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Varied impact on Africa expected from new European currency

For better or for worse: the euro and the CFA franc

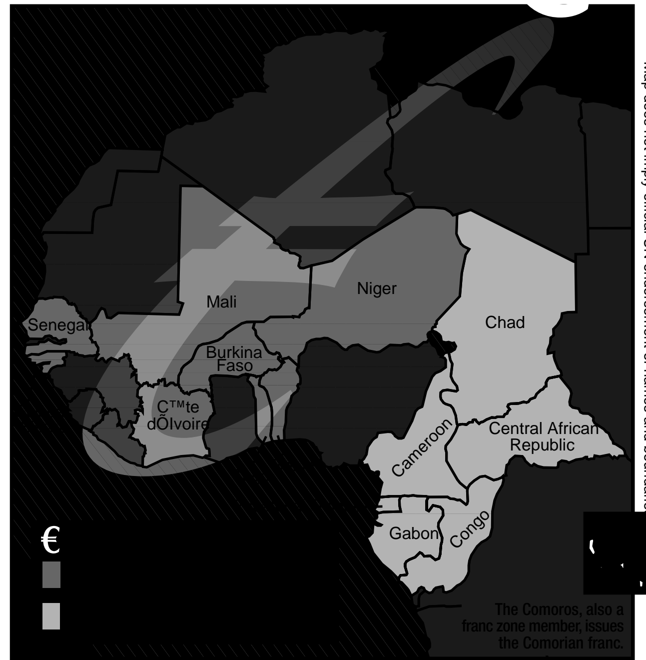
By ***Jacqueline Irving***

Opinions are divided over whether the introduction of the single European currency (euro) on 1 January 1999 will prove to be a boon or a bane for African economies.

Two certainties for the foreseeable future are that the CFA franc used by 14 African countries will be pegged to the euro instead of the French franc — to which it has been tied since 1948 — and that 65 per cent of these countries' external reserves will continue to be kept in an account held by the French Treasury.

Many economists and financial analysts agree that the euro — which will be the only legal tender in 11 countries known as "euroland" after 30 June 2002 (see box, page 25) — will alter trade and financial flows between Europe and Africa. The CFA countries — together with Central Europe and the Southern Mediterranean — comprise the three groups of countries outside euroland that will be "affected most" by the euro's introduction, according to a December 1998 World Bank report. But the direction of change is not yet clear, (see box, below). Some analysts point out that actual outcomes for Africa could vary considerably by region and over time.

Trade links between euroland and African countries, particularly in the CFA zone, are already tight. Trade with euroland accounts for 40-50 per cent of total African trade, according to IMF figures. The figures are generally at the higher end of this range for CFA countries (although CFA trade with the European Union countries has declined quite steeply in recent years — see graph, page 28). If the euro regime leads to an economic upswing in euroland, it could boost that region's output and demand for imports. In turn, this could benefit the economies of euroland's African trading partners. For companies in CFA countries trading with companies in the European countries sharing the euro with France, the shift in the currency peg from the French franc to the euro would also mean lower commercial and currency transaction costs.



The introduction of the euro is expected to tighten economic links between euroland on the one hand, and the CFA franc zone countries and the Comoros, on the other.

Central bankers of the mainly francophone West African Economic and Monetary Union (WAEMU) are optimistic. The CFA franc-euro link "will give a new impulse to trade and financial flows" between WAEMU and European countries, offering "new opportunities to the economies of WAEMU and new markets to European countries," said an official of WAEMU's Central Bank of West African States (BCEAO). The link should also offer to WAEMU's eight members the distinct advantages of "more commercial outlets, [the ability to] attract more European investors and access to the European financial market." But WAEMU officials also note that among the challenges posed by the euro link is the continuing obligation that WAEMU members "implement sound and convergent economic and financial policies."

