



United Nations  
Economic Commission for Africa



Southern African  
Development Community

# Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence Framework for Regional Financial Integration in SADC







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## Abbreviations and Acronyms

AfDB	African Development Bank
AMU	Arab Maghreb Union
ASEAN	Association of Southeast Asian Nations
AU	African Union
BCEAO	Central Bank of West African States ( <i>Banque Centrale des Etats de l'Afrique de l'Ouest</i> )
BEAC	Central Bank of Central African States ( <i>Banque des Etats de l'Afrique Centrale</i> )
BIS	Bank for International Settlements
CCBG	(SADC) Committee of Central Bank Governors
CEMAC	Central African Economic and Monetary Community
CFA	<i>Communauté Financière Africaine</i>
COMESA	Common Market for Eastern and Southern Africa
CMA	Common Monetary Area
CISNA	Committee of Insurance Securities and Non-Banking Financial Authority
COSSE	Committee of SADC Stock Exchanges
CPSS	Committee on Payment and Settlement Systems
CU	Customs Union
DBSA	Development Bank of Southern Africa
DFI	Development Financial Institutions
DFRC	Development Finance Resource Centre
EDF	European Development Fund
ESAF	East and Southern Africa Banking Supervisors Group
EU	European Union
FIP	(SADC) Protocol on Finance and Investment
IAS	International Accounting Standards
IFI	International financial Institution
IMF	International Monetary Fund
IOSCO	International Organisations of Securities Commissions

IFRS	International Financial Reporting Standards
MU	Monetary Union
NEPAD	New Partnership for Africa's Development
OAU	Organisation of African Unity
OHADA	Organisation for Harmonisation of Business Law in Africa
REC	Regional Economic Community
REPSS	Regional Payments and Settlement System
RFI	Regional Financial Integration
RISDP	Regional Indicative Strategic Development Plan
RTGS	Real Time Gross Settlement
SADC	Southern African Development Community
TARGET	Trans-European Automated Real-time Gross Settlement Express Transfer System
TIFI	(SADC's) Trade, Industry, Finance and Investment (division)
UNECA	United Nations Economic Commission for Africa
WAEMU	West African Economic and Monetary Union
WAMU	West African Monetary Union

# Foreword

The Southern African Development Community (SADC) is at a critical juncture as it contemplates the short amount of time remaining before it introduces a monetary union in 2016 and a single currency in 2018. The community has progressed markedly to meet some of the key milestones contained in the SADC Regional Indicative Strategic Development Plan (RISDP) and Finance and Investment Protocol (FIP).

Specific completed projects include the draft SADC Model Central Bank Law, which now is awaiting consideration and approval by Member States. Further progress, albeit not to the extent initially envisaged, is noted in the drafting of regional frameworks and laws for national payment, clearing and settlement systems; and bank supervision. Cross-cutting areas such as human resource development, inter-central bank communication and the Information Communication Technology (ICT), and the coordination of regional and international resources are receiving due attention.

This progress, although notable, remains limited. Member States are mindful of the enormous work ahead, made more difficult by lingering technical and capacity constraints. They are forging partnerships with indigenous private sector, international and regional financial institutions, and think-tank organisations in order to leverage on these partners' financial resources and technical expertise. These partnerships are particularly important as Member States remain committed to execute planned activities and to roll out programmes and projects outlined in the RISDP and FIP despite time constraints.

As part of the SADC Secretariat and the United Nations Economic Commission for Africa (UNECA) collaborative efforts over the years, guided by their multi-year programme, this study was produced by UNECA-Southern Africa Office (UNECA-SA) in collaboration with the SADC Committee of Central Bank Governors (CCBG) Secretariat. The study gives an overview of the ongoing financial integration process within SADC and the challenges for creating a unified regional financial market and a common monetary union. It covers some pertinent issues, including the integration of banking and capital markets, the harmonisation of national payment systems, regulatory questions, as well as institutional aspects of central bank independence, corporate governance, capacity building and inter-central bank communication.

A systematic analysis of these issues, and highlighting areas where progress has been lacking or slow is an important contribution to identifying and operationalising the steps that will be required, if the community's highly ambitious goals are to be achieved. The study's pre-eminent proposal of a Framework for Regional Financial Integration to guide the path towards the creation of a common currency for SADC is timely and such a Framework is needed urgently.

In the context of the preparation of this study, we would like to express our gratitude to the officials of the CCBG and UNECA for their diligence and enthusiasm in drafting this paper

and jointly facilitating the review Workshop on *Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence Framework for Regional Financial Integration* which took place in Johannesburg, South Africa from 19th to 20th November 2009. Under the general guidance of Mr. Alfred Latigo, Senior Economic Affairs Officer and Head: Regional Integration and Macroeconomic Policy Analysis Section of the UNECA-SA, the lead authors were UNECA-SA Economic Affairs Officer, Mr. Mzwanele G. Mfunwa, and UNECA-SA Social Affairs Officer, Mr. Jack Jones Zulu. These authors' drafting efforts were complemented by contributions from Mr. Gops Pillay and Ms. Masebili Dorothy Hlajoane, both from the South African Reserve Bank.

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This paper served as a background document to the above-mentioned Workshop. We wish to extend our sincere gratitude to the participants for their expert advice and their sharing of country situations. Their names are listed in the annexure to the Workshop report, attached to this paper. The deliberations and recommendations for improving the publication are highly appreciated.

Needless to say, the views expressed and conclusions reached in the background document are entirely those of the authors and do not necessarily reflect the official views of the UNECA or the CCBG, or of collaborating persons and affiliated institutions. All errors of omission and commission are the authors'.

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## Executive Summary

The Southern African Development Community (SADC) has an ambitious integration programme that includes establishing a regional central bank and monetary union in 2016; and a regional single currency in 2018. According to the SADC Regional Indicative Strategic Development Plan (RISDP), the community's development framework, these initiatives constitute the deepest form of economic and financial integration, and are a part of a strategic push to integrate the region financially and economically.

With a mere seven years before the SADC monetary union is due for launching, there is a heightened realisation that the timeframes are tight, while the list of the remaining assignments is long. In a frank assessment recently, the SADC Committee of the Central Bank Governors (CCBG) Secretariat took note of the SADC achievements in macroeconomic convergence and financial integration (Belle, 2009) while drawing the attention of policy-makers to the need for policy changes if deadlines are to be met.

