South Africa's role in macroeconomic convergence in SADC

J Rossouw[1]

Introduction

In an analysis of economic goals for Africa, it becomes immediately obvious that the macroeconomic convergence goals set for its various regions are important preconditions for long-term stability. The achievement of these goals is a major challenge, and the governments of countries committed to convergence have to apply sound macroeconomic management and policy principles for the goals to be achieved. Achieving the goals will contribute to Africa's economic stability and, therefore, economic growth and job creation. As an important region in Africa, the Southern African Development Community (SADC) serves as an example to the rest of Africa in the achievement of the convergence goals.

This paper considers progress towards the achievement of macroeconomic convergence targets in SADC and South Africa's supporting role in this regard. Only the economic aspects underpinning convergence are considered. Political initiatives or obstacles are outside the scope of this conference and therefore of this paper, as such challenges should be ideally addressed at a conference focusing specifically on political challenges facing the achievement of convergence goals in Africa.

The paper is arranged as follows: The first section describes SADC and other monetary unions and regional monetary co-operation initiatives in Africa. The second section highlights the macroeconomic convergence criteria and goals set for the SADC region. An assessment of the achievement of the convergence goals by SADC countries is highlighted in the third section. The fourth section highlights an important lesson for SADC from failed earlier attempts to establish monetary unions in Europe. The last section concludes.

Monetary unions and macroeconomic convergence initiatives in Africa

The African continent is characterised by numerous co-operation initiatives between countries in different regions, but explicit currency arrangements or convergence criteria and goals have been set only for the Common Monetary Area (CMA), the two CFA franc zones, the Economic Community of West African States (ECOWAS) and SADC.

The CMA comprises South Africa, Lesotho, Namibia and Swaziland (Metzger, 2004[2]). The CMA was initially established as the Rand Monetary Area, with South Africa, Botswana, Lesotho and Swaziland as members. Botswana left the CMA in 1976 and Namibia joined after its independence in 1990. Although member countries have their own currencies, these currencies trade at par and these countries also apply similar exchange control regulations, implying that capital flows freely between the CMA countries (Nielson et al., 2005: 711).

The South African rand serves as an anchor for the currencies of the CMA owing to the dominating role of the South African economy in the CMA, and the South African Reserve Bank serves as *de facto* (albeit not *de jure*) central bank of the CMA. South Africa's gross domestic product (GDP) *per capita* is, for instance, 1,5 times that of Namibia and nearly six times larger than that of Lesotho (Masson et al., 2005: 67). In addition, South Africa's GDP comprised some 95 per cent of the GDP of the CMA in 2002 (ISS, [S.a.][3]). No macroeconomic convergence criteria have been set for CMA countries, owing to the fact that these countries all adhere to the criteria set for SADC.

[1] The views and opinions in this paper do not necessarily reflect the views and opinions of the Reserve Bank.
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The two CFA franc zones, established after the Second World War, are the following:

- West African Economic and Monetary Union (WAEMU), comprising Benin, Burkina Faso, Guinea-Bissau, Ivory Coast, Mali, Niger, Senegal and Togo, with the BCEAO in Dakar as its central bank, and a regional development bank in Lomé (US Department of State, 2002: 1). In this instance CFA is an abbreviation for *Communauté Financière Africaine* (IMF Survey, 2002: 284). The regional currency has been pegged, with the support of France, to the euro since its inception, after it had been pegged to the French franc since 1949. No convergence criteria have been set for the zone.

- Central African Economic and Monetary Community (abbreviated as CAEMC or as CEMAC in French), comprising Cameroon, Central African Republic, Chad, Equatorial-Guinea, Gabon and the Republic of Congo (Republic of South Africa, 2004: 1), with the BEAC in Yaoundé as its central bank. In this instance CFA is an abbreviation for *Coopération Financière en Afrique centrale* (IMF Survey, 2002: 284). With the support of France, the regional currency is in this instance also pegged to the euro, after having been pegged to the French franc since 1949. As is the case with WAEMU, no convergence criteria have been set for the CAEMC zone.