Optimism not universal

Some economists are more dubious about the extent to which the euro's introduction will have positive trade effects for any countries, including those in the CFA zone. "I don't believe that there is going to be much benefit

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Impact of the euro on Africa

Possible gains for Africa from the euro include:	But the euro would be bad for African economies if it causes:
• Increased export sales	• A loss of export markets
• Faster growth	• Slower growth
• Transaction cost savings	• Macroeconomic instability
• Improved macroeconomic stability	• Diversion of international investment from Africa
• More inbound foreign investment	• Less favourable foreign borrowing conditions
• Cheaper foreign borrowing rates	• Setbacks in local capital market development
• A spur to regional integration	• Impediments to regional integration

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in terms of trade to any partner of the euro zone, including the CFA," says Mr. Yilmaz Akyuz, Chief, Macroeconomic and Development Policies of the UN Conference on Trade and Development (UNCTAD). He acknowledges that reduced transaction costs and the elimination of exchange rate uncertainty within Europe following the euro's introduction could boost euroland's income levels and demand for imports. But citing recent economic forecasts, Mr. Akyuz points out that, in the period to 2010, total income for all euroland could rise just 3 per cent and increased trade with euroland would lead to a rise in developing countries' GDP of just 0.3 per cent over the same period.

Moreover, Mr. Akyuz speculates that euroland's growth may not even reach 3 per cent as a result of costs associated with member countries' obligation to meet tight fiscal and monetary policy targets. And even if the overall effects on African trade are positive, the euro regime could have a negative impact on certain businesses, sectors and/or economies in Europe. In turn, this could slow export growth in certain sectors of African economies.

Freer, greater financial flows

In the positive scenario for financial flows, exchange rate stability promoted by the CFA-euro link could lead to benefits such as greater inflows of direct investment from euroland countries, says a recent International Monetary Fund (IMF) report[1]. Other investment flows from Europe into the CFA zone could increase if European institutional investors — such as pension fund and insurance companies — decide to diversify their portfolios by moving some of their funds to CFA countries, another recent IMF report notes[2]. And these benefits could be enhanced and reinforced by the improved access of CFA countries to euroland's financial markets. Borrowers in CFA countries would find that they could raise funds more easily and at cheaper rates in the deeper, more competitive financial markets expected to emerge in euroland.

Addressing the European Parliament in late October, Mr. Tommaso Padoa-Schioppa, member of the Executive Board of the European Central Bank, drew a promising picture. "Capital movements between the CFA franc zone and the entire euro area, and not only France, are expected to be liberalized after the pegging of the CFA franc to the euro," Mr. Padoa-Schioppa remarked. "This, together with the ongoing trade liberalization within the CFA franc zone, should help the zone to reap the benefits from globalization. However, this will take time and will also depend on the pursuit of sound macroeconomic policies and the strengthening of domestic financial systems."

BCEAO officials recently said that they expect the CFA-euro peg to attract more European investors to CFA financial markets, who will be notably more interested in the operations of the regional stock market in Abidjan, Côte d'Ivoire.

But there is a possible downside associated with the freer, greater financial flows expected between the two regions. For example, freer access to euroland financial markets could mean that many CFA borrowers would leave CFA financial markets altogether, hindering their development. In a different scenario, if the euro boosts productivity and growth in euroland and increases the relative attractiveness of euro assets, borrowing costs for CFA countries could actually increase.

And in the event of a crisis of confidence — if the euro gains so much strength that a devaluation of the CFA franc becomes necessary — capital flight from the CFA to euroland could be destabilizing. This risk is not new, however: the possibility of capital flight following a speculative attack also existed under the French franc-CFA franc link.

Strong or volatile euro poses risks

Exploring possible negative aspects of the CFA-euro link, some analysts warn that either a strong or a volatile euro could harm CFA economies. Among the main risks associated with the euro peg "could be the potential appreciation of the real effective exchange rate of the CFA franc zone countries" which could undermine the competitiveness of CFA countries' exports, says Mr. Cornelius Mwalwanda, Senior Economic Affairs Officer with the UN Economic Commission for Africa. Heightened volatility of the euro in terms of other major currencies, "both in the transition and early years as well as over the long run" would also hurt CFA countries' trade performance, he adds.

Such risks, said Mr. Mwalwanda, were among the many issues raised at a November 1998 symposium on the future of the CFA franc zone, held by the Council for the Development of Social Science Research in Africa (Codesria) in Dakar, Senegal.

