BOSTON UNIVERSITY Global Development Policy Center

Centre for Human Rights
UNIVERSITY OF PRETORIA

GEGI POLICY BRIEF 008 • 07/2019

Jump-starting the African Monetary Fund

Hadiza Gagara Dagah *is a Hubert Humphrey Fellow at Boston University. She has been the Chief Financial Officer of Ecobank Niger.*

William N Kring *is the Assistant Director of the Global Development Policy Center, a university-wide center in partnership with the Frederick S. Pardee School for Global Studies.*

Daniel Bradlow *is SARCHI Professor of International Development Law and African Economic Relations at the University of Pretoria and Professor Emeritus, American University Washington College of Law. He was previously the first Head of the International Economic Relations and Policy at the South African Reserve Bank.*

HADIZA GAGARA DAGAH, WILLIAM N. KRING AND DANIEL BRADLOW

1. Summary

Given the rising concerns about debt sustainability and volatile growth in Africa, African Union leaders should use this week's trade summit as a venue to move forward on the establishment of the African Monetary Fund. On 7-8 July, African Union (AU) leaders will gather in Niger for their annual summit where the African Continental Free Trade Area (AfCFTA) agreement will be a core agenda item. This focus is appropriate given the significant benefits that intraregional trade agreements can offer in expanding the scope of south-south trade. However, this summit should also be used to reinvigorate efforts to implement a regional financial arrangement (RFA) for AU members, as a RFA would complement and strengthen the prospects of the AfCFTA. Fortunately, AU leaders approved a comprehensive African Monetary Fund (AMF) treaty in 2014 that has been signed, but not ratified, by eleven AU member countries to date. Fifteen member countries must ratify the statutes for the AMF to become operational.

When member states can turn to a mechanism that provides liquidity or balance payments support in moments of crisis, they are less likely to take actions that impede intraregional trade flows. This has been shown to be the case with RFAs such as the Latin American Reserve Fund (FLAR), which have historically supported and safeguarded intraregional trade by acting as a buffer to various short-term liquidity and/or balance of payments challenges. Hence the AU should pursue an approach to regional integration that seeks to deepen the economic ties of intraregional trade and to implement the AMF as a safeguard in cases of imbalances. Such an integrative approach has long been advocated by policy makers in Africa, as evidenced by the Organisation of African Unity Lagos Plan of Action for Economic Development of Africa (1980) and the Abuja Treaty (1991).

That said, AU members will have to confront a number of challenges in implementing the AMF when it enters into force. While the broad parameters of the AMF are outlined in a comprehensive treaty, a number of design and implementation choices have not yet been made. This offers policy

makers some flexibility in implementing the AMF. This policy brief draws lessons from the existing landscape of RFAs and their implementation and operations to propose concrete next steps for AU members in implementing an AMF that complements intraregional trade efforts.

In brief, AU member states should take three steps in order to create an effective AMF. First, AU leadership must emphasize the benefits and synergies of pursuing regional trade integration along with the implementation of the AMF. Second, an AU member state or group of member states should become the champion for advancing the ratification process. Finally, a re-established AMF steering committee should draw upon lessons from existing RFAs to develop a plan for addressing the current barriers to AMF implementation, such as resource constraints. Together, these initiatives, by promoting the AMF, will help foster a more integrated and prosperous Africa.

Table 1: Proposed AMF Implementation Timeline

1-3 Years	4-6 Years	7-10 Years
Steering Committee (SC): -Reinvigorate the AMF steering committee, including the recapitalization of resources for the committee. -AMF SC should create a scalable and flexible capitalization plan to lobby and incentivize AU members to ratify. --AMF SC Director should attend all RFA international meetings. **Issue linkage:** -Publicly link RFAs to trade integration efforts **Ratification:** -AU Heads of State should call for the initial 11 AMF signatories to ratify the agreement.	**Steering Committee (SC):** -SC should works to secure the ratifications of 15 members by year 2023, on target with the initial plan for AMF to be operational by 2023. -AMF SC Director should attend all RFA international meetings. **Issue linkage:** -AU should make member country ratification a core agenda item at AU annual summit in 2023. **Ratification:** -By year 2025, 4-6 of the current signatories should ratify the AMF and begin the process of contributing paid-in capital	**Steering Committee (SC):** -SC should continue to encourage member states to ratify -SC should be replaced with AMF staff at the Cameroon HQ and both the Board of Governors and Board of Directors appointed. **Ratification:** -By year 2029, all AU member states shall have ratified the treaty and paid in capital for all member must be in compliance with the AMF charter. -AMF should formally join RFA group and send staff to participate in all meetings and workshops.