The Economic Communion of West African States (ECOWAS) ratified macroeconomic convergence criteria and goals for its member countries on 20 April 2000. ECOWAS was established in 1975 in terms of sections 3 and 51 to 55 of the treaty on the establishment of an economic and monetary union for the member countries, comprising Ghana, Guinea, Liberia, Nigeria, Sierra Leone and the Gambia (WAMI, [S.a.][4]). In order to achieve the goals of ECOWAS, the heads of state of five member countries ratified a declaration for the establishment of the West African Monetary Zone and agreed that a common currency for the region would be called the ECO on 20 April 2000 in Accra (WAMI, [S.a.]). Liberia elected not to ratify the declaration owing to the burden of rebuilding its infrastructure after a period of internal conflict (WAMI, [S.a.]).

The SADC region, the largest region in Africa striving, *inter alia,* towards macroeconomic convergence goals, comprises Angola, Botswana, Democratic Republic of Congo (DRC), Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe, and Madagascar that joined during August 2005. A previous member, the Seychelles, left SADC owing to a number of reasons, *inter alia,* the cost of membership. The activities of SADC are co-ordinated by a secretariat, located in Gaborone in Botswana (Background information on SADC, 2000[5]).

The Southern African Development Co-ordination Conference (SADCC), established on 1 April 1980 in Lusaka, Zambia, preceded SADC. The SADCC changed its name to SADC on 17 August 1992 in Windhoek, Namibia (Background information on SADC, 2000). South Africa joined SADC in 1994. SADC's macroeconomic convergence goals are highlighted in the next section.

Macroeconomic convergence goals for SADC

SADC has agreed to macroeconomic convergence criteria and goals for countries of the region. These are, according to Masson et al., " … a set of indicators that will allow monitoring of progress towards … convergence" (2005: 114). This aligns SADC with initiatives aimed at promoting " … economic development in Africa. Article 44 of the Abuja Treaty calls for the harmonisation of economic policies across the African continent. The Treaty emphasises two important pillars of economic integration across the African continent: The promotion of intra-Africa trade and the enhancement of monetary co-operation. The African Monetary Co-operation Programme (AMCP) seeks to operationalise the monetary co-operation mandate of the Abuja Treaty. In the main, this involves a single monetary area, encompassing a common

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currency and a common central bank … [for Africa] … by the year 2021" (Mboweni, 2003[6]). Progress towards the achievement of these goals is monitored by the Committee of Central Bank Governors (CCBG) in SADC. As South Africa has been entrusted with sectoral responsibility for finance and investment in SADC (Background information on SADC, 2000), the CCBG is chaired by the Governor of the South African Reserve Bank, Mr T T Mboweni.

Convergence goals have been set for 2008, 2012, 2015 and 2018, with more challenging goals set for the later periods. The convergence criteria and goals are contained in a Memorandum of Understanding, agreed to by the Ministers of Finance of countries in the SADC region. In terms of the initial criteria set for 2008, SADC countries should have single-digit inflation rates; a budget deficit of less than 5 per cent of GDP; the nominal value of public and publicly guaranteed debt, as a ratio of GDP, should not exceed 60 per cent; foreign reserves should be equal to three months' imports; and central bank credit to the government should be less than 10 per cent of the previous year's tax income (see for instance Mboweni, 2003). Co-operation aimed at achieving macroeconomic convergence in SADC and regional integration are also enhanced by " … [t]he harmonisation of legal and operational frameworks of SADC central banks, the SADC payment, clearance and settlement systems, as well as the co-ordination of training of central bank officials" (Gaolathe, 2004: 5). The macroeconomic convergence targets for the relevant years are summarised in Table 1.