For example, one symposium participant, Mr. Karamoko Kane of the Cheikh Anta Diop University in Dakar, Senegal, was willing to bet that "the euro will be in future one of the strongest currencies of the international monetary system." In this scenario, the CFA franc would "follow the euro in its appreciation against the US dollar or yen and also, in the same movement, against the currencies of developing countries, notably those of Asia and Latin America which are fixed to the dollar,

What is the euro?

The euro — the single European currency — will replace the national currencies of 11 member countries* of the European Union (euroland) during a three-and-a-half year period that began on 1 January 1999. On this date, the exchange rates of the euroland countries were "irrevocably fixed" to the euro. The 11 national currencies and the euro will coexist until mid-2002, the date by which the national currencies must be completely withdrawn from circulation.

While marking a milestone in the European Union's economic integration process, the launch of the euro has significance beyond Europe. Some economists and financial experts believe the euro could become a major international currency to rival the US dollar.

The euro does not yet circulate in the form of notes and coins, but many banks, businesses and other institutions — within and outside euroland — already have begun denominating transactions in euro.

** Austrian schilling, Belgian franc, Finnish markka, French franc, German deutschemark, Irish pound, Italian lira, Luxembourg franc, Dutch guilder, Portuguese escudo, Spanish peseta.*

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[1] *Michael T. Hadjimichael and Michel Galy,* The CFA Franc Zone and the EMU, *IMF Working Paper, No. WP/97/156 (Washington, DC, November 1997).*

[2] *John Green and Phillip L. Swagel, "The Euro Area and the World Economy,"* Finance & Development, *Volume 35, No. 4 (December 1998).*

yen and even to the [IMF's] special drawing right (SDR)." Mr. Kane concluded: "A developing region with an overvalued currency would be excluded from global competition."

In other words, a strong euro could hit CFA economies hard by making their exports more expensive and by making import prices cheaper than those of competing domestically-produced goods. This could be especially devastating in the light of stiffer competition already posed by exports from countries with devalued currencies in Asia and in other emerging market countries.

And because the euro is forecast to be a stronger currency than the French franc, some believe this could put pressure on the CFA franc to devalue against the euro. "If the euro is strong, I expect that the CFA countries will come under pressure in terms of loss of competitiveness and this could effectively necessitate more frequent [exchange rate] adjustments than we've seen under the system of pegging to the French franc," Mr. Akyuz of UNCTAD told *Africa Recovery.*

In fact, the CFA franc has only undergone one devaluation in its 50-year history — in January 1994, it went from CFA 50 to CFA 100 = FF1 — a measure virtually imposed by France, the IMF and the World Bank to jump start franc zone economies after nearly a decade of recession. The memories of the 1994 devaluation and its immediate effects linger. Described at the time as "brutal and painful" by Benin's then-President Nicéphore Soglo, the devaluation was followed by a series of harsh economic policy changes. But many economists now give credit to the 1994 devaluation, together with the associated policy changes, for the region's stronger economic performance of recent years.

Devaluation fears recede — for now

In the months preceding the euro's launch, officials within the CFA franc zone and France sought to dispel periodic rumours that the shift in the CFA franc's peg to the euro would lead to a devaluation of the CFA franc. On numerous occasions in the last year, French government officials publicly reaffirmed the French treasury's commitment to defending the fixed parity following the euro's introduction (see box, page 27).

BCEAO governor Charles Konan Banny also has been giving repeated and emphatic reassurances that the euro's launch would not imply a CFA franc devaluation. In a late November 1998 speech, Mr. Banny stressed that the CFA franc "is currently supported by a sound and efficient macroeconomic framework which will permit it to maintain its value before and after its pegging to the euro." Citing single digit inflation in WAEMU economies since 1995, along with robust economic growth rates, reduced public deficits, improvements in the trade account and increased foreign reserves, Mr. Banny declared that the "major difficulties affecting [WAEMU] have been surmounted and the future is rather promising." All market economies are open to speculative attacks, Mr. Banny said, noting that speculators are often wrong, most notably in the recent past, in anticipating a CFA devaluation following the May 1998 meeting of the European Council to determine European countries eligible to participate in the euro. "That's why we should remain serene, be self-confident and have faith in our common currency," he urged.

