source funding for capacity development for NSC members</td>
<td>2010 - 2014</td>
<td>Donor funds secured</td>
<td>WAMI</td>
</tr>
<tr>
<td>Develop a sense of ownership of the programme in the stakeholders</td>
<td>Give responsibility for organizing some sensitization activities to more stakeholder groups</td>
<td>Allow some stakeholder groups organize sensitization activities</td>
<td>2010 - 2014</td>
<td>Number of workshops organized by stakeholder groups</td>
<td>WAMI/Stakeholder groups</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Invite stakeholders to planning meetings</td>
<td>2010 - 2014</td>
<td>Number of stakeholders participating in planning meetings</td>
<td>WAMI</td>
</tr>
<tr>
<td>Improve WAMI’s capacity to carry out sensitization activities at both the national and zonal level</td>
<td>Capacity building for WAMI staff</td>
<td>WAMI staff go to training programmes and workshops on sensitization</td>
<td>2010 - 2013</td>
<td>Training programs and workshops attended</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Study visit to ECB to learn from their sensitization experience</td>
<td>2010 - 2014</td>
<td>Visits made to ECB</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Budget for WAMI sensitization programme</td>
<td>2010 - 2012</td>
<td>Amount budgeted for sensitization activities</td>
<td>WAMI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Source funds from donors</td>
<td>2010 - 2014</td>
<td>Level of donor support</td>
<td>WAMI</td>
</tr>
</tbody>
</table>
### Establishment of an institutional structure for the WACB

<table>
<thead>
<tr>
<th>Action</th>
<th>Responsible Parties</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adoption of central banking system</td>
<td>WAMI Committee of Governors/WAMI</td>
</tr>
<tr>
<td>Adoption of WACB Statute</td>
<td>WAMI Convergence Council/WAMI</td>
</tr>
<tr>
<td>Ratification of the Statute</td>
<td>Member States/WAMI</td>
</tr>
<tr>
<td>Establishment of an institutional structure for the WACB (cont’d)</td>
<td></td>
</tr>
<tr>
<td>Establish an appropriate capital base for the WACB</td>
<td>Working paper on an appropriate capital base for the WACB</td>
</tr>
<tr>
<td>Provide adequate capital base for the take-off of the WACB</td>
<td>Preparation of contributions table in tranches for Member States</td>
</tr>
<tr>
<td>Acquisition of the WACB building</td>
<td></td>
</tr>
<tr>
<td>Ensure the delineation and initial set-up of the offices</td>
<td></td>
</tr>
<tr>
<td>Consultancies for the Accounting &amp; Budgetary procedures, auditing manual and human resources manual for the WACB</td>
<td></td>
</tr>
<tr>
<td>Board appointments &amp; Staffing of the WACB</td>
<td></td>
</tr>
<tr>
<td>Ensure member countries make Contributions to the SCF</td>
<td></td>
</tr>
<tr>
<td>Operationalization of the SCF</td>
<td></td>
</tr>
</tbody>
</table>

### Establishment of an institutional structure for the WACB (cont’d)

<table>
<thead>
<tr>
<th>Action</th>
<th>Responsible Parties</th>
</tr>
</thead>
<tbody>
<tr>
<td>Review and approval of the WACB capital base</td>
<td>Approval by Council</td>
</tr>
<tr>
<td>Preparation of Budget for the WAMZ Secretariat</td>
<td>Preparation of activities for Commencement of the WACB</td>
</tr>
<tr>
<td>Preparation of Budget for the WAMZ Secretariat</td>
<td>Preparation of activities for Commencement of the WACB</td>
</tr>
<tr>
<td>Preparation of Budget for the WAMZ Secretariat</td>
<td>Preparation of activities for Commencement of the WACB</td>
</tr>
<tr>
<td>Preparation of Budget for the WAMZ Secretariat</td>
<td>Preparation of activities for Commencement of the WACB</td>
</tr>
<tr>
<td>Acquisition of the WACB building</td>
<td>Building and all necessary infrastructures ready</td>
</tr>
<tr>
<td>Ensure the delineation and initial set-up of the offices</td>
<td>Offices ready for occupation</td>
</tr>
<tr>
<td>Consultancies for the Accounting &amp; Budgetary procedures, auditing manual and human resources manual for the WACB</td>
<td>Procedural manuals for the WACB prepared</td>
</tr>
<tr>
<td>Board appointments &amp; Staffing of the WACB</td>
<td>Staff and board appointments carried out as well as training/induction</td>
</tr>
<tr>
<td>Ensure member countries make Contributions to the SCF</td>
<td>Table of contributions in tranches prepared</td>
</tr>
</tbody>
</table>