A number of Member States have shown good results towards meeting the macroeconomic convergence indicators, even if the global financial crisis has stalled greater progress. Nonetheless, given the volume of commitments still to meet, coupled with the seemingly poor state of readiness of Member States, and the obvious clash between the sub-regional and continental timeframes, it may be necessary to re-adjust the SADC integration timeframes.

Doubtless, the SADC monetary union and the single currency goals face more daunting challenges. At the political level, a rather weak support for a monetary union is shown by the fact that not all Member States have ratified the Finance and Investment Protocol (FIP), which is an instrument to bolster macroeconomic stability and reinforce a sound financial and investment environment in order to achieve deeper monetary integration.

At the policy level, SADC is still far from meeting the two key conditions to meet its goals. First, the exchange rate union, which permanently fixes relationship among countries' exchange rates, is no where in sight. The drafting of a framework to guide processes towards this union has not even commenced. The same situation obtains on the second condition, namely, the full convertibility of the regional currencies among Member States. The process of eliminating exchange controls among Member States is still to gain traction in the face of tensions emanating from considerations of national economic interests.

At the programme implementation level, there is a significant amount of work undone to develop the various focus area frameworks and model regional bills as required by the FIP. Those few that have been completed (for example, on central bank and payment and settlement systems) have gaps in that they lack timelines for absorption into national legislations, as well as the absence of enforcement clauses.

The vast number of ongoing and pending programmes and projects, and the proliferation of committees and sub-committees to implement them, highlights the distinct nature of the processes and steps to reach a monetary union and single currency. In this situation, the risks of conflict of timetables and lack of coordination become elevated. To be sure, the SADC Treaty and the FIP do address the initial stages of integration, but there is no specific all-encompassing document yet that takes the process beyond this initial point.

The central objective of this study, therefore, is to encourage SADC to develop an overriding Framework for Regional Financial Integration that would solidify the integration process. Such a Framework will display all disparate processes of regional financial integration in a logically consistent format, sequencing key milestones and including timelines for each step of the way. Experiences from other monetary cooperation regions show that the suggested Framework tends to be comprehensive, covering financial policies and the development of suitable infrastructure and institutions. The Framework should also set out the key criteria for measuring progress towards integration.

Properly done, such a Framework promises a number of benefits. It would pinpoint and bring to light instances of lukewarm political support, and identify ways to re-energise political enthusiasm in a timely fashion. Second, it would make clear the apparent clashes of integration timeframes among RECs of which some SADC Member States are part of<sup>1</sup>, as well as incompatibility of timeframes with those of the African Union<sup>2</sup>.

Furthermore, the proposed Framework should identify slippages in the implementation of the various programmes and projects in a timely manner and allow for corrective measures. Some areas where countries have previously faced difficulties include (i) inadequate support at the national level for the integration process, (ii) a dearth of human and technological resources to implement some of the technical aspects, and (iii) the presence of weak regional policies and procedures. Indeed, a detailed Framework should identify resource requirements for each of the stages, and measures to assist resource poor Member countries.

The proposed Framework must stress the need for a participatory approach to regional integration. To secure regional ownership and support, the shape of regional institutions tasked with implementing various policies, including the regional monetary policy, must be endorsed and supported by all stakeholders, not only the political leadership. Therefore, it is important to roll out public education programmes about the SADC integration agenda, encourage the participation of non-governmental organisations, trade unions and the general public in the debates about regional policies, institutions and how these should impact national policies and institutions.

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<sup>1</sup> For example, a timeframe that may clash with that of other regional economic communities to which some SADC Member States may belong.

<sup>2</sup> For example, the timeframe of the African Monetary Cooperation Programme (AMCP) of the African Union clashes with that of RISDP with respect to achieving the single central bank, with AMCP's goals coming in earlier than that of RISDP.

It is, therefore, critical that the proposed Framework should outline the modalities for an inclusive regional financial integration process. Accordingly, this paper commends the stance adopted by the recent presentation to the CCBG that the citizens of SADC countries should no longer be kept in the dark about what is happening. Indeed, the participatory approach should: “*Ensure that education [about] the cost and benefits of a monetary union occurs and debate takes place early [involving] the public, non-governmental organisations and trade unions, the likely parties to be affected by regional economic integration*” (Belle, 2009).

In sum, this paper is an attempt to urge the SADC leadership to kick-start the process of compiling a comprehensive Framework for Regional Financial Integration. It raises some of the issues that should be addressed by such a Framework, including whether the timeframes in the RISDP and FIP remain viable; how the weak political support could be revitalised, including through measures to support poorer Member States; how the capacity issues can be addressed to avert implementation delays; and importantly how to inject a participatory content in the entire regional integration programmes to gain more adherents.

## **Assigning roles to stakeholders**

The SADC Member States should decide on the roles that various stakeholders should play in the region’s financial integration agenda. First, the specific role of the SADC Secretariat should be enhanced as it assumes more prominence in the region. If Member States decide that it should take lead in putting together the Framework, they should consider capacity implications as well.

Second, necessarily the Framework will put more responsibilities on individual Member States including the task of ensuring sound national institutions, political buy-in, citizen participation, provision of resources to meet regional obligations, and others. Member States must carefully consider how to accomplish these tasks, and how they expect resource-poor Member States to meet integration, including institutional reform costs.

Third, in light of the imperative to forge partnerships with non-state actors and gain public support, Member States should incorporate into the Framework, and institutionalise, modalities for the participation of the private sector, civil society, media and the general public in the integration processes. Sufficient time needs to be allocated to public debates on key integration policies and programmes. These debates could also take place in the context of parliamentary processes.

Finally, the Framework should outline modalities for international cooperating partners’ involvement. It will have to incorporate some of the key principles contained in the 2005 Paris Declaration, for example, on donor support of harmonisation and coordination in the sub-region, and of supporting internal democratic processes.