CFA franc zone trade with France and the European Union (1990-96; %)

	Exports[1]		Imports[1]	
	France	EU	France	EU
Benin	1.7	30.5	23.5	51.2
Burkina Faso	11.8	26.9	22.5	34.4
Côte d'Ivoire	14.5	54.2	28.9	52.0
Mali	3.9	37.2	18.9	35.0
Niger	68.2	77.6	22.0	39.6
Senegal	24.6	40.9	33.1	57.4
Togo	5.5	26.6	16.5	34.1
WAEMU[2,3]	**16.2**	**49.3**	**25.6**	**46.3**
Cameroon	26.0	73.4	37.6	69.7
Central African Rep.	7.2	53.1	42.4	56.2
Chad	8.5	67.5	43.1	60.2
Congo, Republic of	10.0	48.9	44.7	68.1
Equatorial Guinea	5.7	49.8	13.6	54.5
Gabon	20.7	31.6	44.2	64.7
CEMAC[4]	**19.5**	**50.2**	**40.7**	**66.3**
Total CFA franc zone[3]	**18.0**	**49.8**	**30.6**	**53.4**

1 Shares of France and all European Union countries in the exports and imports of CFA franc countries.

2 West African Economic and Monetary Union

3 With the exception of Guinea-Bissau, which joined WAEMU and the CFA franc zone in 1997

4 Central African Economic and Monetary Community

Source: IMF, Direction of Trade Statistics, *various years*

Fears of a devaluation in the near-term now seem to have been put to rest. The BCEAO cut in the discount rate by 0.5 percentage point at the time of the euro's launch "is not behaviour that smacks of a fear of devaluation," Mr. Jean-Louis Sarbib, World Bank Vice President for Africa, told *Africa Recovery*.

But in the medium- to long-term, others feel less certain that the euro and the CFA franc will be kept at the current parity. Some analysts advise companies dealing in CFA francs to keep contracts short to protect against a possible devaluation.

Mr. Pierre Messmer, a former French prime minister who forecast the 1994 CFA franc devaluation several months in advance, predicts that the currency will come under increasing pressure to devalue in the next few years. Because France is committed to fiscal restraint under European Economic and Monetary Union (EMU) rules, Mr. Messmer argues that France will not be able indefinitely to cover CFA franc zone deficits and defend the CFA franc's value.

Mr. Messmer and others even doubt that the currency peg will last. This reflects uncertainty surrounding both the future of the euro as the system's anchor and the future of the euro itself. "In the long term we don't know whether the euro will survive or not… It's speculative at this stage to say what's going to happen in 10 or 20 years' time to the euro as an anchor currency, as a reserve currency and as a main competitor in the denomination of international trade, assets and liabilities," notes Mr. Akyuz.

Symposium debates CFA franc's future

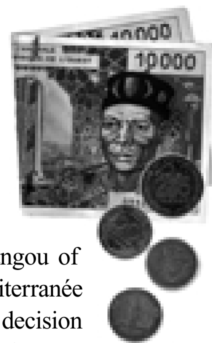
The uncertainty associated with the CFA franc-euro peg has intensified the debate within CFA countries on whether or not a fixed exchange rate system anchored to a non-CFA currency should remain in place. Indeed, this question tended to dominate the presentations and discussions at the symposium on the future of the CFA franc zone held in Dakar in November 1998.

Among those at the symposium discussing ideas for alternative exchange rate systems was Mr. Wilfrid René M'Voula of the Gabonese Ministry of Economy and Finance. The possible scenarios envisaged by Mr. M'Voula and other participants included a fixed exchange rate system managed by the CFA countries themselves, and complete abandonment of fixed exchange rates in favour of 14 freely floating rates. Mr. M'Voula noted that monetary policy sovereignty associated with floating exchange rates "would permit these countries to make the adjustments

needed to render their economies competitive."

While the CFA-euro peg is the "most probable" scenario in the short- to medium-term, Mr. M'Voula believes that "the break up, recomposition or independence of the two African monetary unions [comprising the CFA zone] is possible," in the longer term.

Arguing in favour of flexible exchange rates, Mr. Célestin Monga, a World Bank consultant, urged CFA countries to "abandon both their fixed exchange rate regime and their determination to build an artificial integration, in order for each country to develop, at the national level, a true development policy that maximizes the advantages of an independent monetary policy."



