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Establishment of an African Monetary Fund

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ESTABLISHMENT OF AN AFRICAN MONETARY FUND

EXCHANGE RATE AND EXCHANGE CONTROL POLICIES AND PRACTICES IN AFRICAN COUNTRIES

I. INTRODUCTION

1. The second meeting of the Intergovernmental Group of Experts on the establishment of an African Monetary Fund examined the feasibility study entitled "The Establishment of an African Monetary Fund: Structure and Mechanism", and largely adopted the major recommendations. The meeting, however, felt that it was necessary to include a section on exchange rate and exchange control policies and practices in Africa as was called for in the terms of reference. It therefore directed that a paper on this subject should be prepared and submitted to the meeting of Ministers of Finance and Governors of Central Banks for their consideration.

2. This paper is prepared in response to that request and gives a summary of the existing exchange rate policies and exchange control practices in African countries, 1/ with a view to indicating that the establishment of an African Monetary Fund would provide a framework within which African countries could work to harmonize their exchange rates and exchange control legislations and practices.

II. EXCHANGE RATE ARRANGEMENTS IN AFRICA

3. The African region is characterized by a multiplicity of non-traded currencies whose values are in most cases fixed in terms of either one of the major world currencies, the Special Drawing Right (SDR) or a currency basket of currencies other than the SDR. Without exception, the exchange rates of African currencies are expressed in different units and in various other currencies. The monetary authorities - mainly the ministries of Finance and central banks, are responsible for determining the exchange rates of their currencies which in most cases take the form of "pegging" to one currency or a basket of major internationally traded currencies.

4. The countries and their currency pegging are shown in Table 1 below. As of 29 March 1985, six African currencies were pegged to the United States dollars; eight to the Special Drawing Right (SDR) of the International Monetary Fund; fourteen to the French franc; twelve to currency basket other than the SDR; one to the pound sterling; two to the South African Rand; four currencies had their exchange rates determined by market rates in currency units per US dollar and adjusted according to a set of indicators; and two countries maintained multiple currency practices and/or dual exchange markets.

1/ African Centre for Monetary Studies "Towards the Harmonization of Exchange Control Regulations and Practices in the North, West, Central, East and Southern African Subregions" (four volumes), unpublished, Dakar, 1980-1982.

Table 1

Exchange Arrangements for 49 African countries, 29 March 1985

		Exchange rate
1.	Pegged to US dollar	
	Djibouti (franc)	177.731
	Egypt (pound)	0.700
	Ethiopia (birr)	2.070
	Liberia (dollar)	1.000
	Libya (dinar)	0.296
	Sudan (pound)	2.500
2.	Pegged to SDR	
	Burundi (franc)	122.7
	Guinea (Syli)	24.685
	Guinea-Bissau (peso)	84.054
	Kenya (shilling)	15.897
	Rwanda (franc)	102.710
	Sao Tome et Principe (dobra)	45.250
	Seychelles (rupee)	7.235
	Sierra Leone (Leone)	6.270
3.	Pegged to the French Franc	
	Benin (franc)	50.000
	Burkina Faso (franc)	50.000
	Cameroon "	50.000
	Central African Republic(franc)	50.000
	Chad (franc)	50.000
	Comoros (franc)	50.000
	Congo (franc)	50.000
	Equatorial Guinea (franc)	50.000
	Gabon (franc)	50.000
	Ivory Coast (franc)	50.000
	Mali (franc)	50.000
	Niger (franc)	50.000
	Senegal (franc)	50.000
	Togo (franc)	50.000

4.	Pegged to currency basket other than SDR	Exchange Rate
	Algeria (dinar)	5.104
	Botswana (pula)	1.711
	Cape Verde (escudo)	93.950
	Madagascar (franc)	677.770
	Malawi (Kwacha)	1.617
	Mauritania (Ouguiya)	na.
	Mauritius (rupee)	15.970
	Mozambique (metical)	43.852
	Tanzania (shilling)	17.898
	Tunisia (dinar)	0.856
	Zambia (kwacha)	na.
	Zimbabwe (dollar)	1.537
5.	Pegged to the Pound Sterling	
	Gambia (dalasi)	5.000
6.	Pegged to the South African Rand	
	Lesotho (maloti)	1.000
	Swaziland (lilangeni)	1.000
7.	Floating Independently or adjusted According to a set of Indicators	
	Ghana (cedi)	50.000
	Morocco (dirham)	9.702
	Somalia (shilling)	37.000
	Zaire (Zaire)	47.200
3.	Maintaining Multiple Currency Practices or Dual Exchange Market	
	Nigeria (Naira)	na.
	Uganda (shilling)	na.

Source: IMF Survey, Washington DC. 29 March 1985

Note: Angola's currency (kwanza) is not included.