## Key recommendations

The recommendations of the SADC experts at the Workshop that took place in Johannesburg, South Africa, from 19th to 20th November 2009 to discuss this paper and provide the ECA and the CCBG with a way forward are useful. These recommendations are as follows:

On policy and institutional issues, the Framework should draw the attention of Member States to the following matters:

- The SADC Committee of Central Bank Governors (CCBG), the SADC Secretariat and partners under the FIP should undertake a cost/benefit study to inform the process of establishing the SADC Monetary Union, including the extent of ‘asymmetric of shocks’ across countries, and the possibility of adopting a gradualist approach towards the monetary union [example, the use of Common Monetary Area (CMA) as a building block].
- The fear of losing monetary policy control at the national level could be addressed through a transparent and participatory approach to a monetary union involving all national central banks and ministries of finance.
- A compensatory facility should be considered to address adjustment costs for adversely affected economies. There is a further need to reassess the macroeconomic convergence parameters in the context of SADC members’ economic realities, especially in light of current global environment.
- Against the backdrop of the recent political decision of SADC/EAC/COMESA to harmonise policies, the SADC should strive to avoid duplication of efforts but instead should draw on the experiences of these other RECs such as on Financial Stability Indicators being considered by the COMESA.
- Political commitments should be shown by drawing up and implementing an action plan for attaining the monetary union. This action plan should include the provision of adequate resources, including strengthening human capacity of the SADC Secretariat. Furthermore, such a political commitment should go beyond the mere signing of protocols and treaties, to actual domestication of these instruments into national laws.
- Given the complexity of the process towards the monetary union, and the amount of work still to be done between now and the targeted completion date, there is need for Member States to develop national strategies, structures and programmes to implement the monetary union agenda.



- On harmonisation of bank supervision and regulation, the meeting advocated the need to promote adherence to international norms and standards by banks as well as share information regarding banking regulatory and supervisory matters. In addition, consideration could be given to the establishment of a regional supranational supervisory authority
- Inter-central bank communication and coordination should be enhanced to include devising a common policy approach in order to deal with external economic shocks collectively.
- The ‘variable geometry’ approach should be followed in the process of establishing the monetary union.
- There is need for a Monetary Union Agreement to be developed and signed by Member States

On capacity building, the Framework should underscore these issues:

- There is an urgent need to address capacity at different levels: human, financial, institutional and technical.
- In the spirit of the Paris Declaration on Aid Effectiveness of 2005, there is a need for SADC to harmonise and coordinate the International Cooperating Partner’s ( ICPs) support to the monetary union process.

On participation of the public in the SADC regional financial integration agenda and processes, the Workshop recommended as follows:

- The SADC Secretariat and Member States need to come up with a strategy such as domesticating the regional integration process to involve the public in the monetary union process, in particular, and the integration agenda, in general.
- The SADC Secretariat and Member States should sufficiently sensitise the objectives, costs and benefits of the monetary union and regional integration agenda to the wider public.



# Introduction and Background

# 1

## 1.1 Origins of SADC Financial Integration

1. The goal of a common African currency has long been a pillar of an African unity, a symbol of the strength that will emerge from efforts to integrate the continent. The prospect of a single African currency was set as a goal of the Organisation for African Unity (OAU), created in 1963, and given a renewed priority in 2001 when the OAU's Member States transformed this continental body into the African Union (AU). In August 2003, the Association of African Central Bank Governors further announced that it would work for a single currency and common central bank by 2021.
2. The success of the AU monetary union strategy depends on the success of the existing five regional economic communities (RECs)<sup>3</sup> to individually reach such a union. These regional unions would be an intermediate stage, leading ultimately to their merger, creating a single African central bank and currency. In pushing forward the integration agenda of the African Economic Community (AEC)<sup>4</sup>, these RECs are contemplating establishing monetary unions in the belief that monetary integration will deepen regional integration (UNECA & AU, 2008).
3. The creation of monetary unions in Africa is motivated by several factors, including anticipated economic benefits. For example, deeper continental integration is projected to induce increased trade and investment, which in turn will create employment opportunities. Furthermore, it is hoped that such integration will get African nations to participate effectively in the globalisation process. Ultimately, African leaders, therefore, view regional integration as a spur for sustained economic growth and development, as well as lowered levels of poverty (UNECA & AU, 2008).
4. For Southern African countries, the formation of a monetary union in the SADC<sup>5</sup> is provided for under various articles of the SADC Treaty. In the preamble to the SADC Treaty the Community seeks *“to promote the interdependence and integration of our national economies for the harmonious, balanced and equitable develop-*

***“The success of the AU monetary union strategy depends on the success of the existing five regional economic communities”***

<sup>3</sup> These RECs are: Arab Maghreb Union (AMU), the East African Community (EAC), the Economic Community of West African States (ECOWAS), the Economic Community of Central African States (ECCAS), the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA).

<sup>4</sup> The framework contained in the Abuja Treaty of 1991 calls for the creation of a continent-wide AEC and lays six stages for the implementation of the integration agenda. Included in these stages is the creation of a monetary union for the continent.

<sup>5</sup> This objective was also envisaged in those of SADC's predecessor, namely the Southern African Development Coordinating Conference (SADCC) whose members were Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, Zimbabwe and, later, Namibia. The 1980 Lusaka Declaration states the SADCC objectives as (i) a reduction of economic dependence in general (not only on apartheid South Africa), (ii) the forging of links to create a genuinely meaningful and equitable system of regional integration, (iii) the mobilisation of resources to support national, interstate, and regional policies, and (iv) a concerted action to secure international cooperation for the purpose of economic liberalisation.

*ment of the Region for an overarching objective to achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the peoples of Southern Africa and support the socially disadvantaged through regional integration”*<sup>6</sup>. Moreover, “*Member States will seek to harmonise political and socio-economic policies and plans...*”<sup>7</sup> and “*improve economic management and performance through regional co-operation*”.<sup>8</sup>

5. More specifically, according to the SADC RISDP, the overarching goal of the community is to attain a monetary union through the creation of a regional central bank by 2016 and adoption of a single currency by 2018 in a systematic and progressive manner. The envisaged monetary union in the SADC is predicated on a number of economic and financial imperatives aimed at galvanising efforts by Member States to achieve deeper forms of regional integration. Member States expected the realisation of a monetary integration to be a gradual process, starting with a free trade area in 2008 and ending with a single currency by 2018.

## **1.2 Rationale for a SADC Financial Integration Framework**

6. This study is part of the multi-year programme (MYP) between the SADC Secretariat and the UN Economic Commission for Africa that, inter alia, seeks to improve the governance of financial institutions in order to accelerate regional financial integration in the region. As part of this MYP the two organisations have conducted an assessment of the SADC macroeconomic convergence programme based on a number of macroeconomic indicators. The first comprehensive review of Member States’ performance relating to macroeconomic convergence was done in 2005. Reports of the review were finalised and presented to the Ministers of Finance and Investment in July 2007 for approval. It is planned that brief reviews will be conducted twice a year.
7. However, an outstanding assignment to assist in the planning for a SADC monetary union is a drafting of a Framework that would define the process leading to such a union as well as the introduction of a common currency. Such a Framework needs to set out criteria for measuring progress towards a regional financial integration. It should further cover issues of financial policies (e.g. financing of public sector), financial infrastructure (for example, regulation, supervision and financial reporting standards, payment systems, legal frameworks, credit information), and financial institutions (for example, banks, non-bank financial institutions, credit and capital markets).