But the "question of the future of the CFA franc should not be posed in terms of issues of sovereignty or dependence but in terms of efficiency," argued Mr. Fidèle Magouangou of the University of the Méditerranée Aix-Marseille II. While the decision to peg the CFA franc to the euro "appears acceptable," he stressed that the CFA economies would not benefit from the peg unless there were "some reforms of the functioning of the CFA franc zone."

He pointed to the need to neutralize the negative effects of a strong euro on the competitiveness of the countries concerned and to "limit the transmission of shocks from the center to the periphery." For Mr. Magouangou, therefore, the principal reform would be "the adoption of a regularly adjustable peg [to the euro] in place of a fixed peg." But in the long term, as CFA monetary institutions get stronger, he envisages "an African 'monetary destiny' that is independent of that of the Europeans."

French neo-colonialism?

One of the hottest issues at the Dakar symposium was the question of whether maintaining a currency link defended by the French Treasury perpetuates French neo-colonialism. While CFA countries have made some gains in the franc zone system, Mr. Tchetche N'Guessan, Director of the Côte d'Ivoire Centre for Economic and Social Research, was among those arguing that France has reaped much greater benefits.

Reviewing the history of economic relations and monetary systems between France and its former African colonies, Mr. N'Guessan said these systems took various forms but were always designed to enhance France's development as a colonial power. Many CFA franc zone

The CFA franc: new peg for a common currency

The CFA franc is the common currency of 14 countries in West and Central Africa, 12 of which are former French colonies. These 14 countries comprise the African Financial Community, which in turn is comprised of two regional economic and monetary groupings. Eight countries — Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo — form the West African Economic and Monetary Union (WAEMU) while six countries — Cameroon, Central African Republic, Chad, Republic of Congo, Equatorial Guinea and Gabon — are linked as members of the Central African Economic and Monetary Community (CEMAC).

Each regional grouping issues its own CFA franc. The common currency of WAEMU is the *franc de la Communauté financière de l'Afrique* (CFA franc), issued by the *Banque centrale des Etats de l'Afrique de l'Ouest* (BCEAO). CEMAC's common currency is the *franc de la Coopération financière africaine* (also known as CFA franc), issued by the *Banque des Etats de l'Afrique centrale* (BEAC). Although the two CFA francs are legal tender only in their respective regions, each region's central bank maintains the same parity of its CFA franc against the French franc and capital can move freely between the two regions.

The CFA franc has been pegged to the French franc since 1948*. Only one devaluation has occurred during the history of the currency peg — from CFA50 to CFA100 = FF1 in January 1994.

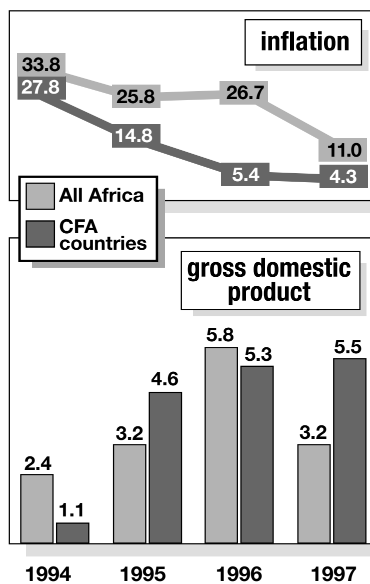
With the introduction of the euro on January 1, 1999, the French franc is fixed against the currencies of the 10 other European countries participating in the euro. Nevertheless, the member countries of the CFA franc zone and France agreed to maintain the currency peg following the euro's introduction through an arrangement with the French Treasury.

The French Treasury has retained sole responsibility for guaranteeing convertibility of CFA francs into euros, without any monetary policy implication for the Bank of France (French central bank) or the European Central Bank. While the two CFA central banks maintain an overdraft facility with the French Treasury, the amount that can be withdrawn is limited by operating rules that have applied since 1973. Each CFA central bank must keep at least 65 per cent of its foreign assets in its operations account with the French Treasury; provide for foreign exchange cover of at least 20 per cent for sight liabilities; and impose a cap on credit extended to each member country equivalent to 20 per cent of that country's public revenue in the preceding year.