5. As already pointed out earlier, the exchange rates of most African currencies are fixed by their monetary authorities. Over the past several years countries tended to stick to fixed rates for considerably long periods instead of adjusting the exchange rates to reflect the underlying economic conditions particularly the domestic balance of payments and the foreign reserve positions. 2/

6. Faced with problems of balance of payments and shortages of foreign exchange, African countries have resorted to a host of exchange control policies and practices in order to ensure an adequate supply of foreign exchange to finance essential imports. These problems are aggravated by the current system of generalized floating of the internationally traded currencies to which African currencies are pegged. Administered exchange rates have become a source of problems because the key currencies to which African currencies are pegged exhibit strong degrees of volatility so that currencies pegged to an overvalued currency also become overvalued relative to other African currencies.

7. Within the framework of the proposed African Monetary Fund, it is envisaged that one of its objectives will be the promotion of stability of African currencies through appropriate stabilization policies including exchange rate systems at the national, subregional and regional levels. 3/ Fluctuating exchange rates have profound effects on a wide variety of development facets of the African economies, including trade balance and price levels, pricing systems, tax revenues, international capital movements external indebtedness and foreign exchange reserves. Therefore the African Monetary Fund, as a regional financial institution, would constitute a forum within which some monetary and financial order would be established for the African region.

III. EXCHANGE CONTROL POLICIES AND PRACTICES

8. Most African countries have adopted measures to restrict imports and current payments in response to severe balance-of-payments problems. One of the measures resorted to in restricting imports and current payments has been the instituting of exchange control measures. In most of these countries, exchange control policy is determined by the Ministry of Finance while the day-to-day administration of exchange control is carried out by the Central Bank. 4/

2/ African Centre for Monetary Studies, Currency Arrangements in the African Monetary Fund: A Proposal, Dakar, April 1984.

3/ ECA, The Establishment of an African Monetary Fund: Structure and Mechanism, Addis Ababa, 22 January 1985.

4/ See International Monetary Fund, Annual Report on Exchange Arrangements and Exchange Restrictions, annual report, 1983.

9. The application of exchange control policies and practices in Africa varies from country to country according to the balance of payments positions, the economic management policies and the special financial arrangements with other African countries. For example, when countries have unfavourable balance-of-payments positions they tend to apply more restrictive exchange control measures than otherwise. In this respect, the main rationale for exchange control is the need to ensure an adequate supply of foreign exchange to finance essential imports of goods and services. In such a situation, the authorities tend to adopt stringent and discriminatory exchange control policies whereby only imports of goods and services which are deemed to be of absolute necessity for development in the countries are allocated foreign exchange.

10. In cases where countries have balance-of-payments surpluses as was the case in The Gambia, Botswana and Malawi in the late 1970s, exchange control measures were less stringent. Similarly, in principle, there are liberal or no exchange controls applied among African countries belongting to special financial and monetary arrangements such as the West African Monetary Union or members of the Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO), Banque des Etats de l'Afrique Centrale (BEAC), the Rand Monetary Area and Liberia which uses the United States dollar as its currency.

11. Furthermore some African countries have special financial arrangements such as free payments zones among themselves. Two such cases existing in Africa are (a) franc zone countries of the West African Monetary Union and those of the Central Bank of Central African States both of which use the CFA franc which is tied to the French franc and (b) the free payments zone is in Southern Africa where Swaziland, Botswana, Lesotho and South Africa have lifted all restrictions on payments among themselves within the framework of the Rand Monetary Area. This special relationship guarantees freedom of payments for current and capital transactions between member countries. However, both the franc zone countries and the Rand Monetary Area countries apply an array of exchange controls when it comes to payments involving countries outside their respective payments areas. The existence of subregional clearing houses in Western, Central, Eastern and Southern Africa also adds another element of special financial arrangements in Africa which allows transaction settlements among member countries to be made in local currencies, but balances at the end of each settlement period are always settled in convertible currencies.

IV. EXCHANGE CONTROLS ON VISIBLE AND INVISIBLE TRADE

12. Outside the special arrangements mentioned above, all transaction settlements are usually carried out in convertible currencies. Restrictions put on external payments vary from country to country but they invariably affect visible and invisible trade as well as capital transactions. Exchange controls on imports take a variety of forms such as general restrictions, license requirements and designated importers, import payments restrictions, and taxes. Some African countries sometimes prohibit certain imports on social, health or security grounds or even political grounds as is the case of imports from South Africa which are banned by many African countries. Usually most African countries

operate a system of import licensing whose degree of restriction varies according to the countries involved. Some countries issue free general licences while others require the issuance of a specific licence for all imports. A certain number of countries requires an exchange license in addition or in place of the specific license for all imports.