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<sup>6</sup> SADC Treaty, Article 5(1)(a)

<sup>7</sup> SADC Treaty, Article 5(2)(a)

<sup>8</sup> SADC Treaty, Article 5(2)(g)

8. The SADC Memorandum of Understanding on Macroeconomic Convergence calls for the creation of “*appropriate institutions and mechanisms for the implementation of programmes and operations of SADC*”. In short, the monetary union will need strong regional institutions that conform to a set of criteria on common standards and international best practices. Furthermore, these institutions must adhere to the tenets of good governance by putting in place transparency, reporting and compliance mechanisms. Finally, they should have effective accounting regimes with clearly defined functions and roles for various stakeholders.

**“The monetary union will need strong regional institutions”**

### **1.3 Contribution of this study to the SADC Framework for Regional Financial Integration**

9. In light of the above, this study seeks to contribute to the SADC goal of regional financial integration by calling on the community to compile a Framework for Regional Financial Integration. The assumption is that if the deadline of 2016 for a monetary union is to be met, such a Framework is urgently needed to assist in the harmonisation of Member States’ financial institutions to regional requirements.

### **1.4 Research methodology**

10. This is a desk-top study that relies on secondary sources of information and data. Most of the data sources are web-based and consist, inter alia, of the Committee of SADC Central Bankers; laws of SADC central banks; websites of SADC central banks, AU Commission, New Partnership for Africa’s Development (NEPAD), RECs, and regional and international financial organisations. The study was carried out with the collaboration of the Secretariat of the SADC Committee of Central Bank Governors, located at the South African Reserve Bank.

### **1.5 Structure of the paper**

11. Given the overall objective of this study, chapter 2 considers conceptual issues of regional financial integration. The aim is not to propagate a step-wise process for SADC, but merely to highlight various stages that are involved to reach a monetary union. This non-linearity is borne out by actual experiences discussed in Chapter 3. Chapter 3 further attempts to draw some lessons for SADC.

12. Chapters 4 to 7 select a few focus areas that dominate considerations for regional financial integration. The central message is that all these areas should be harmonised across SADC; they must meet high international standards; and Member States need to carefully analyse resource requirements, and should identify potential funding sources. Some of the cross-cutting issues are considered in chapters 8 to 10. Chapter 11 summarises issues that have been raised in the paper.

# Regional Financial Integration Conceptual Issues

## 2.1 Introduction

13. Regional financial integration is deemed capable of redressing several economic problems associated with the small, fragmented financial markets in Africa. Linn and Wagh (2008) note that consolidated financial markets, a result of regional financial integration, have many benefits such as: bringing together scarce savings, viable investment projects and financial infrastructure; boosting the numbers and types of financial institutions and instruments; increasing competition and innovation; reducing inefficiencies in lending; expanding opportunities for risk diversification; helping to improve regulatory and supervisory bodies; insulating central banks from domestic fiscal excesses; harmonising regional laws and institutions; and creating additional opportunities for learning by doing.
14. In the same vein, Park (2004) cites the Asian financial crisis of 1997 which prompted the region to enhance their financial integration efforts. These efforts led to their developing mutual surveillance mechanisms and encouraging members to extend financial assistance to each other when confronted by threats to economic stability. In this case, regional integration not only led to economic benefits but also strengthened regional solidarity.
15. Furthermore, Park and Yang (2006) argue that financial integration with international financial markets can enhance growth potential and ease the burden of adjustment to external shocks in emerging economies. They further postulate that an increase in capital mobility between the north and south allows for a high rate of investment and hence a high rate of growth in capital-poor emerging market economies while offering a higher rate of return on capital to capital-rich advanced countries. Through the efficient allocation of resources, financial market integration leads to specialisation in production, optimal economic policies and development in general.

## 2.2 Stages leading to full regional financial integration

16. In a project titled *Making Finance Work for Africa*, the African Development Bank (2008) argues that “*regional financial integration is the culmination of a long process that begins with gradually increasing information sharing and extending to cooperation or collaboration, harmonisation, and finally to unification in the entire spectrum of financial policies, financial infrastructure and financial institutions*” (AfDB, 2008). The actual process, however, is not necessarily a step-wise process as it

might theoretically be conceived in table 1 below. In fact, the steps are outlined to enable policy-makers to note the measures they need to take in order to reach a particular stage of regional financial integration. Indeed, in practice, a rigid stratification may not be entirely feasible and some policies and some institutions may be implemented earlier or later “*while not departing from the implementation of a timetable of the core policies and institutions*” (AfDB, 2008).

**Table 1: Regional Financial Integration: A Generic Roadmap**

Stage of RFI	Domestic Measures	Regional Measures
<b>Pre-conditions</b>	<b>Macroeconomic Stability Bank soundness</b>	
<p><b>Stage 1:</b> Preparatory Member countries begin to take steps to modernise their financial systems by implementing part of international financial standards &amp; initiate exchange of information among themselves regarding the programme being made.</p>	<ul style="list-style-type: none"> <li>• Improve national payment systems (RTGS) to reduce payment delays and transfer costs.</li> <li>• Strengthen bank supervision &amp; regulatory framework;</li> <li>• Improve accounting standards (IFRS);</li> <li>• Improve core elements of legal system (land &amp; corporate registries, property rights, contract enforcement)</li> </ul>	<ul style="list-style-type: none"> <li>• Agree to establish FTA;</li> <li>• Regional secretaries advance &amp; implement regional agenda;</li> <li>• Exchange of information &amp; regular meetings between monetary &amp; financial authorities;</li> <li>• Regional committees delineate areas &amp; modalities of integration process;</li> <li>• Bilateral &amp; regional agreements offer technical assistance to ‘less developed’ members to upgrade their financial systems</li> </ul>