### Activation of WAMZ Institutions WACB

<table>
<thead>
<tr>
<th>Action</th>
<th>Responsible Parties</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regular consultation with the Ghanaian Authorities on provision of the building &amp; other infrastructures</td>
<td>Building and all necessary infrastructures ready</td>
</tr>
<tr>
<td>Assign office area and fit equipment and fittings</td>
<td>Offices ready for occupation</td>
</tr>
<tr>
<td>Review the existing manuals</td>
<td>Procedural manuals for the WACB prepared</td>
</tr>
<tr>
<td>Appointment of the Executive Board of the WACB</td>
<td>Staff and board appointments carried out as well as training/induction</td>
</tr>
<tr>
<td>Recruitments required staff of the WACB</td>
<td>Table of contributions in tranches prepared</td>
</tr>
<tr>
<td>Preparation of contributions table in tranches for Member States</td>
<td>Contributions by member countries received</td>
</tr>
<tr>
<td>Dispatch of demand/ notification letters to Member States</td>
<td>Contributions by member countries received</td>
</tr>
<tr>
<td>Payment of contributions by Member States</td>
<td>Contributions by member countries received</td>
</tr>
</tbody>
</table>
## Operationalization of WAFSA

<table>
<thead>
<tr>
<th>Activity</th>
<th>Description</th>
<th>Timeframe</th>
<th>Responsible Party</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquisition of the WAFSA building</td>
<td>Board appointments &amp; Staffing of the WAFSA</td>
<td>Ensure the delineation and initial set up of the offices</td>
<td>Q3 2009 - Q4 2013</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Q4 2013 - Q4 2013</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Q4 2013 - Q2 2014</td>
</tr>
<tr>
<td></td>
<td>Recruitment exercise for staff and the appointment of the Board of Directors</td>
<td>Assign office area and fit equipment and fittings</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Regular consultation with the Nigerian Authorities on developments</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Procurement and installation of ICT infrastructure for operational functions</td>
<td>Procurement and installation of ICT infrastructure for policy functions</td>
<td>Q3 2013 - Q1 2014</td>
</tr>
</tbody>
</table>

## Establishment and operationalization of the WAMZ Secretariat

<table>
<thead>
<tr>
<th>Activity</th>
<th>Description</th>
<th>Timeframe</th>
<th>Responsible Party</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquisition of the Secretariat building</td>
<td>Initial set up of the offices</td>
<td>Board appointments &amp; Staffing of the Secretariat</td>
<td>Q3 2009 - Q4 2013</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Q4 2013 - Q4 2013</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Q4 2013 - Q2 2014</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Q3 2013 - Q1 2014</td>
</tr>
<tr>
<td></td>
<td>Setting up the offices</td>
<td>Appointment of the Board of Directors</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Regular consultation with the Guinean Authorities on developments</td>
<td>Recruitment of required staff of the Secretariat</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Procurement and installation of infrastructure</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>ICT infrastructure for operational functions</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>ICT infrastructure for policy functions</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Development of ICT Infrastructure

<table>
<thead>
<tr>
<th>Activity</th>
<th>Description</th>
<th>Timeframe</th>
<th>Responsible Party</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ensure the provision of ICT infrastructure for operational functions</td>
<td>Procurement and installation of infrastructure</td>
<td></td>
<td>WAMI/Member States</td>
</tr>
<tr>
<td></td>
<td>Procurement and installation of infrastructure</td>
<td>Q3 2013 - Q1 2014</td>
<td>WAMI/Member States</td>
</tr>
</tbody>
</table>