Table 1 Macroeconomic convergence criteria and goals for SADC

Criterion	2008	2012	2015	2018
Inflation rate	Single digits	5%	5%	3%
Budget deficit	5% or less of GDP	3% of GDP as anchor, with a range of 1%	3% of GDP as anchor, with a range of 1%	3% of GDP as anchor, with a range of 1%
Government debt*	Less than 60% of GDP	Less than 60% of GDP	Less than 60% of GDP	Less than 60% of GDP
Foreign reserves	3 months' import cover	More than 6 months' import cover	More than 6 months' import cover	More than 6 months' import cover
Central bank credit to the government	Less than 10% of the previous year's tax income	Less than 10% of the previous year's tax income	Less than 5% of the previous year's tax income	Less than 5% of the previous year's tax income

* Government's domestic and foreign debt and debt guaranteed by government

Sources: Adapted from Mboweni, 2003; and Mboweni, 2005; see also Rossouw, 2006

The next section analyses the current status of SADC countries in respect of achieving the macroeconomic convergence criteria.

Assessment of macroeconomic convergence in SADC

Progress with regard to the goal of achieving the convergence goals is monitored by the CCBG in terms of SADC's *Regional Indicative Strategic Development Plan*, launched on 12 March 2004 in Arusha, Tanzania (Gaolathe, 2004: 4). Table 2 highlights the achievement of convergence criteria set for 2008 by each of the SADC countries, based on data for 2004; the period for which the most recent information is available.

In respect of inflation, the majority of the SADC countries already achieved by 2004 the convergence goals for 2008. Only four countries did not achieve by 2004 the inflation goals set for 2008.

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Table 2 Achievement by 2004 of macroeconomic convergence goals set for 2008

Country	Inflation rate (single digits)	Budget deficit (< 5 % of GPD)	Government debt (< 60 % of GDP)	Foreign reserves # (3 months' imports)	Central bank credit to the government (< 10 % of tax income)
Angola	31,0	- 7,0	**	**	5,7
Botswana	7,8	- 0,2	5,0	17	0,0
DRC	9,2	- 0,8	**	1	42,9
Lesotho	5,1	- 5,2	53,7	5,7	5,9
Malawi	11,5	- 6,4	163,9	2,3	60,0
Mauritius	4,7	- 5,4	56,5	**	7,2
Mozambique	9,1	*	**	5,4	0,0
Namibia	3,9	- 1,6	35,1	**	0,0
South Africa	1,4	- 1,9	36,0	5	5,3
Swaziland	3,4	- 3,6	24,1	2	5,3
Tanzania	4,1	- 3,3	88,9	8	10,4
Zambia	18,0	- 1,7	**	1,3	36,1
Zimbabwe	350,0	- 6,7	95,0	**	6,5

* The GDP of Mozambique has not yet been calculated for 2004
** Figures not available
\# Figures in months

Sources: Adapted from Banco de Moçambique, 2005; and Committee of Central Bank Governors, 2005

SADC countries showed the largest degree of macroeconomic convergence in respect of containing budget deficits in terms of data for 2004. However, in this analysis it is important to note the difference between the calculation of the ratios for the budget deficit and for central bank credit to the government. The deficit calculation regards grants received by the government as income in as much as the criterion is set for a deficit specified as the difference between expenditure on the one hand and revenue plus grants on the other (Committee of Central Bank Governors, 2005: D-25).

SADC countries still experience problems with the calculation of government debt figures as they lack aggregated data on internal and external public debt (Banco de Moçambique, 2005: 16) and they experience problems in ascertaining the extent of government debt guarantees. Moreover, based on 2004 data, divergence rather than convergence occurred between the government debt figures of the countries that had the necessary information available, as the figures ranged from 5,0 per cent in the case of Botswana to 163,9 per cent in the case of Malawi.

As is the case with government debt, SADC countries experience difficulty in calculating foreign reserve levels, while large discrepancies between reserve levels of the countries are obvious in terms of the 2004 data.