Stage of RFI	Domestic Measures	Regional Measures
<b>Pre-conditions</b>	<b>Macroeconomic Stability</b> <b>Bank soundness</b>	
<p><b>Stage 2: Harmonisation</b></p> <p>Member countries to modernise their financial system. Steps should be taken to harmonise &amp; link regional financial policies, institutions, and rules &amp; regulations</p>	<ul style="list-style-type: none"> <li>• Expand payments systems to include electronic fund transfers, security deposit systems, and payment switches;</li> <li>• Devise cost-effective systems for small transfers;</li> <li>• Further strengthen bank supervision &amp; regulation by ‘large’ compliance with IAS, etc. ;</li> <li>• Remove intra-regional exchange controls;</li> <li>• Liberalise foreign capital inflows;</li> <li>• Strengthen stock exchange (if it exists) rules &amp; regulations, &amp; implement supervision (IOSCO) principles;</li> </ul>	<ul style="list-style-type: none"> <li>• FTA fully effective;</li> <li>• Agree on relevant convergence criteria;</li> <li>• Establish surveillance &amp; monitoring mechanisms;</li> <li>• Regular meetings between country regulators &amp; supervisors occur;</li> <li>• Harmonise policies regarding inward capital flows;</li> <li>• Link national payments systems to (REPSS &lt; TARGET);</li> <li>• Establish private financial sector consultative bodies</li> <li>• Regional physical infrastructure development bodies</li> </ul>
	<p>Substantially complete the modernisation of the financial systems, making them market-based; Central bank autonomy &amp; reinforced supervisory authority; Remove barriers to entry of regional &amp; foreign banks to improve competition; Develop national credit information systems.</p>	

Stage of RFI	Domestic Measures	Regional Measures
<b>Pre-conditions</b>	<b>Macroeconomic Stability Bank soundness</b>	
<b>Stage 3:</b> Cooperative Members make substantial cooperative moves towards harmonisation & linking their financial sector policies. They also strengthen & make more operative the regional surveillance & monitoring mechanism	<ul style="list-style-type: none"> <li>• Gradually liberalise exchange controls vis-à-vis the rest of the world;</li> <li>• implement regionally agreed comprehensive convergence criteria;</li> <li>• Coordination of monetary &amp; exchange rate policies</li> </ul>	<ul style="list-style-type: none"> <li>• Agree to establish customs union;</li> <li>• Regional FDI regime;</li> <li>• Establishment of comprehensive convergence criteria &amp; its monitoring with MDBs/IFIs support;</li> <li>• Fully harmonise regulatory, supervisors, &amp; accounting standards;</li> <li>• Single bank licensing, cross-border participation of regulators &amp; supervisors in bank supervision;</li> <li>• Develop a centralised credit information system;</li> <li>• Develop region-wide securities market infrastructure &amp; regulations.</li> </ul>
<b>Stage 4:</b> Members move to unify their institutions, rules and regulations, as well as financial products		<ul style="list-style-type: none"> <li>• CU fully effective;</li> <li>• Unify stock exchanges;</li> <li>• Adopt broad legal system;</li> <li>• Partially pool reserves;</li> <li>• Regional bond market</li> </ul>
<b>Stage 5:</b> In this stage members yield sovereignty in monetary policy to a regional authority	<ul style="list-style-type: none"> <li>• Exchange local currency for a regional currency;</li> <li>• Reserves in common currency.</li> </ul>	<ul style="list-style-type: none"> <li>• Regional CB;</li> <li>• Regional common currency.</li> </ul>

Source: AfDB, 2008

17. In the preparatory stage policy-makers modernise domestic financial systems, including payment systems. Member States also agree to enter into a free trade agreement and increase information-sharing endeavors about each member's progress. At the harmonisation stage, Member States attempt to comply with various international standards and practices in the financial sector, and pursue regional harmonisation of policies and institutions. Here, intra-regional exchange controls are eliminated; foreign investment inflows get liberalised; and stock exchanges strengthened. Furthermore, Member States actually enter into a formal FTA.
18. The cooperation stage is a critical one. Here, countries seek to cooperate in implementing agreed convergences criteria, which get monitored and evaluated by a regional ministerial council. Countries further complete the full harmonisation process relating to regulatory, supervisory, and accounting procedures started in the harmonisation stage. They also cooperate in cross-border regulation and supervisory activities; link domestic securities markets; and enter into a customs union on a gradual basis. Legal systems are reformed to enable cross-border enforceability of contracts, while cooperation in monetary and exchange policies begins in earnest. In the SADC context, Member States will need to determine what monetary and exchange rate cooperation they deem feasible. In doing this, one possibility is to gradually extend the CMA beyond current membership, starting with countries with immediate geographical proximity (e.g. Zimbabwe and Mozambique).
19. The fourth stage is the integration phase that shifts focus of action to the regional level. Here, (i) the customs union is fully operational; and (ii) various national financial institutions are integrated including in the exercise of regulatory and supervisory functions that incorporates a single bank licensing, a single regulatory agency and increased cross-border presence of financial institutions originating from Member States. There is also a partial pooling of external reserves to meet balance of payment difficulties, the establishment of regional bond market and, maybe, a unified stock exchange.
20. After the above processes have been completed, Member States can now engage seriously with the unification programme in which they introduce a common currency and a regional central bank. At this stage, an economic community may also be launched. An introduction of a common central bank would imply that Member States yield their sovereignty in monetary matters to a supra-national central bank. Institutional arrangements are put in motion to facilitate the transition from national currencies, exchange rates and central banks to the unified monetary system. Detailed attention is given to institutional set-up, including political leadership. Strong political will is central at this stage, while dedicated civil service and civil society acceptance of the integration arrangement will be cardinal.

**“A  
common  
central bank  
would imply  
that Member  
States yield  
their sovereignty  
in monetary  
matters to a  
supra-national  
central bank”**

## 2.3 Economic Implications of Regional Financial Integration on SADC Countries

***“Member States hope that the process will vastly improve the economies of all, particularly the less developed countries”***