2. Justifying the Need for an African Monetary Fund

The push for intraregional trade in Africa comes at a pivotal moment for the continent. Across the region, growth in gross domestic product (GDP) remains very uneven. Africa's growth rate "reached an estimated 3.5 percent in 2018, about the same as in 2017 and up from 2.1 percent in 2016" and is expected to hit 4 percent in 2019. In large part, this sluggish growth is due to the lackluster performance of the three largest economies. But it is also due to increasing debt vulnerabilities across the continent, as public sector debt has risen to levels that could increase borrowing costs and divert resources from other needed areas. Further, intraregional trade remains relatively low when compared to other regions of the world. While sub-regional trade integration may improve some opportunities for member countries, especially commodity exporters, to diversify their economies, increased intraregional trade "will allow Africa to be more competitive in global trade and value chains."

Regional trade offers many benefits but is also accompanied by risks. Trade interdependency between countries and greater integration across economic sectors not only provides significant growth opportunities, but also increases the risk of economic shocks via "spillover channels." When a country that is a member of a trading group or regional integration effort experiences an economic shock or recession, its economic linkages to its neighbors or the other members of the group can amplify the recession's impact on those other countries. These "spillover" impacts occur through the interruption of trade flows, integrated supply chains, and intra-regional non-FDI financial flows. To help mitigate these impacts, researchers at the International Monetary Fund (IMF) have argued that African nations should "build precautionary cushions…to set the state for growth and stability."

Since many African countries rely heavily on the export of primary products, vulnerability to fluctuations in commodity prices "has impeded most African economies from sustaining high growth… [and]…has also reduced macroeconomic levers." For example, the shock to commodity prices beginning in 2015 and the lack of access to sufficient external financing, caused many African countries to use their limited external reserves to buffer the shock. In addition, there is growing debt vulnerability across the continent, as many countries have been increasing public external debt levels, with much of the debt being dollar denominated.

In times of economic stress, market failures can drive-up borrowing costs for countries requiring liquidity or debt transformation to unsustainable levels and in some instances, completely shut off access to capital. In such instances, the AMF could provide member countries with liquidity support when the private sector will not provide sufficient liquidity. Additionally, by acting as a buffer that provides timely liquidity resources, the AMF would help to prevent disruption of intraregional trade. The FLAR in Latin America provides evidence of the potential effectiveness of RFAs in supporting regional trade. The relative successes of existing RFAs has helped spawn the proliferation of southern-led RFAs since the 2007-8 financial crisis.

The AMF could help member countries manage their sovereign debt by providing a stopgap in the form of liquidity assistance should debt service become unsustainable. Like other RFAs, the AMF could provide short-term liquidity resources or medium-term balance of payments via a variety of lending instruments to its member countries. In this way, the AMF would help safeguard the progress towards regional integration being made by the AU member countries.