The fixed parity between the euro and the CFA franc is based on the official, fixed conversion rate for the French franc and the euro set on January 1, 1999 (FF6.55957 = EURO1). As a result, the value of the CFA franc is now fixed against all 11 euro-zone country currencies. Since the CFA100 = FF1 exchange rate has remained unchanged, the CFA franc-euro exchange rate is simply CFA665.957 = EURO1.

The CFA franc is actually pegged to the euro in de facto terms from January 1999. The peg will become official in 2002 — when France and the other euro-zone countries must completely withdraw their national currencies from circulation.

Macroeconomic trends of the CFA franc zone
(annual percentage change)



Source: UN Africa Recovery from IMF, World Economic Outlook *(May 1996, October 1998)*

**The Comoros also pegs its currency, the Comorian franc, to the French franc and, since January 1999, to the euro. The Comorian franc was also devalued against the French franc in January 1994, by 33 per cent.*

mechanisms were simply the "monetary dimension of the colonial agreement," he said, noting that "exchange rate policies played a major role in [France's] domination of its colonies." And today, the fixed exchange rate regime "remains an essential factor in determining the economic performance of the CFA franc zone," Mr. N'Guessan argued.

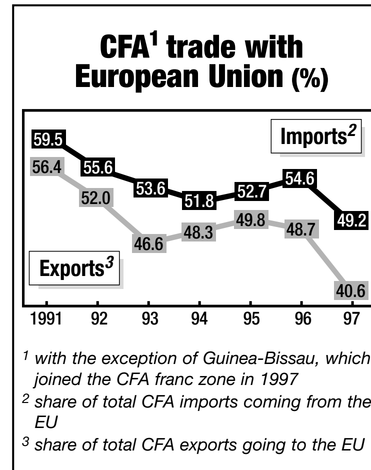
When the terms of trade were favourable, Mr. N'Guessan continued, CFA countries had good track records in containing inflation and achieving superior growth relative to non-CFA countries. But he blamed the "financial repression" associated with the exchange rate regime for poor performance in terms of savings and debt levels.

The balance sheet according to Mr. Jean-Louis Sarbib of the World Bank, is very different. "It's really quite extraordinary that these African countries in the CFA zone have had for years what euroland has only had for several weeks. If you look at the performance over a period of time, I think the advantages of the current fixed exchange rate arrangement outweigh the disadvantages… the only real shock, so to speak, was the 1994 devaluation from which I think countries have benefited," he told *Africa Recovery.* This good performance is largely due to the peg to a stable currency, Mr. Sarbib continued, adding: "I don't know of many other places in Africa where management of the currency has been as good as it has been in the franc zone."

Some analysts think that the shift in the currency peg from French franc to euro might weaken French influence in the CFA region. "To the extent that the French influence over the [euro-zone] exchange rates is less than the French influence over the French franc… the political link between France and the CFA countries may be expected to weaken a bit," says Mr. Akyuz. "But on the other hand, France becomes the main country [within the euro zone] that takes care of the interests of the CFA countries."

The shift to the CFA franc-euro peg will have "no political implications [for the euro member countries] as such," Mr. Georges Pineau, Deputy Director-General for International and European Relations at the European Central Bank (ECB), told *Africa Recovery.* "Clearly, there is no implication whatsoever for the other [euroland] countries and certainly not for the ECB," says Mr. Pineau after pointing out that the French Treasury has retained sole responsibility for guaranteeing convertibility of CFA francs into euros. This means the French Treasury can defend the exchange rate by making credits to the CFA central banks to cover deficits on their operating accounts (see box, page 27).

Mr. Pineau echoes the official French position on this issue: the currency peg is an internal French budgetary matter, not a monetary issue that would involve France's euro partners. And French officials point to data showing that the CFA central banks' operating account deficits have constituted only a tiny share of the total French budget deficit.



Source: UN Africa Recovery from IMF, Direction of Trade Statistics Yearbook, 1998

But some are not so sanguine about the continued ability of France alone to cover CFA franc zone deficits. Mr. Messmer, one of the most vocal critics of the CFA franc mechanism, argues that French fiscal commitments under European economic and monetary union will make it impossible for the mechanism to remain intact.