***“Member States are supporting deeper regional financial integration in order to boost intra-regional trade”***

21. The SADC is a region with one of the most diverse economies in the world comprising Africa’s largest economy (South Africa), some of the poorest, small landlocked economies (Lesotho, Swaziland, and Malawi), and small island economies (Seychelles, Madagascar, and Mauritius). Differences in incomes are also vast, ranging from middle-income countries (South Africa, Botswana, Lesotho, Namibia, Swaziland, and Mauritius), to low-income countries (Madagascar, Malawi, Mozambique, Tanzania, and Zambia), to fragile states (Democratic Republic of Congo, and Zimbabwe), and to oil exporter (Angola).
22. In these geographical and economical landscapes, attempts to deepen cross-border financial integration pose both opportunities and challenges. Member States hope that, on net, the process will vastly improve the economies of all, particularly the less developed countries. Some of the arguments point to the current regional set-up and say that firm foundations for deeper financial integration have been set. For example, financial integration is already deep among the Common Monetary Area (CMA) members (South Africa, Lesotho, Namibia and Swaziland), with monetary policy among them highly synchronised. Beyond CMA, South African banks have significant presence in the rest of the region (Botswana, Mozambique, Tanzania, Zambia, and Zimbabwe). In other areas, integration has a long history as well. On labour flows, large numbers of unskilled and semi-skilled workers from Botswana, Lesotho, Malawi, Mozambique and Swaziland sought employment in South African mines, resulting in remittances being a major source of foreign earnings for these countries.
23. Member States are supporting deeper regional financial integration in order to boost the budding intra-regional trade. Currently, intra-SADC trade remains low compared to other blocs, and dominated by South Africa. They hope that the SADC free trade area launched in August 2008 will alter the patterns of trade for the better in favour of smaller countries through concerted efforts to improve regional infrastructure, and attending to barriers to trade matters such as the ‘rules of origin’ problem.
24. South Africa dominates foreign investment in the region as well, accounting for 6 per cent of the stock of total foreign direct investment in SADC on average and over 10 per cent in Botswana, the DRC, Malawi, Mozambique, Swaziland, and Zimbabwe. These investments are largely in the resources sector, although investments in other sectors (telecommunications, financial services and retailing) is increasing. The elimination of the exchange rate risk that comes with financial integration process will allow for an increased capital inflow, as well as regional investment opportunities that should result in economic growth and welfare gains. Eliminating exchange rate risk will also reduce transaction costs

usually incurred when changing one currency to another. More trade and investment flows will greatly increase in a monetary union whose benefits should entail price stability and monetary policy credibility.

25. There are concerns around the move towards a monetary union, however. By far the most often talked about concern is the loss of autonomy to use the key tools of macroeconomic management, namely the monetary and fiscal policies. As many SADC Member States rely on fickle donor flows (for example, Zambia, Malawi, the DRC, and Tanzania) and unpredictable prices of commodities (for example, Angola, Zambia), the argument is that the monetary policy instrument allows a country the freedom and flexibility to steer the economy in a particular direction. Moreover, limitations on the ability of government to conduct fiscal policy, constrained by the limits collectively agreed upon and imposed in respect of budget deficit financing could prove socially and politically difficult to honour, even if these limitations are sound for the entire community. For example, an imposition of limits on deficit financing may be desirable to prevent Member States from running large unsustainable deficits that could put upward pressure on interest rates and exchange rates in the entire monetary union area.

26. In conclusion, it bears to mention that these concerns are contested in some circles. On the loss of monetary policy as a tool of economic policy, for example, Reade and Volz (2009) show that the *de facto* degree of monetary policy autonomy (in contrast to *de jure* sovereignty) of most small open economies is limited, as their monetary policy decisions are in many cases driven by the monetary policies of large neighbouring countries or the world's leading central banks (for example, the US Federal Reserve Bank and the European Central Bank). These small economies would, therefore, have not much to lose when joining a monetary union. This argument could be held true in the case of CMA countries whose *de facto* monetary policy was determined by South Africa, but an arrangement which has served the economies of Namibia, Lesotho and Swaziland well. In any event, in SADC, it is likely that Member States will gain monetary policy influence (as happened in the EU) by getting a seat at the policy-making decision body of the SADC Central Bank.

**“Member States will gain monetary policy influence by getting a seat at the policy-making decision body of the SADC Central Bank”**

## Regional Monetary Cooperation Experiences

### 3.1 Introduction

27. An overview of the various RECs that have experimented with monetary cooperation indicates that indeed, a step-wise process as described in chapter 2 is not observable. As indicated below, monetary cooperation experiments have been slow to reach agreed milestones; political support has been lukewarm; and implementation of integration programmes has been patchy at best, adducing the lack of popular support, dearth of institutional backing, meagre resources, and a lack of political-will. Indeed, African RECs are plagued by problems associated with multiple memberships, as well as the inability to see beyond the short-term costs of integration.
28. These weaknesses notwithstanding, there are indications of progress shown by the increasing intra-regional trade, deepening financial cooperation, and increasing willingness to pool regional resources to implement regional projects. The paragraphs below serve two main purposes: to take a parenthetical look at the current integration status of various RECs, and to cull lessons for the envisaged SADC monetary union project.

***“Monetary cooperation experiments have been slow to reach agreed milestones”***

### 3.2 Asia

29. The Association of Southeast Asian Nations (ASEAN)<sup>9</sup>, established in 1967, sees the end-goal of its economic integration agenda as ASEAN Economic Community (AEC). One of the key activities towards this goal is a roadmap for financial and monetary integration of ASEAN in four areas, namely: capital market development, capital account liberalisation, liberalisation of financial services and currency cooperation. Furthermore, ASEAN has developed an AEC Scorecard mechanism to track the implementation of Member States’ commitments. This scorecard seeks to provide a comprehensive picture of how ASEAN is progressing to an AEC by 2015.
30. Ongoing projects to deepen ASEAN financial cooperation include the setting up of regional liquidity support arrangements through the Chiang Mai Initiative (CMI), and the establishment of the Asian Bond Fund. The Asian financial crisis of

<sup>9</sup> ASEAN Member States are: Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam

1997 provided an impetus for deeper regional financial cooperation. Through lessons from that crisis, Asian countries have reached a consensus to enhance their own risk management abilities in order to prevent and resolve any future financial crises. A series of initiatives at the regional level have been instituted to boost regional self-sufficiency ranging from information sharing to financing arrangements in foreign exchange. Governments have also taken steps to deepen bonds markets to reduce reliance on bank financing and to shelter the regional economy from possible future repercussions of capital volatility emanating from elsewhere in the world (Zanello, 2006).