3. A Burgeoning RFA Landscape

There is a burgeoning Global Financial Safety Net across the world though Africa remains to be one of the glaring gaps in the system. Following the 2007-8 Financial Crisis, there was approximately US $5 trillion available in the global economy for liquidity support, excluding the C6 swap lines (bilateral swaps provided by the US Federal Reserve, European Central Bank, Bank of Japan, Bank of England, Swiss National Bank, and Bank of Canada). The majority of this financing came from the IMF and national reserve holdings of member countries, with less than US $100 billion coming from RFAs. Fast-forward to 2018 and there is more than US $900 billion in liquidity available from the RFAs. This increase was due to both the creation of new RFAs and the expansion of the size and scope of existing RFAs. A number of new RFAs were introduced, such as the Eurasian Fund for Stabilization and Development (US $8.51 billion), the BRICS Contingent Reserve Arrangement (US $100 billion), and the European Stability Fund (US $563 billion), that added new liquidity to the global financial safety net (GFSN). Additionally, existing RFAs received infusions of additional resources and the expansion of their capacities. Most notably, the Chiang Mai Initiative was multilateralized and nearly tripled in size to US $240 billion.

Table 2: RFAs across the GFSN

Mechanism	Year Founded	Capital/Swap Amount (billions USD)	Lending Capacity (billions USD)
Arab Monetary Fund	1976	3.5	12.5
Latin American Reserve Fund	1978	2.9	4.7
Chiang Mai Initiative Multilateralization	2000	240	243.5
Eurasian Fund for Stabilization and Development	2009	8.5	8.5
European Stability Mechanism	2012	90.6	563
Contingent Reserve Arrangement	2015	100	85 (estimate)
African Monetary Fund*	2014	22.6	45.3
Total		**445.52**	**917.18**

*Founded via treaty, but not yet operational. Not included in calculation of available resources in GFSN.

While the new RFAs provide a much-needed expansion of resources in the GFSN, they also have contributed to the collective mobilization of RFAs to coordinate and act as a bloc. The FLAR and the ESM spearheaded an effort to open dialogue between the RFAs, through annual conferences, workshops, and high-level dialogues alongside the IMF-World Bank Annual Meetings. The RFAs have also begun to engage with the IMF on crisis response and to co-finance in certain instances, demonstrating the expanded capacities of an integrated but autonomous GFSN. The implementation of an AMF would give the AU an important and valuable seat at the table in these discussions.

The G20 Eminent Persons Group (EPG) appointed to assess post-financial crisis global economic governance sees tremendous potential in a decentralized GFSN. The EPG finds that the current GFSN "is highly uneven in scale and coverage across regions, has major components that are untested in crisis, and lacks coordination."

The ratification and implementation of the AMF would expand liquidity resources to 45 additional countries that do not currently have access to a RFA. Yet despite the promise of RFAs and potential benefits of an AMF in particular, no states have ratified the treaty and the institution's implementation is in a holding pattern. While a number of obstacles to AMF implementation remain, this policy brief outlines some policy prescriptions, coupled with a proposed timeline for implementation, that would overcome these obstacles.

4. Towards an African Monetary Fund: Progress and Remaining Obstacles

As part of Africa's efforts to promote regional integration, the AMF was conceived as a component of an AU regional institutional complex that would also include the African Central Bank and the African Investment Bank. Capable and autonomous regional institutions "at all levels and in all spheres" are seen as key to achieving the AU's growth and stability objectives for the region. The adoption of the AMF statutes in June of 2014 by 54 AU member countries was a key first step in establishing the institution. Unfortunately, the steering committee established in 2009 to set-up and operationalize the AMF ran out of money in 2011.

While progress of the AMF steering committee has largely stalled, the adoption of its founding texts by the Heads of State and Government of the AU represents a significant milestone. The expressed purpose of the AMF is to:

"a. Correct disequilibria in the balances of payments of States Parties; b. ensure stability of exchange rates among currencies and their mutual convertibility; c. promote African monetary cooperation so as to achieve African economic integration and speed up the process of economic development in State parties; d. reinforce capacity building in the design and the implementation of debt management policies in States parties as a means to achieving sustainable debt levels; e. promote the development of African financial markets; f. work towards the facilitation of settlement of commercial debts and the establishment of a clearing system for trade transactions amongst States Parties in order to promote intra African trade."

The AMF would be established with US $22.64 billion in authorized capital, of which at least fifty percent shall be paid-in capital. Upon the ratification of the statutes by 15 AU member countries, the AMF will be deemed operational.