Spurring regional integration

One potential benefit of the CFA-euro peg is if the maintenance and strengthening of a common currency acts as a spur to broader economic integration in West and Central Africa. "Because maintenance of the common currency requires harmonization of policies — including fiscal and trade policies — it's a strong incentive to do the right thing to build a bigger base for regional integration," Mr. Sarbib explained.

In West Africa, for example, CFA countries form half of the 16-nation Economic Community of West African States (ECOWAS). Assuming the CFA countries continue to enjoy low inflation, strong growth and improved economic stability through the macroeconomic policies associated with the euro peg, the "ECOWAS region as a whole will benefit from the spillover effects," Mr. R.D. Asante, who heads the Money and Payments Division of the ECOWAS Secretariat, told *Africa Recovery*. Mr. Asante refers to the euro as an incentive to non-CFA, ECOWAS countries to work towards greater harmonization of monetary and financial policies with the CFA. "And now there is talk of having a dual monetary zone in Africa because of what is happening with the euro," he adds.

Other economists and public officials predict renewed impetus for regional integration throughout Africa. The euro is likely to "reinvigorate the current slow pace of economic integration in Africa, particularly in non-CFA Africa," Mr. Maurice Kanga, Chief Economist at the Central Bank of Kenya, says. He went on to declare that "it will be beneficial, from an economies of scale point of view, to unify the many [African] currencies to face the euro."

Echoing this view, Mr. J.E.O. Mwencha, Secretary-General of the Common Market for Eastern and Southern Africa (COMESA), told *Africa Recovery:* "Strong regional trading blocs are taking shape and we see this as a call for the countries in Africa also to integrate their economies." While he saw this call as one of the euro's positive effects on the 21 member states of COMESA, Mr. Mwencha also cautioned that competition for export markets in euroland is going to intensify. "External suppliers will find it more difficult to penetrate the European market because the euro will make that market even more efficient," he noted. While the European Union is the destination of more than 60 per cent of total COMESA exports, most of those exports are raw materials. Consequently, they may not be too greatly affected by increased competition from other suppliers in euroland, he explained. "But we see the European Union becoming more prosperous and increasingly integrated [as a result of the euro]. So we hope these countries will look outward to invest in Africa, where there is higher return on capital," Mr. Mwencha added.

Within weeks of the euro's launch, the central bank of one COMESA member, Sudan, issued a circular to local banks urging them to conduct commercial transactions in euro. Since the bulk of Sudan's trade is with Europe and because the euro could reduce transaction costs for Sudanese traders, "we are encouraging our

banks to try to deal in euro and to encourage their customers — exporters and importers — also to deal in euro," Mr. Sabir Muhammad al-Hassan, Governor of the Bank of Sudan, told *Africa Recovery*.

But Mr. al-Hassan also pointed out that Sudan may be "a special case" because the economic embargo imposed on it by the US since 1997 makes transfers in US dollars by Sudanese businesses and banks subject to confiscation. "There's a lot of risk involved and there are also additional transaction costs involved to avoid dollars in our transfers. So, by moving into euro, we will remove that risk, of course," he explained.

CFA economies will not benefit from the euro peg unless there are "some reforms of the functioning of the CFA franc zone."

— Fidèle Magouangou
University of the Méditerranée Aix-Marseille II

Still, the euro could help promote regional integration, says Mr. al-Hassan. "In the COMESA area, the trade settlement arrangement is [transacted] in dollars. Because of the US embargo, we were having difficulty benefiting from this arrangement. Now with the euro's introduction we have proposed [to our COMESA partners] that the settlement also be done in euro, not just in dollars." According to Mr. al-Hassan, this would likely increase trading activity throughout the COMESA area.

Ten COMESA member states are also members of the 14-nation Southern African Development Community (SADC). While anticipating that the euro will lead to greater demand for SADC exports by euroland countries, Mr. F.C. Kani, Chief Economist for SADC, also stresses the role of the euro as "a corridor to the low inflation experienced in the euroland region." To the extent that the low inflation rates and low interest rates in euroland result in lower import prices for SADC countries, "this will transmit into lower inflation in the SADC region itself because the pass-through effects of import prices in most SADC economies will be quite high," he explained.

