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The Devaluation of the CFA Franc: Some Preliminary Results

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Résumé: La dévaluation du franc CFA officiellement annoncée le 11 janvier 1994 a eu lieu suite à la détérioration constante et générale des économies des pays africains de la zone franc depuis les années 1980. Ce processus fût marqué par des crises financières répétées qui ont mené à l'adoption de toute une série de programmes d'ajustements structurels avec la plupart du temps la bénédiction des institutions de Bretton-Woods. Alors que d'autres pays en développement d'Amérique latine et d'Asie sont parvenus à modifier la structure de la composition sectorielle de leurs économies et à gagner des parts du marché mondial, les exportations de la zone franc n'évoluent pas depuis 1985. L'étude relève les premiers résultats de l'effet de la dévaluation sur les économies de la zone franc après une année d'application et tente de vérifier si les mesures d'accompagnement qui ont été prises dans le cadre de l'ajustement structurel pourront relancer ces économies, basées sur une restriction de la demande et poursuivies pendant trop longtemps dans des circonstances où il fallait plus de réflexion et une plus grande insistance sur les politiques d'offre intérieures et de «développement durable».

General Overview

Among the many facets of the relations between Europe and Africa is the link between France and its former thirteen colonies, grouped into a so-called 'Communauté financière africaine' (CFA). The CFA zone is a monetary arrangement consisting of two currency unions, one in the West and the other in Central Africa, whose rules of operation are connected with France. The common currency of the two unions — the CFA franc — was freely convertible and guaranteed by the Bank at fixed exchange rate since 1947 and any change in parity requires the unanimous consent of the CFA zone member states, including the French government. In turn, the CFA member states were required to deposit 65 per cent of their exchange reserves in French francs with the Bank of France.

In 1990, however, within the context of the Single European Market, the French government has advocated the substitution of this special institutional

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relationship with a new one, involving direct links between the CFA franc and a proposed European Federal Reserve Bank. Hence, starting that year, the CFA franc was effectively pegged to the ECU as realignment between French franc and other EC currencies became more infrequent and inflexible. However, if the Delors Plan for a European monetary union proceeds as planned during the late 1990s, the future of the relationship between the CFA franc zone and the Bank of France may be called into question and the other EC member states were much less sympathetic to the maintenance of direct financial relations with what they perceive as unstable economies of Africa.

Although the precise structure of the European monetary union has yet to be decided, the majority of EC currencies are already very tightly aligned to one another. With this tight monetary policy and an increasingly fixed exchange rate, the African CFA zone countries will find it difficult to maintain their competitiveness because their CFA currency will, in effect, be overvalued, as they will be unable to influence collective EC actions at a time when France is increasingly distracted by European policy imperatives.

Hence, the African franc zone countries feared that any diminution or weakening of franc zone links after the SEM 1992 could well result in a diversion of investment and financial flows from Europe in general, and from France in particular to their economies, since there will be a greater loss of control over their exchange rate determination as the 1992 SEM programme unfolds. There were two alternatives left to them. At first, the CFA zone members took all these contingencies into account in the post-1973 energy crisis period in maintaining the original decision of fixed parity and, hence, forgo the opportunity to devalue their nominal exchange rate because the founders of the zone calculated the inflation-controlling benefits of a fixed exchange rate but they did not anticipate the costs in terms of their countries' inability to adjust to unfavourable external circumstances. Hence, the very faster and more stable growth in the 1970s prevented them from adjusting to external shocks of the 1980s.

The other alternative was that, as the French franc becomes increasingly tied to other European currencies, so does the CFA franc, and therefore. if the Delors Plan for a European monetary union is adopted, the CFA franc will be pegged to the single European currency and the parity of the CFA franc to that currency will have to be re-established, by effecting the devaluation that until recently has been resisted; otherwise, if the other European partners are unwilling to support the CFA franc, the outcome may be a severing of its link with the French franc. This may have been one of the reasons why the Heads of State and Government of the zone countries were compelled to take a decision in January 1994 in

Dakar, to devalue the CFA franc by 50 per cent, with a parity changing from 1 FF = 50 F CFA to 1FF = 100 F CFA. However, a change in the CFA franc parity is equivalent to abandoning its fixed exchange rate and the credibility, which made the original arrangement tenable for so long, is now lost. Once it is known that the CFA franc can be devalued, pressures will amount for it to be devalued again and again. Once this process is set in motion, the convertibility of the currency and the guarantee from the Bank of France or from the future European Federal Reserve Bank could become less tenable and be abandoned.

The question of overvaluation of the CFA was the very controversial one, in its magnitude and its effects not only *vis-à-vis* the European currencies but also its coexistence *vis-à-vis* the neighbouring countries' currencies most of which have known constant devaluations during the 1980s. The fact that the CFA was not adjusted created distortions to the detriments of exports of the member countries of the CFA zone. The fixed parity and overvaluation of the CFA franc have impaired the flexibility and mobility of factors in the franc zone and led to loss of competitiveness as the productivity and the proportion of goods with a high added value in the export sector had not improved since the middle-1980s. However, the fixed parity ensured stability in the exchange rate which reduces the risks and prevents the inflationary anticipations. The question raised is whether or not the devaluation of the CFA franc will be profitable for the CFA zone member countries.

The attendant needs of devaluation is to shift resources from non-tradable to tradable by reducing export prices in the foreign currency and increasing import prices in the local currency. By putting exports cheaper, it increases foreign demand of the country's exports and hence increases foreign exchange receipts; and parallelly, by making imports expensive, it reduces the domestic demand for imports, reduces the external payments and hence, improves the trade and the situation of balance of payments.

The other advantage of devaluation is that it eliminates the overvaluation of the local currency and makes the traded products more competitive in the international market. But, in order to realise this, certain conditions have to be met: that the sum of price elasticity of export demand and the price elasticity of import demand is greater than one (Marshall-Lerner conditions). But looking at the structure of African exports, it is less probable that these price-elasticity conditions be met, given the fact that the price of raw agricultural products and some mining products were low and failing in the international markets. The adjustment of the demand elasticities to changes in relative prices take time in order that their sum exceeds one unity. Local prices can increase in the proportion of devaluation should a deflationary policy (reduction of public

spending and compression of the money supply) be missing and this will be to the detriment of the production and employment.

The experience of the other non-CFA African countries showed that constant changes in the exchange rate in the 1980s had not allowed countries to rectify the external disequilibrium. On the contrary, the deficit of balance of payments continued to increase and that the rate of inflation was much higher in these countries than in the CFA zone countries (UN-ECA 1991:16). In the case of the CFA zone, the current account of the CFA countries started to deteriorate in 1984, due to the drastic fall in the price of cacao (Côte d'Ivoire), coffee (Cameroon), uranium (Niger), and petroleum (Cameroon, Gabon and Congo). However, the current account of the other CFA countries than these improved despite the overvalued CFA currency *vis-à-vis* the US$ by 30 per cent between 1984 and 1989. Therefore, one would expect that the devaluation of CFA franc may have the following effects: (i) increase in the general price level; (ii) the deterioration of balance of payments due to the non-satisfaction of the Marshall-Lerner conditions, as there is in the CFA countries a very strong domestic demand for imported products and a very weak external demand for export products; (iii) an increase in external debt burden through increased debt servicing ratios.

The preliminary study presented by ECA at the conference of African Ministers of Finance in Libreville, however, shows that these perversive effects of devaluation can be attenuated if there are at the same time accompanying measures such as : (a) the implementation of restrictive fiscal and monetary policy (compression of budgetary spending and price controls); (b) an increase in external aid by 30 per cent increase achieved in past years); (c) the implementation of differential interest rate and selective credit policies; (d) consolidation of debt relief and debt cancellation; (e) transformation and diversification of production and trade through the implementation of dual or multiple exchange rate policy; (f) strengthening of the subregional monetary cooperation between CFA and non-CFA countries through ensuring stable convertibility between African currencies and renegotiation of monetary agreements with France (UN-ECA 1994).