## Establishment of national Steering Committee

<table>
<thead>
<tr>
<th>Activity</th>
<th>Description</th>
<th>Timeframe</th>
<th>Responsible Party</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ensure full co-operation and effective coordination among all stakeholders throughout the process and after integration</td>
<td>Regular consultations with Member States</td>
<td></td>
<td>Member States/ WAMI</td>
</tr>
<tr>
<td></td>
<td>Appointment of members in various Member States and WAMI staff (task force)</td>
<td>Q3 2009 - Q2 2014</td>
<td>National Steering is established and Operationalized</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Q3 2009 ongoing</td>
<td>Member States</td>
</tr>
</tbody>
</table>
ANNEX 3. Support of Key Development Partners to the Monetary Coordination and Financial Sector Integration Process in the East African Community

This annex summarizes the following projects and programmes of assistance to the financial integration and monetary coordination process: (i) the EAC Financial System Development and Regionalization Project supervised by the World Bank; (ii) the Swedish International Development Agency (SIDA), IFC and World Bank Project for Regionalization of the EAC Financial Markets under the ESMID overall programme; (iii) the Assistance of the European Central Bank for the Establishment of a Monetary Union among EAC member States; (iv) the IMF Project for Regionalization of the EAC Financial System; and (v) the ADB and USAID Project to Develop and Integrate the EAC Payments System.

1. EAC Financial System Development and Regionalization Project supervised by the World Bank

The key objective of the project (EAC FSDRP), whose Protocol was signed in April 2010, is to sustain the broadening and deepening of the financial sector through the establishment of a single financial services market among EAC member States, with the ambition of developing a broad range of financial products and services, accessible to all segments of the population at affordable cost. The project was developed in close cooperation with the World Bank (IDA), the International Organization of Securities Commissions (IOSCO), the DFID and SIDA. It is expected that other bodies or donors would join the partnership and that the EAC Secretariat will be responsible for mobilizing other donors.

This key objective should be achieved at the end of the 9-year project duration through two successive projects: FSDRP I from the first quarter of 2011 to the first quarter of 2014 and FSDRP II which would be implemented between 2014 and 2009. The set objectives of each component (or thrust) are described in the table below. The second project component, which should cover 6 years (2014-2019), is intended to support the achievement of significant progress with a view to establishing a single financial services market within the EAC.

<table>
<thead>
<tr>
<th>Component/Thrust</th>
<th>Objectives</th>
</tr>
</thead>
<tbody>
<tr>
<td>Component 1 - Financial inclusion and strengthening of market participants</td>
<td>Leverage the establishment of a common market and the benefits of economies of scale associated with regionalization, and make a broader range of formal financial products/services available to a greater number of users (including the currently financially excluded segment of the population).</td>
</tr>
<tr>
<td>Component 2 - Harmonization of financial laws and regulations</td>
<td>Move towards legal and regulatory harmonization in banking and accounting standards, securities markets, pensions and investment funds, pivotal to achieving an effective functioning of a common financial services market through instruments to be enacted by the EAC Secretariat.</td>
</tr>
<tr>
<td>Component 3 - mutual recognition of supervisory agencies</td>
<td>Support the establishment of a system wherein a financial institution or market broker licensed by the supervisory authority in one Member State shall be allowed to operate in all the member States upon simple notification to the supervisory authority in the host country.</td>
</tr>
<tr>
<td>Component 4 - Integration of financial market infrastructure</td>
<td>Support the creation of an efficient market infrastructure, compatible at the regional level.</td>
</tr>
<tr>
<td>Component 5 - Development of a regional bond market</td>
<td>Support the development of a bond market for government securities in each of the member countries, and allow issuers of debentures in the various EAC member countries access to pool liquidities on a single market.</td>
</tr>
<tr>
<td>Component 6 - Capacity building</td>
<td>It will strengthen capacity at both the regional (including the EAC Secretariat) and the national level to ensure that the integrated market functions effectively and that all economic agents in the regional area are aware of and able to realize the benefits of the integration process.</td>
</tr>
</tbody>
</table>

74. For example, a request of the EAC Secretariat was forwarded to the ADB to participate in this project, particularly in the areas of payments systems and microfinance.
2. SIDA, EFC and World Bank Project for Regionalization of EAC Financial Markets under the ESMID Overall Programme

The EAC Financial Markets (stocks and bonds markets) Regionalization Project ties with of the ESMID overall programme implemented by SIDA, SFI and the World Bank, to foster institutional development and the efficiency of capital markets in Africa.