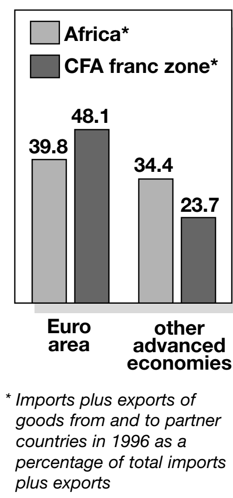
Emphasizing that it is "early days yet," Mr. Kani did not completely rule out an alternative scenario, where macroeconomic performance in euroland deteriorates. "If, for instance, inflation [in euroland] starts going up or there's a recessionary trend in the European economy… that can indirectly have a negative impact on the growth and inflation statistics within the SADC region itself."

Nevertheless, Mr. Kani feels that the euro is more likely to bring benefits than costs to SADC economies. The emergence of a highly liquid capital market from euroland's stable exchange rate regime and low-interest rate environment would be a "very attractive source of capital and short-term financing for African countries, and especially the SADC region," he noted.

"The successful introduction of the euro will stimulate the ambitious and long-term objective of financial integration in SADC," declared Mr. Chris Stahls, Governor of the South African Reserve Bank (the central bank), speaking at a January meeting with ambassadors of euro countries to South Africa.

Mr. Stahls shares Mr. Kani's view that African countries could benefit from the euro's stimulating effect on European capital markets. "As the euro establishes itself as a stable currency, and as liquidity in the financial markets of the participating [euro] countries is integrated, South Africa will most probably look more to Europe, not only for short-term trade financing, but also for raising longer-term loan and equity funds," declared Mr. Stahls.

End-1997 figures show the European Union already accounting for 58 per cent of total foreign investment in South Africa, which has the largest economy in Africa. Moreover, Mr. Stahls forecast an increase in the flow of investment from South Africa to euroland countries.



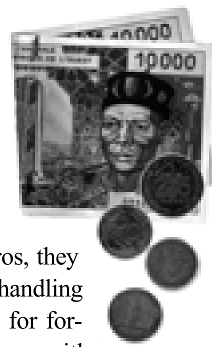
* Imports plus exports of goods from and to partner countries in 1996 as a percentage of total imports plus exports

Source: UN Africa Recovery from IMF, World Economic Outlook, October 1998

More euro transactions likely

Mr. Stahls also pointed out the considerable merchandise trade benefits expected to accrue to South Africa following the euro's launch, in view of the fact that euroland accounts for 28 per cent of South Africa's foreign trade. Predicting that the euro will gain in stature as a major international currency, he said a greater share of South African trade with Europe would likely be transacted in euro in future.

"We've really gone the 'big bang' route at Standard Bank Johannesburg — we can now entertain clients' requests for any of the [euroland national] currencies or for the euro," says Mr. Willie Potgieter, Director of Foreign Exchange and responsible for setting up the euro systems for Standard Corporate and Merchant Bank, a top South African bank. He expects many of the bank's corporate clients to convert to using the euro over the next year as their trading partners in euroland also switch over. As companies convert into euros, they can enjoy the benefits of handling cash and risk management for foreign exchange transactions with euroland in just one currency, he says.



"In response to the challenge posed by the euro, we are expecting to see greater pressure for monetary and economic integration [in West Africa] and this can only serve to boost business volumes," says Ms. Karen Tanoh, financial controller of Ecobank (Ghana). The bank's customers still continue to prefer the national currencies to the euro, reports Ms. Tanoh, though she notes that Ecobank's European counterparts are happier dealing in euro and it is likely the volume of euro transactions will increase in future.

Not all observers expect the euro to have far-reaching effects on their countries' businesses and economies. "In talking to our customers, my impression is that the impact of the euro's introduction has been negligible," says Mr. Atedo Peterside, Chief Executive Officer of Investment Banking & Trust Company (IBTC), a top merchant bank in Nigeria. Mr. Peterside attributes this largely to the fact that the main destination of Nigeria's crude oil, which accounts for some 95 per cent of export revenues, is the US, and the bulk of these exports is priced in dollars. "Even where European countries buy crude oil, they tend to pay a dollar price," he notes.

"But our bank offers accounts in euros since 1 January, the date of the euro's launch. I expect that deutschemark and French franc business will decrease while euro business will increase, though this hasn't really begun to happen yet," he adds. ■