This paper summarises, first, the ECA simple simulation model, stating its perceived assumptions and results. Second, the paper analyses the economic situation in the CFA zone countries after the devaluation, derived from the information we compiled during our missions to various CFA countries at the end of 1994. Finally, the paper concludes by evaluating the reform programmes as applied in Africa in general.

ECA Simple Devaluation-Simulation Model

The Model

During the annual meeting of the African Ministers of Finance that was held in Libreville, Gabon, from 1-2 March 1994, ECA experts presented a paper on 'Dynamic Simulation of the Macroeconomic Effects of the CFA Franc Devaluation', using a simple macroeconomic model. The model concentrates essentially on the effects of the CFA devaluation on the production, exports and imports of the Franc zone countries. It is composed of five equations as follows :

Production

(1) $\text{LogGDP} = a_{10} + a_{11}\ \text{logIF} + \log a_{12} \log CG + a_{13} \log YD + a_{14} \log X + a_{15} \log M = a_{16} \log \text{GDP}_{-1}$

Investment

(2) $LogIF = a_{20} + a_{21} logGDP_{-1} + a_{22} logF$

Exports

(3) $LogX = a_{30} + a_{31} logY_{OECD} + a_{32} logX_{-1} + a_{33} log\left(\frac{PM}{P}\right)$

Imports

(4) $LogM = a_{40} + a_{41} logF + a_{42} logX_{-1} + a_{43} log\left(\frac{PM}{P}\right)$

Prices

(5) $\text{LogP} = a_{50} + a_{51} logGDP_{-1} + a_{52} logCG + a_{53} logPM + a_{54}\ logM2$

Where:

GDP	=	Gross domestic product; a_{110}; a_{120}; a_{130}; a_{140}; a_{150}; a_{160}
IF	=	Fixed domestic investment; a_{210}; a_{220}
X	=	Exports of goods and services; a_{310}; a_{320}; a_{330}
M	=	Imports of goods and services; a_{410}; a_{43}
Y_{OECD}	=	Combined GNP of developed market economies of OECD
YD	=	Disposable income
F	=	External capital flows and export earnings
CG	=	Government expenditures or consumption
$M2$	=	Money plus quasi-money or credits to the economy
PM	=	Import prices
P	=	GDP deflator; a_{510}; a_{520}; a_{530}; a_{540}
$\frac{PM}{P}$	=	Index of national products competitiveness.

The model parameters are estimated simultaneously using two stages least squares method (2SLS). The data sample include the annual observations for the period 1971-1990.[1]

The model was supplemented by the so-called 'elasticity theorem' to determine the impact of devaluation on the balance of payments. Starting from the trade balance:

(6) $TB = X - tM$

1 The sample includes ten countries, namely Benin, Burkina Faso, Cameroon, Congo, Côte d'Ivoire, Mali, Niger, the Central African Republic, Senegal and Togo. The data used are drawn from the World Bank *World Tables, 1992*: IMF *International Financial Statistics, 1992*; and UN-ECA *Statistical Yearbook* various issues.

Where:

TB	=	Trade balance
X	=	Value of exports in local currency
t.M	=	Value of imports in local currency
t	=	Exchange rate
Xe	=	Price elasticity of exports
Xi	=	Price elasticity of imports

Taking the derivative gives:

$$dTB = Xe.Xdt/t + Xi\,M.dt - Mdt$$

or

$$\textbf{(7)} \quad \frac{dTB}{M} = Xe.Xdt/M + Xi\,dt - dt$$

From the equality (7), we can have:

$$dTB = dX - t.\,dM - M.dt$$

or

$$\textbf{(8)} \quad DX = Xe \times dt/t \text{ and } t.dM = Xi.Mdt$$

Assuming that there is equilibrium in the trade balance from the beginning (that is $TB = 0$ and thus $X/t.M = 1$), the equation (8) can be read:

$$\textbf{(9)} \quad \frac{dTB}{M} = dt.\,(Xe + Xi - 1)$$

In the case of devaluations (i.e. $dt0$) in order that dTB be positive, the sum of the two elasticities must be superior to 1.

The Results

The results of the estimation of the model is as follows :

Table 1 : Estimation Results of the Model (Using two least square method)

	Parameters	Estimations	Standard Error	t. Statistic
Equation (1)	a_{10}	0.880	0.013	67.7
R = 0.93	a_{11}	-0.033	0.181	0.2
	a_{12}	0.203	0.075	2.7
	a_{13}	0.345	0.082	4.2
	a_{14}	0.185	0.082	1.5
	a_{15}	-0.018	0.265	-6.8
	a_{16}	0.514	0.105	4.9
Equation (2)	a_{20}	25.500	0.060	425.0
R = 0.57	a_{21}	-0.184	0.304	-0.6
	a_{22}	0.276	0.089	3.1
Equation (3)	a_{30}	11.880	0.060	198.0
R = 0.95	a_{31}	0.671	0.206	3.3
	a_{32}	0.478	0.153	3.1
	a_{33}	0.376	0.146	2.8
Equation (4)	a_{40}	16.450	0.079	208.2
R = 0.89	a_{41}	0.184	0.035	5.3
	a_{42}	0.260	0.127	2.0
	a_{43}	0.023	0.173	-0.1
Equation (5)	a_{50}	-27.000	0.013	-20.8
R = 0.90	a_{51}	0.714	0.058	12.3
	a_{52}	0.143	0.056	2.6
	a_{53}	0.172	0.025	6.9
	a_{54}	0.183	0.021	6.3

Source: World Bank, IMF and UN-ECA, 1994.

a) Conditions of Elasticities

One can observe from Table 1 above that almost all parameter coefficients of the model are significant and have the expected signs. Looking at the external import prices as compared to the local prices (*PM/P*) causes a rise of 0.376 per cent in exports and a decline of 0.023 per cent in imports (although the latter is not statistically significant). The sum of elasticities of TWO variables (0.353) is far from meeting the Marshal-Learner conditions of over 1 so that the trade balance be improved through devaluation. It seems that imports in the CFA zone are more or less insensitive to changes in relative prices.

On the other hand, the increase in exports due to rise of 1 per cent in relative prices (*PM/P*) is approximately 0.38 per cent (parameter a_{33}), which is insufficient to compensate for the loss in the unit price (Mengisteab 1991). This confirms the fact that the conditions of elasticity sensitivity are not, in general, met for certain agricultural products such as coffee, cacao, groundnut, cotton, etc., which constitute the major export products of the CFA zone member states. Therefore, these results do not justify the expectation of the CFA zone countries of correcting the external deficits of balance of payments through devaluation of the CFA franc. Of course, these overall results need to be tested at the individual country levels where the situation may be different.

b) Effects of 50 per cent Devaluation on Nominal Exchange Rate of FCFA/FF

The results of Table 1 were simulated for a period of six years to project the effects of devaluation on production, investments, exports and prices. A devaluation of 50 per cent of F CFA is equivalent to a rise in external prices (PM expressed in F CFA) by 100 per cent (doubling prices). In theory, local prices (*P*) can remain unchanged if the governments concerned take a vigorous measure to freeze upward price movements. But this measure is difficult to implement, so that, in practice, devaluations are accompanied by a sudden rise in local prices. For example, in Mali, just after devaluation, local prices rose to 30 per cent and up to 100 per cent for some products.

Therefore, in order to appreciate the effects of FCFA devaluation, one should compare the two situations: effects without devaluation and effects with devaluation, other things being held constant. Table 2 gives the simulation results in the absence of devaluation as the last six-year trend projections for the coming six years.