In 2004 central bank credit to the government as a percentage of the previous year's tax income ranged between zero in three SADC countries and 60 per cent in the case of one country, implying that achievement of the convergence goal might still take some time. However, contrary to the criterion used for the calculation of the budget deficits of SADC countries, the criterion for central bank credit to the government is measured in respect of tax revenue of government only (Committee of Central Bank Governors, 2005: D-25 and D-27).

From this analysis it transpires that by 2004 SADC countries by and large achieved the criteria set for 2008, albeit with a minority of countries experiencing difficulties to manage their macroeconomic policies towards convergence. These countries are not only in the minority, but also accounted for a relatively small portion of SADC's gross domestic product (GDP) by 2002 (the most recent comparable data available for all SADC countries), as is evidenced by Table 3.

Table 3 Composition of SADC's GPD by 2002, number (out of five) of convergence goals for 2008 achieved by 2004 and weighting of achievement of convergence goals

Country	GDP in rand millions in 2002*	Percentage contribution	Number of criteria achieved by 2004	Weighted achievement of criteria
Angola	105 918	5,5	1	0,055
Botswana	53 010	2,8	5	0,140
DRC	58 451	3,0	2	0,060
Lesotho	7 370	0,4	3	0,012
Malawi	20 240	1,1	0	0
Mauritius	49 878	2,6	3	0,078
Mozambique	43 222	2,2	2	0,044
Namibia	31 550	1,6	4	0,064
South Africa	1 168 778	61,0	5	3,050
Swaziland	12 437	0,6	4	0,024
Tanzania	102 783	5,3	3	0.159
Zambia	37 880	2,0	1	0,020
Zimbabwe	230 262	12,0	1	0,120
SADC	1 921 779	100,0	2,6**	3,826

* Local currency values converted to rand at average official exchange rate against the rand in 2002
** Number of criteria achieved added together and divided by number of countries

Sources: Adapted from Banco de Moçambique, 2005; Bank of Zambia, [S.a.], and Committee of Central Bank Governors, 2005

The calculation of rand values of the GDP of the SADC countries is not without problems. Zambia and Zimbabwe serve as examples. The Zambian GDP is reported in kwacha as ZK16 250 million (Committee of Central Bank Governors, 2005: T-67). At the prevailing exchange rate of ZK428,4 = R1 in 2002, this equates to a GDP of R38 million, which is a serious misrepresentation of economic activity in Zambia. This figure was accordingly ignored and GDP data available on the website of the Bank of Zambia were used to calculate the GDP figure for 2002. The Bank of Zambia reports the GDP for 2002 as ZK16 228 billion (Bank of Zambia, [S.a.][7]), which is equal to R37 880 million when converted at the prevailing exchange rate for 2002. This figure was accordingly used in Table 3, although it still seems to underestimate the relative size of Zambia's GDP in SADC.

The data available for Zimbabwe pose two problems: (i) Whereas the official rand/Zimbabwe dollar exchange rate for 2002 was used for conversion purposes, the country is characterised by informal foreign-exchange trading in a parallel market; and (ii) between 2002 and 2003, the official exchange rate dropped from Z$1 = R0,1902 to Z$1 = R0,0259, i. e. the currency lost some 86 per cent of its value in the official market. Over the same period, the nominal Zimbabwean GDP increased from Z$1 210 636 million to Z$5 153 358 million. Disregarding inflation over this period, it implies that the nominal GDP of Zimbabwe declined in rand terms from R230 262 million in 2002 to R133 472 million in 2003, or from some 12 per cent of the GDP of SADC to some 6,9 per cent. The relative size of the Zimbabwean economy in SADC by 2002 should accordingly be regarded as a best estimate only.

In weighting the achievement of the number of convergence criteria per country in accordance with its relative importance in terms of the GDP of each country, an even higher degree of achievement by 2004 of the convergence criteria set for 2008 is shown. This is a reassuring finding, as economic stability in a large economy such as South Africa will have positive spill-over effects in smaller economies in SADC. Moreover, South Africa can easily assume a role in SADC similar to its role in the CMA.