However, the delay in implementing the AMF is the result of three key challenges. First, the implementation of the AMF lacks a decisive regional champion. While numerous reports and agendas from the African Union note the benefits of regional integration and an AMF in particular, the slowness with which implementation has advanced demonstrates that member countries have yet to fully commit to completing the establishment of the AMF. This suggests that there is a need for one AU member state to actively promote the AMF by encouraging signatory states to ratify the AMF treaty so that it can enter into force.

A second challenge to the implementation of the AMF is regional resource constraints. While the AMF will offer member countries the opportunity to borrow up to four times the resources they have paid in, regional financial challenges have complicated the capitalization and launch of the AMF. The AMF statutes were agreed by the AU country members in 2014, just a year before a collapse of commodity prices began to impact them. Accordingly, as member countries spent their foreign exchange reserves, it reduced their ability to contribute their share of the paid in capital required to activate the AMF. It should be noted that the treaty allows member states to make their paid-in capital contributions in four annual, equal payments, with the first installment to be paid within 60 days of the treaty entering into force, which will happen with the ratification by the fifteenth member country.

Finally, the perception that the AMF will merely duplicate services that are already available to some key African countries has slowed the adoption of AMF statues. For example, Egypt, Algeria, and Libya are members of the Arab Monetary Fund and South Africa is a member of the BRICS CRA. It is important to note however that most African states are not members of any RFA.

5. Policy Recommendations for AMF Implementation

The adoption of any complex agreement that requires ratification by member countries is likely to face a number of time consuming procedural and technical challenges that will make its implementation a lengthy process, as indicated in the time line below. That said, there are lessons that can be distilled from the creation and implementation of existing RFAs and past regional integration efforts, that provide insight into how AU members can most effectively more forward.

First, the AMF must be explicitly linked to regional integration and trade initiatives. During the negotiation for the FLAR, the implementation of the RFA was explicitly linked to efforts towards regional integration. The presence of an AMF will provide support for ongoing initiatives to boost intraregional trade in Africa and provide a first line of defense to help member countries address short to medium term liquidity challenges without impeding trade activity. Thus, the AMF, like other RFAs, can provide rapid liquidity assistance to member states. This can help to triage a crisis and offer member countries more time to negotiate a package with another source of financial support, such as the IMF. In this regard, it should be noted that eight of the AU member countries (Cape Verde, Comores, Djibouti, Eritrea, Guinea-Bissau, Sao Tome and Principe, Seychelles, and Somalia) will be able to borrow more resources from the AMF than the IMF.

Second, bringing the AMF treaty ratification process to a successful conclusion with require an AU member country to champion the cause of the AMF. A champion of the AMF would lobby other AU member countries to ratify the AMF and also push the AU to recapitalize the AMF steering committee.

Since Cameroon is the designated host country for the AMF's headquarters, it has an incentive to be a champion for the institution. Accordingly, Cameroon as host of the steering committee and future AMF headquarters could increase the visibility of the AMF project by sending Jean-Marie Gankou, Chair of the AMF Steering Committee, to the annual RFA meetings. This would help build linkages between the AMF and its global counterparts and help educate AU member countries about the contributions an RFA can make to Africa. It could also help create opportunities for the AMF to benefit from the expertise and experience of these other RFAs regarding the operationalization of a regional financial arrangement.

Finally, the steering committee for the AMF should develop a plan for overcoming the challenge posed by the substantial regional resource constraints. This will require balancing the AMF's need for resources to be credible with the limited ability of some states to contribute to the AMF. This could be addressed by negotiating an arrangement in which richer countries and other institutions contribute additional capital up-front that will be reimbursed as poorer countries make their paid-in capital contributions. In this regard, it is important to note that the AMF Board of Governors has the authority to extend the payment of paid-in capital for a term of up to 8 years. Further, the small to medium sized member countries should be allowed to count paid-in capital towards their international reserves. In an effort to increase its membership base, the FLAR negotiated such an arrangement with the IMF for new member countries. The AMF should use this agreement as the point of departure for an agreement on paid-in capital with the IMF. This would lower the barriers to the funding of the AMF and make implementation feasible.

