The Significance of Common Currency to the Success of Economic Integration

Oladele Omosegbon

Professor of Economics
DeVoe School of Business

Indiana Wesleyan University
1900 West 50th Street
Marion, Indiana 46953-9393

317-450-0993/765-677-1464 FAX
oladele.omosegbon@indwes.edu

Session:

Allied Social Sciences Association- National Economic Association Annual Conference in
Philadelphia, January 4-7, 2018
The Significance of Common Currency to the Success of Economic Integration

Oladele Omosegbon**

Abstract

The Economic Community of West African States, as one of the regional economic communities in Africa, has been struggling with the creation of a common currency since 2003, when the Eco was scheduled to circulate. But common currency is a necessary condition for an economic community to exist. Without economic union, Africans have been in currency unions before. The ascendancy of ECOWAS in the world stage and the main path to avoid a stunted development, revealed in its logistic population growth, is going to depend on the size of its economy and in the use of a common currency.

JEL: F15, F21, F33 and F45

**Oladele Omosegbon, DeVoe School of Business, Indiana Wesleyan University, at the Allied Social Sciences Association- National Economic Association Annual Conference in Philadelphia, January 4-7, 2018
The Significance of Common Currency to the Success of Economic Integration

Regional economic communities, RECs, in Africa, have been struggling with the creation of common currencies since their inceptions. For the Economic Community of West African States, ECOWAS, the struggle commenced since 2003, when the Eco was scheduled to circulate. We have witnessed several postponements since then, the latest being from the set date of 2015 to 2020. All agents desire a developed, prosperous and united Africa. But if asked about using a common currency, many decision makers run into uncertainties and ambiguities. For many policy makers, the decision of whether to accept a common currency is a big irritation and an embarrassing nuisance.

Academics tend to be intellectually dishonest about the importance of money in an economic community. On the one hand, some display remarkable niceties and dexterity via, for instance, the optimal currency area research, of the near impossibility and incongruence of a common currency in most African RECs Ekong and Onye (2012). On the other hand, others, Feenstra (2014), Feldstein (2008) are quick to go into the exegesis of economic integration in, stating, inter alia, that economic unions tend to ensure the free flow of human and material resources among cooperating nations, and hence, countries uniting tend to benefit. But this is intellectually dishonest, because only when common money is instituted can there be the kind of benefits everyone is talking about regarding economic union and cooperation among nations. Common currency is a necessary condition for an economic community to exist but not sufficient. It is sufficient when there is political unification (Fisher, 2011). This fact that common currency is only a necessary condition for an economic community to operate gives some flexibility for the African Union, AU, and its constituent RECs to establish a functional common
currency that will kick start a rather uninspiring, invariant economic fortune, befalling her since the colonizing countries of Europe left more than fifty years ago.

A common currency is itself a signal to a promising and prosperous economic union, bringing to fruition the role money plays in traditional individual economies throughout the world and throughout time. But the new opportunities in the expanded multistate economy bring added platforms for money to play an accelerated and deepening function in not just banking and financial development but also in the overall living of the unionizing peoples. Economic union implies an integration which culminates from the movements from free trade area through customs union to monetary union.

I. Money not the Root of all Evil but an Indispensable Friend

In the grand scheme of things, money is sometimes seen as a stumbling block to wellbeing. We all have examples of clichés like money is the root of all evil, money does not buy happiness and the like. Economists and social scientists readily attempt to compare people and their welfare across the world. We tend to measure happiness and call some citizens the happiest or the least happy in the world. If we measure welfare by GDP, we find no association whatsoever using the Happiness Surveys (sense of purpose, social relationships, financial situations, community involvement and physical health) between happiness and the size of GDP. In fact, the happiest countries, Panama, Costa Rica, Puerto Rico, tend to have relatively smaller GDPs. (Rettner, 2015).

At the individual level, money helps to eliminate wants (poverty) and create freedom; the freedom to move and the freedom to live (Zach, 2017). At the firm level, money dictates the flow of resources and the exercise of preferences by consumers and producers. Money is the basis of intertemporal, intergenerational and international transfer of resources. At the level of a nation
and hence an economic community, common currency facilitates the competitive power of the community in trade and in the bidirectional flow of assets. Common currency is necessary for an economic union and can be created with a lot less difficulty than our African leaders have made it to look so far. After all, without economic union, Africans have been in currency unions before. Examples include in British West Africa, the pound; in Eastern Africa, the East African Shilling and since colonial times, we have been witnessing the many perennial facets of the CFA franc.