This project, which aims at developing stocks and bonds markets in EAC countries and at facilitating the issuance of regional bonds and cross-border stock transactions, is an integral part of the FSDRP.

3. European Central Bank Assistance for the Establishment of a Monetary Union among EAC member States

Commissioned by the EAC Secretariat in 2009, the European Central Bank (ECB), in cooperation with the EAC central banks, completed a study on the establishment of a monetary union among the Partner States of the East African Community in January 2010.

The objective of this study is to guide the EAC in its endeavours to establish a monetary union among its Partner States. Based on EU experience gained particularly by the ECB and its predecessor, the EMI, the study shows what measures should be taken in the process towards the East African Monetary Union (EAMU).

The ECB study proposes a strategy which would be appropriate for the EAC to achieve monetary union (EAMU). It weighs two options: (i) one option is to consider EAMU as a goal, with no firm published timeframe until all prerequisites appear to be within reach, while taking measures leading in the right direction. (ii) Under the other option, Partner States would commit themselves to a firm date for the start of EAMU and to fulfilling the relevant prerequisite conditions, while relying on an institutional drive to act as a catalyst for implementing the necessary preparatory work and reforms.

However, the study maintains that it would be difficult to fulfil all prerequisite conditions for the formation of the monetary union by 2012. It further suggests that key components of the basic infrastructure (Monetary Union Protocol and Statutes of EAMI and EACB) be adopted prior to that date, and the EAMI established. This study provides the below roadmap towards the establishment of a monetary union.

4. IMF Project for Regionalization of the EAC Financial System

The IMF is undertaking a regional financial sector project focused on financial stability and integration in EAC countries. The project will assess the soundness of the region’s financial systems and policy frameworks; examine cross-border/sector linkages and related policy challenges; and evaluate the degree of harmonization of institutional and regulatory infrastructures. It will assess the robustness of and recommend policies to strengthen the financial stability frameworks in the Partner States, and help to improve their positioning vis-à-vis the EAC’s financial integration agenda, especially concerning liberalization and regulatory harmonization.