Table 2: Annual Percentage Changes of Economic Variables in the Absence of Devaluation

Economic Variable	t=0 1993	1 1994	2 1995	3 1996	4 1997	5 1998	6 1999
GDP	0.6	1.40	1.25	1.37	1.44	1.52	1.54
Fixed Investment (IF)	0.11	4.86	4.78	4.74	4.72	4.71	4.64
Exports (X)	0.27	0.84	0.97	1.03	1.60	1.31	1.90
Imports (M)	0.15	0.25	0.31	0.35	0.45	0.52	0.6
Prices (P)	0.46	0.74	1.02	1.17	1.45	1.31	1.60

Source: UN-ECA, 1994.

The simulation of the effect of devaluation and the accompanying measures was made on the basis of the following assumptions (or hypotheses):

H1 - a devaluation of 50 per cent with freezing of local prices during the first year, other things being equal;

H2 - a devaluation of 50 per cent, with a rise of 50 per cent in local prices during the first year, a persistent rise in government expenditures of 5 per cent per year and an increase in external capital flows by 30 per cent during the first year and, thereafter, by 18 per cent each year;

H3 - same assumptions as H2, but here it is assumed, in addition, that (i) an active policy to control inflation has been put in place, which after devaluation can allow to maintain the ratio *PM/P* constant and (ii) a permanent rise in external capital flow by 30 per cent per year during the six-year projection period.

The results of such simulations are reported in Table 3 as follows.[2]

2 Actually, the ECA paper puts these results in the form of graphs. We are translating the graphs in figures in order to compare them with those of Table 2.

Table 3: Simulation of FCFA Devaluation (annual percentage changes)

Economic variables under alternative hypothesis	0 1993	1 1994	2 1995	3 1996	4 1997	5 1998	6 1999	7 2000
GDP								
H1	0	7.8	8.3	6.5	5.0	3.8	2.9	2.2
H2	0	3.5	3.8	3.1	2.6	2.4	2.2	1.8
H3	0	3.5	3.5	4.2	4.1	3.8	3.7	3.5
Fixed Investment (IF)								
H1	5.0	3.5	3.6	3.8	4.0	4.2	4.5	4.7
H2	8.4	4.3	4.3	4.4	4.5	4.6	4.7	4.8
H3	8.4	7.6	7.5	7.5	7.6	7.7	7.7	7.8
Exports (X)								
H1	0	39.7	20.0	10.0	5.0	2.5	2.4	2.0
H2	0	14.3	7.8	4.1	2.2	2.1	2.0	1.2
H3	0	14.3	8.5	6.4	5.6	5.0	4.6	4.5
Imports (X)								
H1	-0.1	-0.3	10.0	5.0	2.8	1.7	1.0	0.8
H2	-0.3	-0.7	3.8	2.0	1.2	0.6	0.5	0.4
H3	-0.3	-0.7	3.7	2.4	1.7	1.4	1.3	1.2
Prices (P)								
H1	0.8	18.0	4.8	5.0	3.8	2.0	1.0	0.8
H2	2.8	18.2	2.8	3.9	3.8	3.7	3.6	3.6
H3	2.8	18.2	3.0	3.0	2.7	2.1	2.0	1.9

Source: UN-ECA, 1994.

c) The Effects on GDP

Comparison of the simulation results of Table 3 with those of Table 2 shows that the devaluation will allow an output expansion in short run (first year-1994) of 7.8 per cent for the hypothesis 1. Thereafter, there will be a deceleration to reach 2.2 per cent in the 7th year (2000); whereas, without devaluation, GDP growth will range between 0.6 per cent in the first year simulation (1994) to 1.5 per cent

in the long run (7th year-2000)). This will be due to the fact that, with 50 per cent devaluation of F CFA combined with increase by 39.7 per cent in short run and this boosts GDP growth to 7.8 per cent. The GDP growth slow down in the long run will be due to high rises in the rates of inflation after their first year freeze, with the consequence of loss in export markets, increased external payments deficit and reduction of available resources for investment and production.

In the long run, the scenario H3 seems to be more favourable growth of output and investment. In this context, through the price control that renders local products more competitive, and the increased mobilisation of external resources, a rise in exports and investment will sustain the growth in output (GDP) to reach 3.5 per cent in the long-run against 2.2 per cent for the scenario H1 and 1.8 per cent for the scenario H2.

However, the results of the scenario H2 which is perhaps the most realistic of the three, are less favourable for the output growth in both short and long run. The sudden rise in local prices (by 50 per cent) will, in short run, reduce the beneficial effect of the devaluation on the competitiveness of export products of the countries concerned, so that, at the end, a rise in local prices $(\frac{\Delta PM}{\Delta P} = 1)$ equivalent to the rise in foreign prices will nullify the effects of devaluation on GDP. In this case, the simulation results obtained are almost the same as those of the historical trend scenario of Table 2; that is, a GDP growth of approximately 1.5-1.8 per cent in the long run.

d) Effects on Trade Balance

As far as external trade is concerned, one can observe that, in the balance of devaluation, the growth in exports of goods and services in the first year of simulation represented about six times that of imports (0.57 per cent of DX against 0.097 per cent for DM), but throughout the period this changed from 1.9 per cent against 0.6 per cent at the end of the 6th year. In other words, the local products become less and less competitive and the imports cheaper. As a result, the trade balance deteriorates in the F CFA zone.

However, the results obtained after the simulation of devaluation and the accompanying measures did not improve the balance of payment equilibrium. Taking the results of the realistic hypothesis H2, one can see that the impact of 50 per cent devaluation of F CFA on the exports of goods and services was about 14.3 per cent in the first year and, thereafter, the rate of growth slowed down to reach 2.0 per cent at the end of the 6th year against 1.9 per cent in the

absence of devaluation. This is due to the fact devaluation causes a rise in the import prices which is reflected in the domestic prices.

Model Policy Implications

The above results lead the ECA paper to conclude that :

(i) There is need to put in place a mechanism for monitoring the differential rates of inflation by stabilising production costs and national spending. Since the structural transformation of the economy is the major objective of the majority of the African countries, this can be done through selective credit policy which gives priority to financing the agricultural and industrial sectors. As long as these sectors have low productivity compared to that of speculative and trade sectors, a total financial liberalisation will compound the realisation of that objective since it will raise the nominal rate of interest at the level that discourages the initiatives of the small modern operators (particularly in the rural and informal sector) to save.

(ii) Relaxing the financial constraints through the consolidation of long-term external debt with very low interest rates or its cancelling should be taken as accompanying measures of the exchange rate policy. The resource here hence released should be directed toward the productive sectors of the economy.

(iii) Actions should be taken to increase the competitiveness of national products on the international market through an adequate trade strategy which would aim at : (a) imposing its prices and its products; (b) finding partners; and (c) increasing the capacity of adaptation to the changing international conditions. This can be done through diversification of production and the increased productivity of each domestic product.

Preliminary Country Results

Prior to Structural Adjustment Programmes (SAPs), African governments did not consider exchange rate adjustment as a major policy instrument. Many governments believed that a devaluation would increase inflation, aggravate budget deficits and yield minimal benefit in relation to increased exports and lower imports. Thus, between the 1970s and early 1980s, most of African economies suffered from over-valuation of the currency which may have resulted in loss of export competitiveness and encouraged a high level of imports especially in the form of luxury goods and unproductive inputs.

There was disparity in terms of currency and the type of exchange rate regime used in the African context. Some countries (CFA franc zone) have a fixed exchange rate and a convertible currency, whereas most African countries have a floating exchange rate regime and their currencies are not convertible either for

capital or current account transactions. It was therefore necessary for governments to assess the advantages and disadvantages of fixed and flexible exchange rates relative to policy pronouncements and implementation. In the case of a devaluation, under a fixed rate regime, the magnitude of the change is subject to policy decisions (fiscal or monetary) whereas for flexible rate regime, the movement of par value will mostly depend on the removal of restrictions on the foreign exchange market. In terms of structural adjustment, countries with fixed rates regime rely almost entirely on tight money policy which is evidenced through high interest rates and low levels of seigniorage. The flexible rate regime however, provides economies with the choice of depreciation.