13. In the case of other restrictions, the importation of essential commodities is entrusted, in most countries, to one or more state agencies. Export related exchange controls are usually the same as those for imports. They are, however, normally more liberal in the sense that their main aim is to consolidate export proceeds in foreign exchange, facilitate tax collection, prevent domestic shortages, ensure the quality of exports and safeguard the monopoly of designated exporters. Many African countries grant export monopolies to state agencies for the major cash crops or mineral exports.

14. All African countries enforce exchange controls on invisibles such as freight, insurance, travel and remittances. Freight payments are usually treated on the same basis as goods to which they relate. Approval of foreign exchange for freight payments is normally granted at the same time as that for the imported goods. Some countries require insurance to be taken locally while others approve foreign exchange for insurance purposes. As far as travel is concerned, tickets are normally bought in local currencies. However, foreign exchange for travellers is strictly controlled in many countries and the amount authorized depends on the purpose of the trip abroad. Some countries enforce specified foreign exchange limits for every type of travel while others consider foreign exchange applications on an ad hoc basis. Usually business travellers are allowed more foreign exchange than tourists. There are cases where foreign exchange allowances for tourism purposes have been suspended altogether. 5/ Foreign travellers are normally allowed to take out any amount of foreign exchange declared upon entry and not spent locally.

15. Remittances which include company profits, expatriate income, and foreign exchange transfers for education or family support are subject to various exchange control regulations. The degree of liberality of these regulations is very much linked to the balance of payments of the countries concerned. In a few countries such as Rwanda and Swaziland, net dividends and profits may be transferred in full by foreign-owned companies. Other countries allow transfers much less than the full amount of the annual profits and dividends. Expatriate workers are usually allowed to transfer part of their incomes abroad and upon their departure they are normally allowed to take out all their savings. Transfers for family support are alllowed in most cases but the amounts permitted depend on the merits of each case. Remittances for education purposes are normally allowed but are usually restricted to defined ceilings.

5/ For instance in Tanzania allocation of foreign exchange for holiday purposes was suspended.

16. With regard to capital transfers, exchange controls seem to be particularly restrictive on outgoing capital and very liberal on incoming capital. The idea being to retain the available capital for domestic investment, attract productive foreign capital and keep track of a country's external debt position. Although foreign investments benefits from liberal exchange controls, they are still subject to approval in order to ensure their profitability and approval is also required for transfers of profits and dividends, tax holidays, compensation in case of nationalisation and later repatriation of capital invested.

V. PROPOSALS FOR EXCHANGE CONTROL LIBERALIZATION AND HARMONIZATION

17. In view of the fact that exchange controls in Africa are many and varied, their liberalization and harmonization within an integrated framework could bring about benefits to the individual countries in terms of balance-of-payments improvements, increase in economic growth and employment and reduction in the rate of inflation. However, and in order to achieve these benefits they should be accompanied by other economic measures designed to minimize their negative effects.

18. The existence of economic integration arrangements at the various subregional levels (West, Central, Eastern and Southern Africa), which include measures designed to facilitate the expansion of intra-African trade, is a major step towards exchange control liberalization and harmonization. It would therefore be advisable to build new programmes of exchange control liberalization and harmonization on the basis of existing subregional economic integration groupings. Measures should be taken to harmonize exchange control policies and practices in the subregions so as to facilitate the relaxation of exchange control restrictions in Africa and eventually make it possible to work towards some form of limited currency convertibility. This harmonization should be the first part of a programme for the gradual liberalization of exchange regulations. Within the subregional groupings countries which have relatively less liberal exchange control regulations should, in addition to maintaining their current legislation, reduce or abolish other restrictions vis-a-vis members of the subregion first and then other African countries.

19. It would be useful to ensure that the liberalization process is spread over a sufficiently long period of time in order to minimize its negative effects on the balance of payments of some countries. A first stage in the liberalization programme could be the liberalization of exchange controls related to current transactions. During the long period required to achieve complete liberalization of exchange controls, the respective subregional clearing houses would be expected to play an important role in transaction settlements among their member countries. It would also be useful to establish a link between the various subregional clearing houses in order to create channels for payments on a regional basis, preferably through a special window in the African Monetary Fund when established.

20. Since adjustments and financing go together, the African Monetary Fund should assist member countries to obtain the financing necessary for their adjustment programmes and make sure that these funds do not exacerbate the already heavy external debt burden. Appropriate adjustments over a reasonable period of time should enable the authorities to restructure domestic demand for and supply of money efficiently. Within the framework of its activities, the African Monetary Fund should also consider the general co-ordination of fiscal policies in member countries in order to prevent these policies from hampering the expansion of intra-African trade.