31. The on-going debate on monetary integration in Asia is now about whether a common currency or some system of coordination of exchange rate policy across the region can foster enhanced intra-regional trade, investment, and financial flows. The usual concerns are being raised such as the loss of ability to use the exchange rate as a shock absorber during the integration stage when currencies have been permanently fixed to one another. As is the case in SADC, this concern emanates from the marked differences in ASEAN Member States' with (i) economic disparities just being too wide and (ii) economic structures being very different. For example, some economies are governed by advanced technology and services, others are largely agrarian, and still others are dominated by mass manufacturing as the driver of growth. There is also no anchor currency similar to the Deutsche Mark in Europe towards which other currencies can converge (Shanmugaratnam, 2006).
32. To conclude, it is well to note, however, that for now East Asian discussions are less about monetary unification than about monetary cooperation, which would not necessarily lead to the creation of a common currency. Indeed, monetary unification is no official goal of ASEAN+3. Even the 10 ASEAN countries, which aim to create an ASEAN Economic Community, have never declared it their official goal to create a monetary union.

### 3.3 Latin America

33. As in Africa, the formation of a monetary union in Latin America is complicated by multiplicity of RECs which serve similar economic objectives. Vinals (2002) observes that the lack of a unique, well-defined regional economic integration project in Latin America in contrast with the European model makes the formation of a monetary union very difficult. He also notes that the juxtaposition of several sub-regional integration projects often with different levels of ambition - MERCOSUR<sup>10</sup>, Andes region, Central America, and others - has not been effective in promoting economic integration in the region.

<sup>10</sup> MERCOSUR is the Southern Common Market made up of Argentina, Brazil and Paraguay, and came into force in March 1991

**“A monetary union in Latin America is complicated by multiplicity of RECs, which serve similar economic objectives”**

### 3.4 East Africa

34. The East African Community (EAC) <sup>11</sup> aims to establish among Member States “a Customs Union, a Common Market, subsequently a Monetary Union and ultimately a Political Federation in order to strengthen and regulate the industrial, commercial, infrastructural, cultural, social, political and other relations of the Partner States to the end that there shall be accelerated, harmonious and balanced development and sustained expansion of economic activities, the benefit of which shall be equitably shared”. <sup>12</sup> The path to a monetary union is outlined in chapter 14 of the Treaty and include undertakings to cooperate in monetary and financial matters and maintain the convertibility of their currencies as a basis for the establishment of a Monetary Union, as well as harmonise their macro-economic policies especially in exchange rate policy, interest rate policy, monetary and fiscal policies.

#### Box 1: History of the East African Community

The EAC is a regional organisation comprising Kenya, Tanzania, Uganda, Burundi and Rwanda. Members of the EAC have a long history of economic cooperation, dating back to a customs union between Kenya and Uganda established in 1917, which Tanzania joined in 1922. An East African Currency Board issuing legal tender for the three countries was in existence from 1919 to 1965. Amidst severe unrest in the region, the precursor to the current EAC collapsed in 1977. More than two decades later, the current EAC was formally launched in 2001 with the goals of introducing a customs union (by 2010), common market and monetary union with a common currency (by 2012), and ultimately a political union – the East African Federation, with a common President, and a common parliament. Since 2005, members have implemented a common external tariff, but due to overlapping membership of other regional organisations such as COMESA (Burundi, Kenya, Rwanda, and Uganda) and SADC (Tanzania), exceptions have been made so that tariffs apply only to countries that are not members of these organisations.

*Source: adapted from IMF, 2009, “Uganda: Selected Issues” Country Report No. 09/37*

<sup>11</sup> Before 2007 EAC consisted of Kenya, Tanzania and Uganda. In 2007 EAC was expanded to include Burundi and Rwanda. In its expanded version the EAC has a total population of 126 million people.

<sup>12</sup> Article 5(2) of the *Treaty for the establishment of the East African Community*.



35. With the Customs Union now formally in place, the EAC is now moving to a Common Market in 2010. To this end, the EAC Secretariat is consulting with a broad spectrum of stakeholders, including the national central banks, ministries of finance, securities markets authorities, bureaux of statistics, bankers associations, private sector, the media and the civil society, with a view to ensuring that *“the whole process leading towards an East African Monetary Union is an all inclusive one so that the East Africans can fully own and spearhead the integration process.”*<sup>13</sup>
36. Moreover, the EAC has embarked upon a comprehensive study to review the convergence criteria of the region’s monetary frameworks, take stock of the current state of preparedness of each Member State and finally make proposals on the institutional framework and operational structure of the EAC monetary union. The EAC monetary union is scheduled for 2012 brought forward from the earlier target date of 2015.
37. It is unclear, however, whether the original fear of regional integration has been overcome, including the concerns of the smaller Tanzania of being overrun by bigger Kenya and Uganda. To be sure, some progress is being made to allay any lingering concerns through constant communication. For example, there are regular meetings now taking place on bank supervision matters, even though there is as yet no consolidated regional supervision of banks. Also, there is some progress on regionalising the capital markets with a MoU having been signed in 2007 by the three original EAC members on capital market regulatory authority that would ensure that smaller economies do benefit.
38. More work still needs to be done in EAC to reach its goal. In fact, the World Bank concluded recently that *“the EAC countries were not ready for a monetary union and currently do not meet the criteria of an ‘optimal currency area’”* (World Bank, 2007). For example, the payment systems in the community are not functional as yet, credit information is not shared, and legal frameworks are still divergent. Furthermore, other problems besetting other aspiring monetary unions are present in the EAC. These include its operations under the ‘rules of consensus’, meaning that no progress will be made if one member opts for absenteeism. The late arrival of Burundi and Rwanda has complicated the monetary integration process further because now some protocols have to be renegotiated. Finally, the EAC Secretariat lacks capacity and suffers from high staff turnover.

***“Some progress is being made to allay any lingering concerns through constant communication”***

<sup>13</sup> Source: EAC website <http://www.eac.int/component/content/301.html?task=view>