The devaluation of the CFA franc by 50 per cent brought into focus the role of these two regimes in determining the policy mix relative to economic stability, inadequate and distorted financial markets, unproductive state intrusion, inward-oriented trade policies and correcting macroeconomic disequilibrium. The 13 West and Central African states along with the Comoros using the CFA franc had benefited from a long period of low inflation and sustained economic growth. It was not until the 1980s that the imbalance began to emerge as a result of the appreciation of the French franc against the currencies of the zone's major trading partners and worsening of terms of trade in the zone by 45 per cent in 1985 owing mainly to the fall in world market prices for its major exports (cacao, coffee, cotton and petroleum in particular), and to increase in import prices. These scenarios weakened the external competitiveness of countries in the zone, at the same time they were hamstrung by other structural and sectoral problems, particularly relative high wages.

Since the mid-1980s, GDP growth in the zone had been generally low or negative and investment ratios had been declining. Except in Gabon there were chronic current problems and per capita income was falling and financing gaps widening. The governments' financial situation was deteriorating due to a shrinking tax base as a result of declining competitiveness of the export and import substitution sectors. The usage of internal adjustment strategy alone was not enough to correct these serious distortions that had developed. This strategy would have resulted in increased taxes and cuts in priority current and capital public expenditures, particularly on education, health and infrastructure, which would eclipse the basis for sustained growth. But the devaluation came as a surprise and most of the CFA countries were not prepared to anticipate the devaluation so as to introduce complementary measures specifically geared towards mitigating its negative impact.

The focus after the devaluation was then on how have the governments of the CFA countries responded with policies for the short run, medium term and long

run. For the short term, the provision of standby arrangements with the IMF and France writing off debts (mostly Official Development Assistance, ODA) of these countries would provide some cushion. Most of these countries have implemented controls and protective schemes that would mitigate the most immediate impact of the devaluation, especially on the most vulnerable groups. The IMF has assisted in formulating comprehensive adjustment programmes. The Enhanced Structural Adjustment Facility (ESAF) has been provided with US$ 1.6 billion, of which US$ 555 million would have been available in 1994 for these zone countries; at the same time the World Bank had earmarked US$ 1.5 billion in support of adjustment programmes. France has also established a special fund, FF 300 million to finance social projects in those countries mostly affected by the devaluation. The fund was to be used for the purpose of essential drugs, basic equipments and public works.

For the medium-term, almost all of the immediate funding that were made available would have been used up and governments that have not developed some real policies would be groping in economic as well as political darkness. For countries like Chad, Niger, Burkina Faso, Mali and Central African Republic where the absence of food production industries is obvious, the road ahead is tumultuous. In the case of Benin and Togo, they will continue to benefit from the vast market of Nigeria and the impact will be diminished somewhat by the continued convertibility of the CFA franc and the fall of the Naira.

Preliminary results show that the CFA zone area has performed better than expected in the short run both in the export and domestic sectors with an upsurge in the import substitute sector. Even inflation which would have hampered any gains has been controlled, averaging 25-30 per cent.[3] Devaluation has allowed franc zone countries to return to competitive and profitable exporting. Countries like Burkina Faso, Côte d'Ivoire and Togo have experienced marked increase in output of primary commodities (coffee, cotton, cocoa) as well as an increase in producer prices. Senegal's tourist industry is showing an upturn. Intra-zone trade is also flourishing. In competition with subsidised meat exports from the European Union, meat exports have begun to increase. Before the devaluation, only 20 per cent of Côte d'Ivoire's imported meat came from West Africa but now 80 per cent does. Central African Republic, Chad and Cameroon have boosted livestock sales to Gabon. Senegal has increased its fish exports.

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3 Although this is still high compared to the pre-devaluation period where inflation rates ranged between 5-10 per cent.

On the negative side, the transition has been a bit more tumultuous for others. Countries like Cameroon and Chad have not, and there is little optimism, that they can draw any significant advantage from new competitiveness in agriculture and other primary exports. Also, there will be a sizeable shortfall in anticipated revenue for these countries, as well as the slowing down of the administrative and structural reforms that were underway. On the other hand, there has been tremendous growth in world demand and increase in prices for groundnut and cotton. For Senegal, this portends a problem, in that cotton prices have risen about 37 per cent higher than groundnut's such that farmers are now threatening to substitute groundnuts for cotton in their next planting season. This will, in the medium to long term seriously hurt the groundnut sector of the country. Thus, to reap the full benefit of the devaluation, while these countries in the short run will be buttressed by provisions explicitly cited earlier, they would have to conceive and implement, for the middle term and long run fiscal adjustment programmes, relevant monetary policies, wage and price policies and speed up structural reforms.

For the CFA franc zone, the impact of devaluation in the long-term is still shrouded in uncertainties and the policy recommendations, as well as programmes that are developed and executed therefrom will have an effect on these zone countries. For the impact of devaluation to be felt by the poorest farmers, some degree of redistribution policies and public investment should be provided such that the benefits of devaluation do not accrue only to the big trading companies. Along side devaluation is the need for a comprehensive debt strategy so that the political strains of devaluation may not undermine the fragility of emerging democracies in these affected zone countries.

There has been concern as to how the devaluation would impact on government budgets, inflation, productive (manufacturing) sector and imports. Relative to inflation, devaluation, may present a vicious cycle (increase in domestic prices through domestic cost inflation) but this may not be prolonged. Much depends on the package of appropriate fiscal, monetary, wage and price policies along with the exchange rate policy. On government budget, devaluation may immediately raise government receipts through taxes and higher income from exports, increase capital inflows through loans and grants, and subsequently enhance the financial position of parastatals in the export sector, thereby reducing the need for government loans or subsidies. Hence, the notion that devaluation will exacerbate government budgetary problem may not be totally valid. Although devaluation will trigger some offsetting repercussions, the net outcome will depend on the country's specific situation.

In terms of production levels relative to devaluation, there is a pervasive notion of 'elasticity pessimism' production is not price elastic. The counter argument is that although there are structural rigidities, this pessimism should not be so ingrained. The assumption is that most African economies are operating below full capacity because of lack of producer incentive and difficulty in obtaining imported production inputs. Therefore, a devaluation along with an increase in 'quick disbursing' external aid to purchase imported intermediate goods can pay-off in the short-run. Devaluation along with raising incentives and incomes of farmers will help assure market for the additional production of manufactured goods. The conclusion is that production response to real devaluation cannot be generalised because the situation is diverse and the outcome will differ from case to case.

Evaluation of Stabilisation and Structural Adjustment Policies in Africa

Since the CFA devaluation is one component of the overall structural adjustment package, it is worth assessing the impact of that package in Africa in order to understand the likely magnitude that devaluation may impede on the CFA zone countries' economies in general as compared to other African economies. There is a link between the devaluation and the design and implementation of structural adjustment programmes in terms of their objectives of short-term stabilisation and the medium-term expansion of supply.

In general, most African countries, and especially sub-Saharan Africa, started the 1980s with an enormous macroeconomic disequilibrium which was the result of imbalance between aggregate demand and aggregate supply. This disequilibrium occurred as a result of stagnation in the global economy, debt crisis of African countries, collapse of commodity prices and failure of the African economies to adjust promptly to economic shocks. This was reflected in balance of payments deficits, rising prices, increasing foreign debt, declining growth rates and loss of international competition.

Because of these volatile economic conditions, African countries have continued to demand the International Monetary Fund (IMF) and the World Bank (IBRD) resources along with other multilateral and bilateral assistance. This demand has prompted these institutions along with the respective governments, to design and implement Structural Adjustment Programmes (SAPs); now more than a decade old having begun in 1980, to re-establish economic equilibrium and eventually through development policies move toward sustainable development. The inception of SAPs was based erroneously on the fundamental premise that domestic factors were essentially the causes of Africa's economic malaise. However, more recent assessments of SAPs purport that this

was only a contributing factor. It has also been observed that even 'successes' attained as a result of programme implementation have been too modest and minimal (World Bank 1993). SAPs also underemployed human skills, technological capabilities and industrial policies.