Four main areas are covered by the project, namely: (i) soundness of financial systems; (ii) crises prevention and management; (iii) analysis and oversight of cross-border financial relations; and (iv) harmonization of monetary and financial policy objectives.
<table>
<thead>
<tr>
<th>Stages</th>
<th>Justification</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal and institutional changes and logistical preparations required for monetary union - the need for political commitment and public awareness</td>
<td>The project to establish a monetary union and introduce a single currency requires that the objective, timetable, resources and procedures necessary for its achievement be provided for in legal instruments.</td>
</tr>
</tbody>
</table>
| 1. Macro-economic Convergence                                           | The EAC Partner States should:  
  - Globally synchronize their business cycles;  
  - Minimize the adverse effects of external asymmetric shocks (resulting, for instance, from fluctuations in world prices of raw materials);  
  - Develop similar experiences in shock management;  
  - Achieve comparable levels of inflation rates and growth rates;  
  - Gradually bridge the gap between income levels;  
  - Align their interest rates; and  
  - Achieve a high degree of stability of bilateral nominal exchange rates.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
| 2. Fiscal Discipline                                                   | Fiscal policy is the most important component of economic policy which, it may be assumed, would remain at least initially within the jurisdiction of EAC Partner States in the monetary union. However, sustainable monetary union will require permanent, commonly agreed standards for sound fiscal policies. Consequently, the Partner States’ freedom of action should be constrained by common fiscal rules designed to avoid a “free rider” problem, which might give rise to potentially damaging spillover effects on the monetary union. The enforcement of such fiscal rules would require sustained political will.                                                                                       |
| Enhanced cooperation in monetary and exchange rate matters            | The implementation of or continued cooperation in monetary and exchange rate matters should be effective in the period prior to the monetary union (as recognised in the EAC Treaty), the “Development Strategy 2006-2010”, and the Common Market Protocol.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| 1. Economic Integration                                                | The implementation of the Common Market Protocol should also lay the foundations of a more sustained integration, and foster wider integration (in the form of trade in goods and services, financial flows, and cross-border movement of persons and businesses), necessary for the deepening of the monetary union.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| 2. Capacity Building                                                  | The essential preparations (including the establishment of the legal and institutional framework) as well as the implementation of the EAMU may not be completed and operational, without the sustainable and on-going development of human resources and the availability of material and financial resources.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| Strategy for the transition to East African Monetary Union             | The transition to the EAMU requires the design and effective implementation of a global, realistic and comprehensive strategy.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| 5. Project for the Development and Integration of EAC Payments and Settlement Systems, Supported by the ADB | The ADB supports the project for the development of national payments and settlement systems and the future establishment of a single and integrated regional payments system within the EAC. The aim of this project is to contribute to developing financial infrastructure, fostering the security of financial flows, reducing the cost of financial services, improving financial inclusion, facilitating cross-border financial flows and remittances, boosting the stability of the regional financial system, regional financial integration and supporting the process to establish the monetary union.  
Furthermore, the project aims at supporting the introduction of a real common market, whose protocol was adopted by the Heads of State of five EAC member countries during the 2009 summit, by facilitating cross-border economic and financial activities through the setting-up of a developed and secure fund transfer platform.  
The launch of the East African Cross Border Payment System, an integrated payment and settlement system within the EAC, is a concrete operational step that will help toward monetary, financial, and economic integration. The system is so far operational in three EAC members—Kenya, Tanzania, and Uganda; two additional members—Rwanda and Burundi—are working on the preparation of their systems (Mira 2013). |
ANNEX 4. EAC Macroeconomic Performance Relative to Convergence Criteria

Annex 4.1. Macroeconomic Convergence Criteria in the EAC

<table>
<thead>
<tr>
<th>STRATEGIES</th>
<th>MEASURES</th>
<th>TIMEFRAMES</th>
<th>INDICATORS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary Criteria</td>
<td>Budget Deficit to GDP ratio Excluding grants Including grants Inflation External reserves</td>
<td>&lt;6% &lt; 3% &lt; 5% &gt; 4 months import cover</td>
<td>&lt;5% &lt; 2% &lt; 5% &gt; 6 months import cover</td>
</tr>
<tr>
<td>Secondary Criteria</td>
<td>Real exchange rate Interest rates Real GDP growth Debt Savings to GDP Ratio Current account (excluding grants) Banking Supervision and Regulations Payment and Settlement systems</td>
<td>Stable Market based &gt; 7% Reduced to sustainable levels &gt; 20% Consistent with debt sustainability Implementation of the 25 Core Principles Adhere to Core Principals for Systematically Important Systems</td>
<td>Market based &gt; 7% Sustainable levels &gt; 20% Consistent with debt sustainability Introduction of single currency</td>
</tr>
</tbody>
</table>

Source: Adapted from Mafusire and Brixiova, 2012. (*) The date of 2024 replaced the previous scheduled date of 2015.

Annex 4.2. EAC Macroeconomic Performance Relative to Convergence Criteria, 2012 (*)

<table>
<thead>
<tr>
<th></th>
<th>GDP Growth (Target: &gt; 7%)</th>
<th>Inflation (Target: &lt; 5%)</th>
<th>Fiscal Balance (including grants) (Target: &lt;2%)</th>
<th>Fiscal Balance (including grants) (Target: &lt;2%)</th>
<th>External reserves (months import cover) (Target: &gt; 6 months import cover)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Burundi</td>
<td>4.2</td>
<td>18.2</td>
<td>-3.4</td>
<td>-7.9</td>
<td>0.8</td>
</tr>
<tr>
<td>Kenya</td>
<td>4.6</td>
<td>9.4</td>
<td>-3.4</td>
<td>-4.2</td>
<td>1.0</td>
</tr>
<tr>
<td>Rwanda</td>
<td>8.0</td>
<td>3.9</td>
<td>-1.2</td>
<td>-12.4</td>
<td>1.3</td>
</tr>
<tr>
<td>Tanzania</td>
<td>6.9</td>
<td>16.0</td>
<td>-9.1</td>
<td>-5.0</td>
<td>0.4</td>
</tr>
<tr>
<td>Uganda</td>
<td>2.8</td>
<td>14.0</td>
<td>-3.0</td>
<td>-5.3</td>
<td>1.2</td>
</tr>
</tbody>
</table>