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Lesson from failed earlier monetary unions in Europe

Masson et al. (2005) recently made an assessment of macroeconomic convergence initiatives and criteria in Africa. In respect of SADC, they reach the conclusion that "[t]he concept of a full monetary union among the SADC countries of southern Africa seems infeasible at this stage … " (2005: 9), citing as one of the reasons for this conclusion that SADC countries are still a long way "… from having converged with the macroeconomic stability of South Africa and its CMA partners" (2005: 9). They also reiterate (2005: 128) the earlier conclusion reached in 1996 by Jenkins et al. that " … the apparent lack of convergence of the southern African economies over time and the current divergence of policy and stability indicators suggest that southern Africa is not yet ready for regional monetary integration" (Jenkins et al., 1996: 23) in their study *Is Southern Africa Ready for Regional Monetary Integration?*

Although Table 3 confirms the conclusion of Masson et al. about a higher degree of convergence between CMA countries than between SADC countries, their overall assessment is too pessimistic when the achievement by 2004 of macroeconomic convergence goals set for achievement by SADC countries in 2008 is considered. Moreover, South Africa's commanding role in SADC, highlighted in Table 3, and its compliance in 2004 with four of the convergence criteria, imply that a positive spill-over effect to other countries in the region will follow.

Monetary unions are never achieved without overcoming continued challenges, as is evidenced by earlier experiences in Europe. Although it is virtually impossible to date the earliest attempts to achieve political and economic unification in Europe, Vanthoor mentions that "[t]wo thousand years of European history bear witness to continual attempts to convert Europe … into a political and economic union" (1996: xiii). Vanthoor traces modern attempts to a united Europe to the introduction of a federal government in Switzerland in 1848 (1996: 4).

In his analysis of developments since 1848, Vanthoor (1996: 141 to 145) identifies the following important previous international monetary unions in Europe, other than the latest monetary union which resulted in the European Central Bank and the acceptance of the euro as a single currency:

- German-Austrian monetary union from 1857 to 1867 between Germany, Austria and Liechtenstein;
- Latin monetary union from 1865 to 1926 between Belgium, France, Italy and Switzerland, which Greece also joined in 1869; and
- Scandinavian monetary union from 1873 to 1931 between Sweden and Denmark (which at the time also included Iceland), and was joined by Norway in 1877.

Vanthoor cites a number of reasons for the disbanding of these earlier monetary unions. By way of summary, however, the German-Austrian monetary union ended in 1867 owing to an economic agreement (supported by a political agreement) reached between Austria and Hungary. The Latin monetary union ended because Switzerland refused to accept as legal tender silver five franc coin minted outside its borders. The Scandinavian monetary union effectively ended when it was decided that certain coin of member countries would no longer be legal tender in all the member countries in the monetary union (1996: 31, 41, 141 to 145).

A deciding factor in each instance leading to the termination of these earlier monetary unions was a lack of a single currency. SADC (and the other regions in Africa) will be able to overcome this problem by establishing regional central banks within the monetary unions, implying the adoption of single regional currencies – by 2016 in the case of SADC.

Conclusion

This analysis of the extent to which SADC countries have achieved the convergence goals shows that considerable progress had already been made by 2004 towards the achievement of the convergence goals set for 2008. This assessment leads to the conclusion that the degree of compliance with the criteria will increase even further between 2004 and 2008, indicating that the region is on track to its goal of a single currency and regional central bank by 2016.

Moreover, in its stated objective of introducing a single currency, the SADC region will avoid the one deciding factor that led to the termination of the earlier monetary unions in Europe, i.e. the timely introduction of single currencies. A single central bank in SADC will contribute to regional economic stability, which is a precondition for the sustained economic growth and job creation required not only in SADC, but also in the rest of Africa. The challenge facing South Africa, given its dominant economic role in SADC, is to ensure the necessary macroeconomic stability in the region to foster continued progress towards the achievement of the convergence goals.

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