These SAPs have focused (with supposedly specifics differing from country to country) on: (i) expenditure reducing policies, (ii) expenditure and product switching policies, and (iii) supply side growth oriented policies. The measures undertaken within these policy stipulations include resource mobilisation, productive allocation and utilisation of resources, liberalisation of trade and investment reforms.

The goal is to see that these policy designs impact positively on macroeconomic structures, *inter alia*, rate of growth of real output, ratio of inflation rate to GDP, ratio of current account balance to GDP and ratio of domestic investment to GDP. The policy instruments and stabilisation measures that have been used include: (a) real devaluation of domestic currency, (b) reduction in government expenditure and increase in taxes, and (c) reduction in growth rate of domestic credit and increase in real interest rate.

In a World Bank study (June 1993), essentially using a 'before/after' approach, out of 29 sub-Saharan Africa (SSA) 'adjusting' countries, 14 had an improvement in GDP growth whereas 14 showed a decline between the period 1987-1991 (World Bank 1993). This concurs with other individual studies which have shown that the result of the policy instruments on macroeconomic indicators are inconclusive. The World Bank study further confirms that in almost all cases, rates of growth, investment and savings were not at levels required for sustainability of development. According to the report, among the possible reasons for this dismal showing, the authors concluded that 'policy reforms effort has been uneven and insufficient'. This is evidence that the onus of the success of the SAPs lies with the respective governments. In the interim, the idea of 'home-grown programmes' has been more pronounced. The thrust here is to make those upon whom SAPs impact more vehemently become part of the conceptualisation, design and implementation of adjustment policies.

Almost all of CFA countries undertook some structural adjustments after devaluation. The programme for Equatorial Guinea aims at accelerating the rate of economic growth, reducing the rate of inflation and improving the overall balance of payments with a view to eliminating the need for accelerated financing by 1996. To achieve their objectives, the authorities intend to strengthen macroeconomic and structural adjustment policies, through tightening financial and incomes policies and deepening reforms in agriculture, public administration, public enterprises and the financial sector. In line with these

medium-term objectives, the programme for 1994 seeks to increase the rate of real economic growth, contain inflation at 35 per cent and reduce the external current account deficit.

Niger, which had some problems with the Bretton Woods institutions and blamed SAPs for its 'economic melt-down' in 1983 after the uranium boom, implemented a new package. The focus is on adjusting prices, taxes and salaries. The main goals are to reduce costs in improving the uranium sector, liberalise the labour market and simplify the custom tariffs which would encourage more and better movement of tradable goods. In Gabon, the reforms focused on diversification away from oil, restraining public spending and reforming public enterprises. The goal is to see budget surplus rising from 4.3 per cent of non-oil GDP in 1994 to 14.1 per cent in 1995 and 14.4 per cent in 1996 when a balanced budget is envisaged. In Côte d'Ivoire, the structural reforms include promoting flexibility in labour markets and strengthening domestic competition, reforming the public sector including an accelerated privatisation programme and eliminating obstacles to free trade. But as the programme was implemented, there was a desire to increase social safety net measures, provide a labour-intensive approach to public works projects and provide temporary price subsidies on essentials for the poor.

The Central African Republic's major thrust after the devaluation is to liberalise the agriculture markets by removing all price stabilisation and subsidy systems. This is to encourage farmers to be more flexible to market forces (demand and prices) and to develop a more diverse range of crops. The core element is the rebuilding of the public finances through increasing revenue. This will be done through strengthening the tax administration and introducing new revenue measures. The programme is important because it binds the government to some fiscal responsibilities and could be a catalyst for resource flows from other sources.

Congo, which has had continuous disagreements with donors, instituted a post-devaluation programme. The main elements are to accelerate the privatisation efforts, phase out subsidies and institute concrete policy measures which will focus not on export competitiveness like other CFA countries but deficit reduction of 13 per cent of GDP in 1994 toward a surplus of 3 per cent in 1996. Other components include customs reforms, changes in investment code, banking reforms and administrative decentralisation. The method of implementation would be through a labour-intensive infrastructure investment approach. This agreement with IMF will provide avenues for other aids, especially with the World Bank which had suspended cooperation with Congo

because of arrears on loan repayments. France has since provided a bridging loan to pay off these arrears.

Burkina Faso, Senegal, Cameroon, Niger and Benin also instituted structural programmes after the devaluation. The focus was on securing those competitive gains from the devaluation to propel sustainable growth with low inflation and controllable balance of payments. Some elements include: targeting real GDP growth of at least 5 per cent, reducing current account deficits, reducing consumer price inflation and using additional funding to buttress the social sector and rebuilding the productive sectors.

The reforms initiated may not get the desired results because: (i) reform agreed on may not be fully implemented and (ii) reform started may later be reserved. This was seen in the case of Guinea which had instituted SAPs since 1986. Problems developed with the IMF and other donors because Guinea was not meeting the real reform standards and the release of funding was halted in 1993. A 'thawing' of relationships ensued in 1994 when a new Enhanced Structural Adjustment Facility (ESAF) agreement was signed as well as the release of the backlog of development funding. There was another situation in Uganda where loans initially approved had remained undrawn because of World Bank's uneasiness with project irregularities.

It is also evident that satisfaction with core elements of the SAPs by the Bretton Woods institutions produces credibility with other donors. This was evident in Ghana where structural adjustment lending and external financial support provided the basis for a significant direct increase in funding for various levels of the society. This is also seen in 1994 in Zimbabwe where its economic reform programme has got IMF and IBRD's support, thus, becoming a priority country for the US Government. This was also the case with the Central African Republic, Congo and Uganda in 1994.

Even though the results of SAPs have not been encouraging, many African countries still undertook some form of economic reform during 1994. Let us examine how the African countries in general and the CFA zone in particular responded in the specific areas of reforms.

Deregulation of Markets and Liberalisation of Prices

One of the conditions for the success of the devaluation is the monitoring of the price movements so as to prevent them from getting out of control. One major component of African countries' Structural Adjustment Programmes (SAPs) has been the *deregulation of markets and the liberalisation of prices*. Prior to SAPs, most of these countries had stringent price and other controls on consumer goods and services. Presumably, these controls were intended not to be set arbitrarily or

hypothetically, but seemingly at a level where an adequate margin of profits would accrue to the producer and not so high that the bulk of consumers would not be able to afford it. But at times, when prices were set at below market prices, excess demand was created and this reinforced the parallel market.

With the advent of SAPs, sweeping decontrol measures were put into effect. The devaluation of the CFA franc in January 1994, however, may have stalled or reversed these measures in order to institute some mitigating steps relative to the devaluation. Ordinarily, the decontrol measures would entail liberalising prices such that the supply and demand mechanism would determine market price. Being that equilibrium price is purely conceptual, policy makers have at times taken a more gradual approach to decontrol.

Deregulation and the liberalisation of markets have exhibited mixed results in African countries undertaking reforms. Despite this situation, countries continue to make them part of their macroeconomic objectives. Immediately after the devaluation, the CFA zone governments have introduced reform measures including, *inter alia*, reintroduction of price controls for a range of products regarded as essentials or as having a decisive effect on the price index; lowering of customs tariffs in certain cases in order to reduce the additional costs of inputs and imported products classified as basic necessities; stabilisation of or limited increases in utility costs; stabilisation or limited increases in wages; and reductions, in certain cases, in direct and indirect domestic tax rates.[4]

The situation is reflective in Cameroon where, since 1989 there has been a gradual phasing out of the system of government regulating price changes on many goods and services. But certain categories of goods, utilities and services had been excluded from these decontrol measures. The first group included consumer necessities (basic food supplies, utilities, housing rent), the second group included prices of energy and fuel, and the third group comprised agricultural input and supplies which were basically subsidies for the sector.