II. Stylized Impediments to the use of Common Currency

Following the example of the European Union’s strict criteria employed in preparing for the launching of the Euro in the 1992 Maastricht Treaty, African countries, including those in ECOWAS, now adopt what are known as Convergence Criteria to gauge, among other things, the readiness of the community in adopting a common currency. For ECOWAS, these are a set of ten (four primary and six secondary) conditions members are expected to meet in order to be assessed ready for the adoption of a common currency, UNECA (2017), Saka, Onafowokan, and Adebayo (2015). It is clear that these criteria have not been met, at least, that is the reason given for the now more than five postponements of dates of circulation of the Eco, the latest postponement was by the Committee of Governors of the Central Banks in ECOWAS announcing a new date of 2020 (Premium Times, July 4, 2016).

It is believed that the real reason the Eco is not circulating in West Africa is due to two factors. The first is the time inconsistency in the decision making by the heads of governments of member states (Omosegbon, 2017). Secondly, it is clear that the CFA, which has been circulating in much of Africa since 1945, is now of questionable benefit to the long-term development of the continent. The two zones of CFA, which are mainly in West and Central Africa, are tied to the
fixed rates based on historical agreement between France and its mostly ex colonies. When there are big swings in the values of cotton and cocoa, some of the primary exports in these CFA countries, or when these countries go into tail spins of political and election instabilities, the exchange rate of the CFA is relatively unaffected. Thus, offering the elite and the middle class in the CFA countries cheap foreign goods and leave the farmers and average consumers with low revenues, since exports are relatively expensive while there is a worldwide decline in demand for these exports at the same time.

III. Africa and Africans: A Race against Time

For ECOWAS, forty-two years on, the dream of an economic union with a common currency and integrated economies is yet to be realized. While it is generally agreed that African economies are underdeveloped or are developing, it is time to start thinking about what the end game is likely to be. The time is not infinite for Africa to make its mark in the world. These economies cannot afford to remain developing for the next fifty years, otherwise, their demographic characteristics would be stunted or dwarfed (Figure 2). It is a good thing that the median age in almost all African countries are below or around 20 years, compared to the more advanced societies of North America, Europe, Japan and Australia, where the median age in many of the countries is around 40 years or more. It is, however, likely, that the huge increases in population expected in these African countries in the coming years would pose serious problems if there are no commensurate advancements in material living. Africa is already predicted to be home to most of the world’s population by 2100 as shown in Tables 1 and 2.

The troubling part of this is that by 2100 (projected populations for 2100 are used as the carrying capacities below), these economies are not predicted to be among the advanced in the
world. In the PwC analysis for projections to 2050, for instance, no single African country makes the list of the top 10 economies (https://www.pwc.com).

TABLE - 1. TEN MOST POPULOUS COUNTRIES IN THE WORLD BY 2100  

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>2050 Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>India</td>
<td>1.66bn</td>
</tr>
<tr>
<td>2.</td>
<td>China</td>
<td>1.004bn</td>
</tr>
<tr>
<td>3.</td>
<td>Nigeria</td>
<td>752m</td>
</tr>
<tr>
<td>4.</td>
<td>US</td>
<td>450m</td>
</tr>
<tr>
<td>5.</td>
<td>DR Congo</td>
<td>389m</td>
</tr>
<tr>
<td>6.</td>
<td>Pakistan</td>
<td>364m</td>
</tr>
<tr>
<td>7.</td>
<td>Indonesia</td>
<td>314m</td>
</tr>
<tr>
<td>8.</td>
<td>Tanzania</td>
<td>299m</td>
</tr>
<tr>
<td>9.</td>
<td>Ethiopia</td>
<td>243m</td>
</tr>
<tr>
<td>10.</td>
<td>Niger</td>
<td>209m</td>
</tr>
</tbody>
</table>

Source: Indy100 (2017)

TABLE 2 - AFRICAN COUNTRIES AMONG THE TEN MOST POPULOUS

<table>
<thead>
<tr>
<th>Country</th>
<th>Median Age 2017</th>
<th>Current Population</th>
<th>Pop. Growth Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nigeria</td>
<td>18.3</td>
<td>752247</td>
<td>2.7</td>
</tr>
<tr>
<td>Congo (DRC)</td>
<td>18.4</td>
<td>388733</td>
<td>3.2</td>
</tr>
<tr>
<td>Tanzania</td>
<td>17.6</td>
<td>299133</td>
<td>3.2</td>
</tr>
<tr>
<td>Ethiopia</td>
<td>17.8</td>
<td>42644</td>
<td>2.5</td>
</tr>
<tr>
<td>Niger</td>
<td>15.3</td>
<td>209334</td>
<td>4.1</td>
</tr>
</tbody>
</table>