Note: (*) 2011 for the fiscal indicators for Rwanda. Source: Author from EAC 2013, EAC facts and Figures 2013, July, Arusha.
Annex 4.3 (Figure). EAC Macroeconomic Performance Relative to Convergence Criteria, 2012 (*)
# Annex 5. WAMZ Macroeconomic Performance Relative to Convergence Criteria

## Annex 5.1. Macroeconomic Convergence Criteria in the WAMZ

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Indicator</th>
<th>Targets</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Primary Criteria</strong></td>
<td>Fiscal balance/GDP</td>
<td>≥ -5 %</td>
</tr>
<tr>
<td></td>
<td>Excluding grants</td>
<td>≥ -3 %</td>
</tr>
<tr>
<td></td>
<td>Including grants</td>
<td>≤ 10 %</td>
</tr>
<tr>
<td></td>
<td>Inflation Rate (end-period)</td>
<td>≥ 3 months</td>
</tr>
<tr>
<td></td>
<td>Gross Reserves in Months of Imports</td>
<td>≤ 10 %</td>
</tr>
<tr>
<td></td>
<td>Central Bank financing of budget deficit in relation to previous year's tax revenue</td>
<td></td>
</tr>
<tr>
<td><strong>Secondary Criteria</strong></td>
<td>Change in Domestic Arrears</td>
<td>≤ 0</td>
</tr>
<tr>
<td></td>
<td>Ratio of Tax Revenue to GDP</td>
<td>≥ 20 %</td>
</tr>
<tr>
<td></td>
<td>Wage bill/Tax Revenue</td>
<td>≤ 35 %</td>
</tr>
<tr>
<td></td>
<td>Domestically Financed Investment/Domestic revenue</td>
<td>&gt; 20</td>
</tr>
<tr>
<td></td>
<td>Nominal Exchange Rate</td>
<td>Within +/- 15% of WAMZ-ERM central rate</td>
</tr>
<tr>
<td></td>
<td>Real Interest Rate</td>
<td>&gt; 0</td>
</tr>
</tbody>
</table>


<table>
<thead>
<tr>
<th></th>
<th>GDP Growth</th>
<th>Inflation</th>
<th>Fiscal Balance (including grants)</th>
<th>Central Bank Financing of Fiscal Deficit</th>
<th>External reserves (months import cover)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(percentage)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gambia</td>
<td>3.9</td>
<td>4.9</td>
<td>13.5</td>
<td>4.0</td>
<td>4.8</td>
</tr>
<tr>
<td>Ghana</td>
<td>7.9</td>
<td>8.8</td>
<td>7.4</td>
<td>9.4</td>
<td>3.4</td>
</tr>
<tr>
<td>Guinea</td>
<td>3.9</td>
<td>12.8</td>
<td>5.5</td>
<td>6.8</td>
<td>3.1</td>
</tr>
<tr>
<td>Liberia</td>
<td>8.3</td>
<td>7.7</td>
<td>-1.8</td>
<td>0.0</td>
<td>2.3</td>
</tr>
<tr>
<td>Nigeria</td>
<td>6.7</td>
<td>12.0</td>
<td>2.5</td>
<td>0.0</td>
<td>9.5</td>
</tr>
<tr>
<td>Sierra Leone</td>
<td>17.9</td>
<td>11.4</td>
<td>8.1</td>
<td>0.0</td>
<td>3.1</td>
</tr>
</tbody>
</table>

Annex 5.3 (Figure). Macroeconomic Convergence Criteria in the WAMZ, 2012
VIII. REFERENCES


———, 2009c, “Zimbabwe: 2009 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Zimbabwe,” IMF Country Report No. 09/139 (Washington: International Monetary Fund).