In a World Bank study of 29 'adjusting' countries, prior to SAPs (during the 1970s and early 1980s), 26 countries had extensive price controls on 26 or more goods. Two countries (The Gambia and Malawi) had moderate controls on 10 to 25 goods. Only Chad of the 29 countries had controls on fewer than 10 goods. In 1993, with these identical countries implementing some form of SAP, only Mozambique and Burkina Faso had extensive price controls. Five countries had

4 UNIDO Secretariat, Summary Report of 'Subregional Workshop on the Impact of the Devaluation of the CFA Franc on the Manufacturing Sector of the Countries of the West African Economic and Monetary Union', Bamako, Mali, June 1994, p.4.

moderate controls, 13 had few controls, whereas in 9 countries, including Zambia, Uganda, Ghana and the Gambia, there were no controls.

The devaluation, as stated earlier forestalled some of the decontrol measures and some countries had to revert to price control, once again, at least to stem some of the potential negative effects of the devaluation in the short run. In Benin, there was a failed attempt to institute controls because of the lack of experience in imposing or policing price controls. This problem exists because there is no centralised enforcement agency and also the populace is accustomed to buying mostly imported foodstuff, medicaments and other essential consumer goods. Countries instituting new levels of price control included Chad, Gabon, Central African Republic, Togo and Burkina Faso.

In Gabon, price controls were placed on bread, flour and other essentials, as well as public utility tariffs, which include telephone, water, electricity and internal transport. In Central African Republic, there was a freeze on all prices of goods and services which led to hoarding due to inflationary expectations. Although inflation is expected to rise in all zone countries, the rate in the Central African Republic was expected to average 35 per cent above the rate in other countries. This is due to the country's limited manufacturing base and the need to import finished products. The goal is to bring inflation rate to 3 per cent in 1995 and keep it under 2 per cent. This may be possible if the zone's record of tight monetary policy and low inflation remains intact. In Burkina Faso, basic item costs were frozen and price rises between 24 and 39 per cent were allowed for other items. In Togo, all petroleum prices were frozen.

In some countries, to accommodate the devaluation, emphasis was also placed on the supply side to ease the transfer of cost to the consumers. This included reduction or elimination of duties and reprisals for disobeying price controls. This process was carried out in Togo where duties on salt and pharmaceuticals were eliminated and duties on school books, pencils, chalks and others were halved. Burkina Faso reduced custom duties on essentials (rice, sugar, milk, flour). The authorities were also commencing reprisals against those disobeying price controls. These included closure of business and/or fines.

Although the CFA zone devaluation was the most prominent in terms of exchange rate policy, other African economies pursued some of their own. In Algeria, along with its economic stabilisation programme, the dinar was also devalued to make non-oil exports more price-competitive. In the short run, this will raise the dinar value of hydrocarbon taxes and other government income. The goal here is to substantially reduce the government budget deficit. In the case of Algeria, the policy focused in 1994 on deregulation and market liberalisation because of the transformation from a state-managed system into a

market-oriented economy. The objectives include reducing the budget deficit, containing inflation, generating growth in the economy to create jobs, restructuring public enterprises and promoting private sector activity.

The immediate policy instruments used were to devalue the dinar by 40 per cent, increase interest rate and impose some credit controls. The reform also required a reduction in the subsidies on basic goods and price increases in the products of state companies. But the government has decided to move cautiously given the political ramifications of any decline in standard of living. Some basic targets include GNP growth of 3 per cent in 1994 and 6 per cent in 1995. This may be possible if the present problems in Nigeria persist because the exports level of hydrocarbons from Algeria may rise resulting in increased earnings. It is envisaged that prices will rise due to the devaluation of the dinar by 40 per cent, the reduction of subsidies on basic goods and movement of products from state companies to market levels. This means that prices for nine food items, including bread, flour, milk and domestic fuel prices will increase.

In Egypt, as part of their economic package, there was a reduction in subsidies, increase in direct taxation and continued price deregulation. These measures, when implemented will lead to price increases but not at the full impact of the measures. This is because inflation would be moderated by fiscal and monetary discipline, stable exchange rate, limited wage increases and lowering of tariff rates. Policy makers are estimating the inflation rate to stabilise between 3-5 per cent by the end of 1995. Egypt has embarked upon a policy initiative of maintaining exchange rate stability a priority. The goal here by the Central Bank is to keep investor's confidence high and maintain continuous high capital inflows. Although the Egyptian pound has been stable since the free market rate in 1991, there are concerns that it is overvalued and hinder exports. The government is following a gradual implementation of its programme because of the fear of unrest prompted by economic hardship and austerity. This pace created some friction with the World Bank which led to the delaying of a US$ 4 billion debt write-off.

Morocco's thrust is to develop a market-oriented economy which will attract foreign capital to finance growth and development. The policy elements included tight control on inflation, encouraging investment and generating growth to enhance employment. The government planned to coordinate taxes on various financial mechanisms and to develop the securities and foreign exchange market.

In the absence of controls, consumer prices have continued to increase while stifling economic growth. The major contributing factors include currency devaluation, growth in money supply and removal of subsidies on food staples and other necessities. This was the situation in Nigeria where the removal of fuel

subsidy along with the level of stockpiling or hoarding in anticipation of some social and political unrest prevented any hope of inflation abating.

In Ghana, where the government was anticipating a rate of 15 per cent for 1994, the fear of further increase in ethnic fighting in the North did not materialise. The reason is that much of the food consumed by the populace comes from this region. In Uganda, inflation had ebbed in 1993 showing negative year-on-year rates for 4 out of 12 months. The rise in the rates in March was due to 18.2 per cent increase in food prices. The inflationary history has impelled the government to take firm control by continuing to impose strict monetary growth.

In Madagascar, the main focus was on imports, where 150 non-strategic imports were recommended to be prohibited from being imported. This included private cars, television, washing machines, tobacco and whisky. The concern here is that this will cause reduction in a major source of income and may propagate inefficiency within the domestic enterprises due to the apparent loss of competition from imports. Other measures included the decontrol of the franc, end to restrictions on the use of foreign exchange by exporters, tax reforms to help budget deficit and the restructuring of state-owned banks.

In Mozambique, a loan was approved under the ESAF to support economic reform through 1995. There has been progress despite 16 years of conflicts and the transformation from a centrally planned to a market-oriented economy. The government's medium-term strategy is to overcome widespread poverty and provide a basis for economic growth. Targets include an average annual GDP growth of 6 per cent, a steady reduction of inflation, a reduction in external current account deficit relative to GDP and a recovery in exports through improved and expanded incentives. By the end of 1994, some partially administered price controls had been lifted, reform of the public enterprises and financial sector had progressed significantly and privatisation of large parastatals had been accelerated.

Despite previous concerns about the tremendous social costs of SAPs, and on the heels of exchange rate reforms, Angola adopted a programme in February 1994. The embodiment of the programme was to correct the extreme imbalances which had resulted during the shift from a controlled to a market-oriented economy. The main measures were to reduce budget deficit, bring money creation under economic liberalisation, initiate price reforms and enhance the privatisation process. The goal is to reduce budget deficit to 4 per cent of GDP (from 29 per cent in 1993), reduce money supply from 635 per cent in 1993 to 112 per cent in 1994 and reduce price inflation from 1,838 per cent in December 1993 to 260 per cent in 1994. It is noted that the entire reform process and its

fruition is incumbent upon the cessation of hostilities and the revival of the depressed oil sector.

Zambia showed some resilience from the corruption allegations and benefited from the good graces of donors. The SAP programme was continued also because of improvements in the privatisation process, reduction in the average rate of inflation, and increased budgetary allocation to the social sectors, which was up 150 per cent in 1993.

In Zimbabwe, the Zimbabwean dollar was devalued by 17 per cent in January. By the third quarter, there had been an increase in the market rate *vis-à-vis* the official rate. This narrowing of the gap between the two rates eventually led to an early full convertibility of the Zimbabwean dollar. The IMF approved loans under the Enhanced Structural Adjustment Facility (ESAF) totalling US$ 144 million. This was in association with the reform programme that has made Zimbabwe to reach a total debt burden of Z$ 34.1 billion (US$ 4 billion).