BOSTON UNIVERSITY Global Development Policy Center

Boston University
53 Bay State Road
Boston, MA 02215

gdp@bu.edu
www.twitter.com/gdpc_bu
www.bu.edu/gdp

The Global Economic Governance Initiative (GEGI) is a research inititiative at Boston University's Global Development Policy Center. The GDP Center is a University wide center in partnership with the Frederick S. Pardee School for Global Studies. The Center's mission is to advance policy-oriented research for financial stability, human wellbeing, and environmental sustainability.

www.bu.edu/gdp

The Centre for Human Rights, University of Pretoria, is an internationally recognised university-based institution combining academic excellence and effective activism to advance human rights, particularly in Africa. It aims to contribute to advancing human rights, through education, research and advocacy.

http://www.chr.up.ac.za/

The views expressed in this Policy Brief are strictly those of the author(s) and do not represent the position of Boston University, or the Global Development Policy Center.

REFERENCES:

1 AfCTFA Aims to be operational by July 2019

2 Ocampo, José Antonio, and Daniel A. Titelman (2012). "Regional Monetary Cooperation in Latin America." ADBI Working Paper Series. Asian Development Bank, pp. 1-33 . https://papers.ssrn.com/abstract=2128437.

3 The AMF Steering Committee was previously established in 2009, but disbanded a few years later due to resources constraints.

4 African Development Bank Group (2019). "African Economic Outlook 2019," p. iii. Available at: https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2019AEO/AEO_2019-EN.pdf.

5 https://www.worldbank.org/en/region/afr/publication/taking-the-pulse-of-africas-economy

6 IMF (2018), Regional Economic Outlook: Domestic Revenue Mobilization and Private Investment (SUB-SAHARAN AFRICA).

7 Arizala, Francisco, Matthieu Bellon, and Margaux MacDonald (2018). "Africa Comes Together: Sub-Saharan African is becoming more integrated—which will aid growth but is not without risk." Finance & Development, pp. 48-51.

8 African Development Bank Group (2019), p. iii.

9 Arizala, Francisco, Matthieu Bellon, and Margaux MacDonald (2018), p. 51.

10 Global Economic Prospects, World Bank Group (2016).

11 Arizala, Francisco, Matthieu Bellon, and Margaux MacDonald (2018), p. 51.

12 African Development Bank Group (2019), p. xv.

13 Christensen, Benedicte Vibe (2016). "Challenges of low commodity prices for Africa." BIS Papers, No. 87.

14 Kring, William N., and Kevin P. Gallagher. "Strengthening the Foundations? Alternative Institutions for Finance and Development." Development and Change 50, no. 1 (2019): 3– 23. https://doi.org/10.1111/dech.12464.

15 Perry Mehrling (2015) "Elasticity and Discipline in the Global Swap Network." International Journal of Political Economy, 44:4, 311-324, DOI: 10.1080/08911916.2015.1129848

16 G20 Eminent Persons Group on Global Financial Governance (2018), Report of the G20 Eminent Persons Group on Global Financial Governance: Making the Global Financial System Work for All. https://www.globalfinancialgovernance.org/report-of-the-g20-epg-on-gfg/

17 "Agenda 2063: The Africa We Want." (2015) African Union Commission. Available at: https://www.un.org/en/africa/osaa/pdf/au/agenda2063.pdf.

18 Andzongo, Sylvain. "No African country has yet ratified the acts setting up the African Monetary Fund to be based in Cameroon." Business Cameroon, 07 January 2019. Available at: < https://www.businessincameroon.com/economy/0701-8728-no-african-country-has-yet-ratified-the-acts-setting-up-the-african-monetary-fund-to-be-based-in-cameroon>.

19 "Protocol on the Establishment of the African Monetary Fund." African Union, 27 June 2014, p. 9. Available at: < https://au.int/sites/default/files/treaties/36417-treaty-0046_-_protocol_on_the_establishment_of_the_african_monetary_fund_e.pdf>.