IV. A Primer in Population Growth

Evolutionary biologists and ecologists often propose that the growth of populations of all sorts follows an exponential process. But since we all know by now that populations cannot grow monotonically, the logistic model is hypothesized as a better approximation to this growth process. This way, the growth of populations depends on the size of the population, and the net birth rate (Study.com, 2017). In what follows, it is assumed that population change follows a logistic growth process, which can be approximated by (confirmed by examining world population increases by the billion mark since 1800):

\[
\frac{dN}{dt} = kN(1 - \frac{N}{K}) \quad \text{or} \quad \frac{dN}{dt} = kN\left(\frac{K-N}{K}\right)
\]
N(t) represents population at time t; t = 0, 1, 2..., when the population grows or decays; k is the relative or intrinsic rate of increase of the population; K is the carrying capacity i.e. maximum population that is sustainable by available resources, all else constant.

Data from 1800 reveal that the exponential trend line turns logistic at advanced stages when the world population becomes bigger and bigger: it now takes 14, 18 and 40 years to increase by one billion instead of 12 years earlier, when world population was expanding at faster paces of k. This implies little room for rapid human development for matured population demographics without corresponding economic advancement (dwarfed development). An example of this logistic shape is given by Vandermeer (2010) for the United States population where declines in k originated from higher U.S. population density (Figure 1).

**Figure 1. Population Growth and Density Dependency in the U.S.** Vandermeer, J. (2010, Figure 4)

Returning to equation (1), we can solve for the population at any time t, that is consistent with the carrying capacity, given an initial population value N₀. Vandermeer (2010), equations 1-8; Snider and Brimlow (2013).
(2)  \[ N(t) = \frac{K}{1+Ae^{-kt}} \text{ and } A = \frac{K-N_0}{N_0} \]

Estimating (2) for African countries, those that make the list of ten most populous countries in the world (Table 2), show none is able to make it to its carrying capacity population of the year 2100, which is 85 years out, \( N_0=2015 \), at current population rates. In fact, Niger, the least sustainable, exhausts the gap in ten years while Nigeria, the most sustainable, in 48 years.

Figure 2 is drawn assuming current intrinsic rates of growth are reasonably curtailed by subtracting 1 from its current rates in Table 2. Because of high intrinsic rates of growth in Tanzania and Niger, none of them is still able to postpone the real possibility of dwarfed development that comes with population density. However, Ethiopia and Nigeria are able to grow to their estimated carrying capacity at the end of the period, which is 2100 – period 85.
V. Common Currency Union: The Way Forward

An economic union with a flourishing common currency promises to confer a real importance to Africa’s RECs. It places each to compete as a strong trading bloc in the world for years to come. In the case of ECOWAS, it is the circulation of the Eco in the now 16-member countries with the recent admission of the Kingdom of Morocco. If a common currency, with flexible exchange rate, had been in use, it would take the place and the importance of money in a national economy. In international trade, it would eliminate all the encumbrances of multiple currencies, transaction costs and the vexing issues of triangular currency convertibility.

The ability to directly compare the value and price of goods traded allows several markets to come together forming a homogeneous structure based on one common unit of account. Adoption of a single currency exposes domestic markets to foreign markets thereby increasing competition between member countries and enhancing the competitiveness of national industries. (Saka, O., Onafowokan, A., and Adebayo, A., 2015, p.233).

V. Summary and Conclusion

A common currency is a necessary condition for the realization of the benefits of integration. Common money is the signification of an economic community and a united and developed people. The importance of African economies in global trade is not going to be judged by the power of each country’s individual economy, for there is none, so far, or the stability provided by the benevolence of a colonial master in the use of, for instance, the CFA franc, but in the actual share of the proposed Eco, for ECOWAS countries, in world official foreign reserves, its liquidity in international trade and its role as a competitor against existing reserve currencies of the U.S. dollar, the Euro, the Pound Sterling, the Yen and the Yuan.
Parenthetically, given current demographic conditions with its intrinsic rate of increase, \( k \), many African countries would be mired in a dwarfed or stunted development for years to come. Even, among a few, like Nigeria and Ethiopia, which are able to sustain their populations at current levels far into the future, we note that these are only developing levels of living at best. Thus, it is a sobering manifestation that the only way to avoid a dwarfed or stunted development is for African countries to complete their economic integration efforts of which the circulation of a common currency is a necessary condition. The ascendancy of African countries in the world stage is going to depend, strongly, in the use of its currency as an intervention and an anchor money. This is only possible if the RECs come to full fruition with flourishing common currencies, commanding a widely acceptable internal purchasing power.

References


   