It should be stressed that even with the introduction of price liberalisation there was not a spontaneous cut of subsidies. The curbing of subsidies has been slowed because most of the subsidies which are considered part of the 'social safety net' are targeted for the agricultural sector in the form of agricultural inputs and fertilisers.

The Areas of Fiscal Policy and Public Enterprise Reforms

Fiscal stabilisation measures included ensuring higher income from increased taxation, involving adjustments to the tax base, the simplification of tax law and effective tax collection. The difficulty in dealing with these measures was to distinguish between point-of-entry taxation, whose main objective is to protect domestic products, and Value Added Tax (VAT), whose main objective is to raise income. In general, for external trade taxation, governments opted for simplification and relaxation of tariff procedures; but for the inputs and capital goods, the tariff policy was adjusted so as to cushion the effects of the devaluation, with zero revenue duty for capital goods and reduced rate for inputs. For other goods and finished products, tax adjustments were meant to protect local production, to ensure the provision of essential items such as medicines, sugar, milk, rice, school supplies, etc., taxation policy measures adopted were, for example, gradual phasing out of the employer's flat-rate contribution; strict enforcement of the VAT mechanism so as to maintain its universal applicability; reduction of the rate of profit tax; harmonisation of the minimum-levy system.

For almost all African adjusting economies, the most difficult areas of reform have centred around *public enterprise reforms*. Reform of the public enterprises

was necessary because of their drag on financial sources, inefficiency and crowding out of the private sector in the commercial sector. But the reforms have been slow relative to the pace envisioned by the programmes. This slow pace has been attributed to the absence of data to corroborate reform taking place and the extent of privatisation. However, privatisation of public enterprises is still a priority but its implementation remains a problem. One reason could be that many nationals do not have the economic wherewithal to take responsibility of these parastatals since most governments want to take the 'indigenisation' route. Also, the government may be indecisive as to which enterprises it wants to retain, sell or establish some new form of ownership (e.g. partnership, joint venture). Most of the parastatals may be in such economically depressed state that there are no 'takers' and the government may be weighing the political and social ramifications of a complete shutdown.

Within the framework of SAPs, particularly with respect to the CFA zone, the expansion of supply was made through the fiscal policy rather than through the monetary policy; and it mainly concerned the expansion of the export sector production. Devaluation offered the opportunity to impart a stimulus to supply, for the change in parity that involves a 100-per-cent increase in the price of imports and hence protection from imported-products and an opportunity to increase exports which had become cheap for the foreigners. But this requires that the governments master the factor costs and that there is availability of long-term, stable and affordable financing.

The Areas of Monetary Policy and Financial Reforms

Another difficulty of SAPs relates to the *financial reforms*. The financial sector helps to mobilise savings, allocate financial resources and regulates the payment system. Therefore, it needs to be strong and especially in African least developed countries (LDCs), since it is needed to propel the movement toward sustained economic growth. The reforms have been hampered by an unstable macro-economic and political environment, reliance on financial systems that are inadequate, regulations that suppress private sector borrowers and the absence of the required manpower capacity to sustain a developing financial sector.

Specifically, one of the main policy instruments of adjustment has been currency devaluation. Concern of the overload of this instrument is rampant and that its anticipated impact may not be realised in the absence of other factors. Also its value as an instrument for correcting structural disequilibrium of the economy may be overstated. One example is that if devaluation is being used to increase exports, to sustain that level will entail enlarged export capacity. As empirical evidence do suggest, there is a correlation between exchange rate movement and growth in export volume, especially over the medium term.

However, this develops the 'adding-up problem', which produces a decrease in commodity price of a commodity due to simultaneous increase in supply from respective sources.

The financial issue concerns also the interest rate liberalisation and inflexibility in the monetary policy. So far structural adjustment reforms in the CFA countries were made on the fiscal side and the monetary policy was left out of the scene because CFA franc is closely tied with the French franc and the Banque de France which, together with member-states concerned, should authorise or provide the framework for expanding or reducing money supply in the CFA zone. Therefore, there was a little manoeuvre in the part of African governments to use this tool to finance development. Hence, the path towards a *financial deepening* of the economy has been slow in African countries, compared to other developing countries in Latin America and Asia. Most African bankers continue to play a conservative and traditional role of financing international trade rather than development. Only few countries have succeeded to increase the number of bank branches and other financial institutions to rural areas and to initiate the public at large to hold their wealth in the forms of financial assets.

The interest rate liberalisation policy which was advocated by the structural adjustment programmes, supposedly aiming at increasing the financial deepening, ended up having a high nominal interest rate and, in the absence of price controls (if prices are left to the free interplay of the market forces), this has resulted in a negative real interest rate, thereby discouraging private domestic savings. This is because financial liberalisation through increasing interest rate on deposits is stagflationary, unless portfolio switches take place, say from rentiers holding inflation hedge real assets (such as durable goods, hoarded money, housing, gold, diamond, or inventory stocks) towards productive loans to firms or enterprises (financial assets). This, generally, is not the case in most African countries.

Most of the African countries are, in effect, in the realm of the so-called 'technological dualism'; their economies being composed, on the one hand, by a relatively modern, technologically advanced sector which is identified by exchange market or monetised economy and in which coexist industry, mechanised plantation agriculture, mining, transport, finance, insurance, trading and associated services; and, on the other hand, there is the retarded, traditional sector with a subsistence economy and unorganised markets and in which peasant agriculture, handicrafts, very small-scale industry and their services constitute the principal activities of the economy (Thisen 1982).

Therefore, the SAP arguments to let the market forces determine the single real interest rate can only be applied in developed countries and in the newly industrialising economies of Latin America and Asia. In Africa, in general, the financial assets such as treasury bills, government bonds, prime industrial bonds, readily marketable shares which form the transition between money and real assets in countries with full financial systems play a minor role in the asset portfolios of wealth holders (Polak 1967:30). In contrast, the real or physical assets dominate in the assets portfolios of wealth holders in Africa. Consequently, the substitution effect, stemming from financial assets and operating through interest rate mechanism is smaller in African countries than in the developed countries.

Table 4: Asset Structures in African LDCs versus Advanced Countries

African Countries (LDCs)	Developed Countries
Money	**Money**
↕	- Treasury bill - Government bonds - Prime industrial bonds - Readily marketable shares etc.
Physical Capital	Physical Capital

Source: Compiled by the author

Thus, it would be misleading to assume, as in advanced countries, that in developing African countries with fragmented economies, unintegrated monetary system (formal and informal financial sectors) and imperfect money and capital markets, that there is one single real rate of return on the real and financial assets that represents the uniform opportunity cost of holding money. In those countries the demand for money and the demand for real physical assets tend to be complementary in the private asset portfolios rather than as competitive assets as Keynes and Neo-classical economists argue. As McKinnon (1973) argued, the complementarity factor can be represented by two interest rates: the average rate of the returns on physical capital and the rate of return on holding money adjusted with the expected rate of inflation (McKinnon 1973).

The single market interest rate determination ought to be done gradually until such time that the fragmented sectors of the economy are integrated and the economy is fully monetised. This is a long-term objective. But what is to be done in the transitionary stage? Will it be possible, for developmental purposes, to apply two sets of interest: one in the formally well advanced segments of the economy, to be left to the interplay of the market forces, and the other in the backward or less advanced, informal economy to be determined by administrative promotional measures? This would amount to the application of the so-called differential interest rate policy that the United Nations Economic Commission for Africa has proposed (UN-ECA 1991). In some African countries, for example Ethiopia, financial deepening is taking place more firmly through the extension of commercial bank branches in the rural areas than through the complete liberalisation of interest rates.

Another monetary issue is the fact that the capacity of the banking system and financial institutions to issue money to finance economic development without causing inflation is greater when income velocity of money is falling than when it is constant or rising. This is explained by the fact that when velocity of money declines — as it is the case in many African countries — the cost of production of new money becomes cheaper or less than its exchange value. The issuing financial institutions can inject money into the economy in order to acquire resources from the public as long as its cost of production is below its exchange value. These resources can then be lent or allocated for economic development purposes (Thisen 1982:30-35). This can help also increase the financial deepening of the African economies.

The Issue of Social Dimensions of SAPs

The *social dimension* of structural adjustment programmes has attracted quite a lot of discussions among scholars and policy makers. Recently, (although UNICEF confirmed as early as 1987) the World Bank's study, along with other independent and international organisations studies confirm that despite the implementation of SAPs, the number of the poor are increasing such that there is a reversal in the rate of growth of social progress (Thisen 1982; Cornia *et al.* 1988). An example is the reduction in overall rate of school enrolment (Thisen 1994:79-115).

Ghana, which has been a 'model' for SAPs, in continuing the second phase of its adjustment programme, included the Programme of Action to Mitigate the Social Costs of Adjustment (PAMSCAD). Other such programmes are SDA and PAPSCA. The effort now is to find the best approach to this problem, whether through preventive programming (*ex ante*) or 'restorative remedies' (*ex post*). In any cases, the social dimension should be introduced right from the design of

SAPs and should be sustained during the whole period of the implementation of reforms.

The Issue Related to Income Policies

Another issue relates to *income policies*. In recent years, the dual 'devils' of high unemployment and inflation have simultaneously imputed negatively on world-wide economies but more disastrously on less developing countries, especially African LDCs. The static neo-Keynesian counter-cyclical fiscal approach (fiscal stimulation or fiscal restraint) has become moribund. Therefore, new policy measures have been instituted to complement the traditional ones. These include various forms of income policies such as voluntary or mandatory wage and price restraint.

These policies, when used in developed economies, have been almost exclusively in restraining inflation for brief period of time especially to squash inflationary expectations when the economy is not affected by excess demand. Although these formalised incomes policies are associated with industrialised market economies, this does not preclude the fact that such policies or elements therefrom are relevant for African economies.

Income policies in developing countries have sought to maximise income and income distribution. In contrast to developed economies, income policy and not wage policy is pursued because wages are a much smaller component of total incomes in less developing countries. Thus, incomes policy is more comprehensive in coverage, seeking to influence all forms of income and prices with wage employment often only a small, but nonetheless, an important part.

In developing African countries, incomes policy may include wage policy, fiscal policy, control of wages and salaries above the minimum, more equitable distribution of income and rapid expansion of employment opportunities. The component of better income distribution is spurred on by fiscal policy through taxation of profits and government expenditure in education, health, housing and infrastructure which may be the most important factors in reducing some of the wide disparities in real living standards in sub-Saharan Africa.

In 1994 there were major income policies initiated, invigorated by fiscal reforms stipulated in structural adjustment programmes being undertaken by many countries and the devaluation of the CFA franc. Some countries restructured or enacted legislation which provided for a minimum wage; a setting or a ceiling on wage increases which should not exceed an average of 10 per cent; settlement of all wage arrears so as to reinvigorate consumption and put public finances in order; raising of the agricultural producer prices by an amount slightly higher than the rate of inflation so as to sustain the recovery in

the food and agricultural sector and agro-industries. Among these were Togo, Gabon, Senegal and Burkina Faso. In Togo, the minimum wage had been 72 CFA fr/hr but increased to 75.6 CFA franc in January 1994. The high minimum wage instituted in Gabon has encouraged employees to seek non-Gabonese labour. In 1994, it is stipulated that there will be monthly increases of up to CFA franc 30,000 in wages because of the prolonged civil unrest.

The devaluation of the CFA franc in January 1994 provided for some changes in individual policies relative to income. This may have caused some countries to suspend policies that were to be implemented or to initiate or/and expand new policies. Following the devaluation, minimum wage which had remained unchanged since 1982 in Côte d'Ivoire underwent steep rises in 1994. State employees' salaries increased between 5 and 15 per cent. In Senegal, civil servants received salary increases between 7 and 24 per cent in March. The higher extreme going to those with the lower level positions. The total wage bill for Senegal is expected to increase by 9.6 per cent in 1994. This is in contrast to stipulation within the programme of economic reforms signed in January with the IMF. This percentage increase in the wage bill will amount to a total wage bill of CFA Franc 8.5 billion in 1994. Despite this increase, real income will still fall after devaluation because the government as well as the private sector (where wages will increase between 5 and 20 per cent) cannot accommodate the full impact of the devaluation.

In Burkina Faso, civil service salaries increased between 4 and 8 per cent in April 1994 while the minimum wage also increased by 10 per cent. In Congo, the planned cut in civil service salaries' was postponed. Even for some countries that did not experience any drastic devaluation, there was also state employees' salary increases. In Sao Tome and Principe, public civil servants salaries increased by an average of 30 per cent in 1994. The increase was between 8 and 30 per cent. In July, Zimbabwean civil servants, police and the army also received interim pay raises of 10 to 23 per cent.

Due to the fact that cost of living is increasing faster than average monthly wage in most African economies, especially sub-Saharan Africa, the parallel market is increasing in its volume and expanding in the type of trading and illicit activities. This portends to increase cross border activities. The disparities in civil servant earnings within subregional areas have also necessitated labour movement between borders and heightened black market trade. Reports show that civil servants in Guinea earn 40 per cent less than those in Togo and 20 per cent less than civil servants in Côte d'Ivoire.

In some countries, pay has been linked to some indicators. In Ghana, except in 1992 when pay raises were given prior to the general elections, pay has been

linked to productivity, inflation and ability of companies to pay. This is important because, to effectuate incomes policies in Africa, there has to be some compromise between the social partners-employees, employers and government representative to jointly develop strategies to pursue the goals of growth, equity and price stability.

Since incomes policies cannot serve as a substitute for fiscal and monetary policies, it must be used as a supplement to monetary and fiscal policies in achieving price stability, improving the trade-off between inflation and unemployment and to interrupt inflation expectation in the short run. But even in the absence of a comprehensive and coordinated incomes policy in sub-Saharan Africa, there are invariably connections between various areas of policy. Price changes affect the standard of living and income distribution which directly impacts on minimum wage. Because of these changes, there will be adjustment in the nominal wages which accordingly affects fiscal policy through taxation whereby employees will be entering taxable income brackets for the first time while others will be moving to a higher tax level.

Conclusion

Thus, the road ahead for structural reforms is still laborious and unpredictable. One positive sign is that a consensus seems to be building that Africa's problems are such that a 'quick fix' approach through stabilisation policies and Structural Adjustment Programmes (SAPs) will not bring about the sustainable development on an assured basis. In the 1980s and the first half of the 1990s, ambiguity and theoretical confusion still abound as to what 'structural adjustment' is all about. It began to be used as a synonym for good economic management as planning was used in the 1960s. It has become increasingly more difficult to distinguish the debates about adjustment from those held about 'development'. Consequently, views are being expressed that it is now apropos to return to development — whether 'human development' or 'sustainable development' — as the central theme of economic policy debate in developing Africa (UNDP 1990-1993).

The IMF and World Bank sponsored programmes have provided an 'anchoring effect' and in the process have exposed some caveats of reform programmes relative to developing Africa. Therefore, in formulating alternative programmes that are credible, sustainable and growth oriented, one has to look at exogenous factors that prey on the success of reforms, the speed of adjustment and who bears the burden of adjustment among other factors. One such alternative is the United Nations Economic Commission for Africa's 'Alternative Adjustment Framework to Structural Adjustment Programme for Socio-Economic Recovery and Transformation', (AAF-SAP). The AAF-SAP is more

elaborate and specific because: (i) it is human centred, (ii) it has a holistic approach to socio-economic change, (iii) it looks at the structural rudiments of the African political economy, and (iv) it acknowledges the uniqueness of every country (UN-ECA 1989).

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