### 3.5 West Africa

39. To achieve its objective of promoting co-operation and integration in West Africa, the Economic Community of West African States (ECOWAS),<sup>14</sup> founded in 1975, seeks to establish “*an economic union through the adoption of common policies in the economic, financial social and cultural sectors, and the creation of a monetary union*”.<sup>15</sup> To realise its economic and monetary union ambitions, Article 55 of the ECOWAS Treaty says that:  
“*Member States undertake to complete within five years following the creation of a Custom Union, the establishment of an economic and monetary union through,*” among others, “*the harmonisation of monetary, financial and fiscal policies, the setting up of West African monetary union, the establishment of a single regional Central Bank and the creation of a single West African currency*”.<sup>16</sup>
40. ECOWAS has made some progress towards its monetary union goal. For example, the West African Monetary Agency was established in 1975 to promote trade in the sub-region by providing a payment mechanism for clearing and settlement of intra-regional transactions, and to encourage the use of national currencies in transactions. In 1987 ECOWAS further launched a Monetary Cooperation Programme that defined the process leading to the creation of a single monetary zone and the introduction of a common currency (World Bank 2007).
41. The formation of a Monetary Union was a response to a political commitment by ECOWAS Heads of States, who met in December 1999 in Togo to accelerate the pace of regional integration. In particular, the Accra Declaration on a Second Monetary Zone, signed in April 2000 by six non-WAEMU West African countries,<sup>17</sup> expressed their intention to establish a second common currency in the region by 2003 and to work toward a single currency for ECOWAS by 2004 (Masson and Pattillo, 2001). These six countries committed themselves to reducing central bank financing of budget deficits to 10 per cent of the previous year’s government revenue; reducing budget deficits to 4 percent of GDP by 2003; creating a Convergence Council to help coordinate macroeconomic policies; and setting up a common central bank. Their declaration states that “*Member States recognise the need for strong political commitment and undertake to pursue all such national policies as would facilitate the regional monetary integration process*”.

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<sup>14</sup> Made up of 15 countries, namely, Benin, Burkina Faso, Cape Verde, Cote D’Ivoire, The Gambia, Ghana, Guinea, Guinea Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo. ECOWAS has an estimated 240 million people.

<sup>15</sup> Article 3(2)(e) of the Treaty of ECOWAS

<sup>16</sup> Article 55(1)(iii) of the Treaty of ECOWAS

<sup>17</sup> Nigeria, Ghana, Sierra Leone, Liberia, Guinea, and The Gambia

42. For the entire ECOWAS region, there has however been limited progress on basic issues that define a monetary union. Exchange controls that limit financial integration and cross-border trade are still in place. Throughout the region cash remains the most popular medium of exchange and payment due to still undeveloped regional payment systems.<sup>18</sup> The deepening of regional financial markets is hindered by the lack of depth in individual countries. Some achievements on the harmonisation of bank supervision activities can only be discerned among sub-regions, but “*it is surely unrealistic to expect that ECOWAS will be able to move to common prudential norms in the area of capital adequacy in anything but the long term future*” (World Bank, 2007).
43. ECOWAS has done little to harmonise legal frameworks. It is only in the francophone zone where some success in this area is noted. On the development of credit information systems, the ECOWAS region is still in early stages of addressing the problems posed by a lack of credit reporting and financial information infrastructure. Unresolved regional taxation issues are hampering the development of sub-regional financial instruments on the region’s three main stock exchanges.<sup>19</sup> On net, a whole lot more is still to be done if ECOWAS is to be referred to as a genuine monetary union.

### 3.6 Europe

44. The European Union <sup>20</sup> seeks to “*promote economic and social progress which is balanced and sustainable, in particular through the creation of an area without internal frontiers, through the strengthening of economic and social cohesion and through the establishment of economic and monetary union, ultimately including a single currency in accordance with the provisions of this Treaty*”.<sup>21</sup> The Treaty and related protocols and agreements are elaborate documents that outline every stage of the process, indicating in minute details what roles the envisaged regional institutions will play, who will be responsible for what, and what the role of national institutions will be under the monetary union setting.

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<sup>18</sup> WAMZ and UEMOA are showing better progress than the entire ECOWAS region.

<sup>19</sup> Namely: the Nigerian Stock Exchange, the Ghana Stock Exchange, and Bourse Régionale des Valeurs Mobilières.

<sup>20</sup> Current 27 Member States are: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom. The candidacy of Croatia, Macedonia and Turkey is under consideration.

<sup>21</sup> Title I, Article B of the Treaty on European Union

45. The European model on financial integration shows that the road toward the formation of a monetary union is arduous and long, spanning several decades. The European Monetary Union is a culmination of an integration process that started nearly fifty years ago and which evolved gradually. The process started by fostering trade integration, then went on to financial integration in an environment of closer monetary cooperation, and then achieved a significant degree of economic convergence prior to the creation of monetary union.<sup>22</sup>

**“The EU model was not just a technical process but had economic, institutional and political dimensions”**

46. The EU model was not just a technical process but had economic, institutional and political dimensions. It was underpinned by a well-functioning bureaucracy and a supra-national institutional framework whose capacities were built over a long period of time. With respect to the African monetary union agenda, McCarthy (2008) wonders whether it would be appropriate for Africa, plagued as it is by capacity and resources constraints on many fronts, to adopt the European model in its regional market integration processes. On this basis, he concludes that monetary integration in African is unlikely to occur in the foreseeable future.

### 3.7 Some lessons for SADC

47. With the launch of a SADC free trade area in 2008 the region achieved one of the key milestones toward a monetary union. The planned customs union in 2010, may come before the FTA has been fully consolidated, raising questions about the tightness of the integration agenda. This is the first lesson that SADC can draw from other regions, namely: the road to a monetary union is long and non-linear. The linearity suggested by theory is not borne out in most cases. Member States should do what is politically, socially and economically feasible. It is important though to set targets and achieve them.

**“Member States should do what is politically, socially and economically feasible. It is important though to set targets and achieve them”**

48. Related to the above lesson, the second lesson is that not all potential Member States should be required to be part of the MU from the start. As the case with the EU, monetary unions are contingent upon Member States pursuing certain policies, reforming various institutions, demonstrating over a period of time through public support and political commitment that they are serious about joining a monetary union. Some of the reforms to pursue such as converging macroeconomic policies, harmonising financial policies and instruments, and building the requisite human and institutional capacities, may take a while among SADC Member States. In fact, some countries may choose to let the monetary union “*prove itself*” before they can consider joining, and may then join on a piecemeal basis based on national interests and concerns.

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<sup>22</sup> EMU and Latin America, Conference of Monetary Union, Paper by Jose Vinals, Banco de Espana and CEPR, 16-04-2002

49. Third, a framework that sets out the process is critical. As in the case of Asia (roadmap), EU (treaty) and West Africa (monetary cooperation program), having a Framework to guide the process is critical. Such a Framework should, *inter alia*, contain timelines, the sequencing of steps that will be followed; the assignment of responsibilities to various stakeholders and define accountable measures; and the establishment, in a consultative and comprehensive manner, of the roles that regional institutions will play in a monetary union. The formation of a monetary union requires detail and specificity in the following areas, *inter alia*, (i) identifying the objectives, policy rule, accountability, and degree of independence of envisaged regional institutions including the common central bank; (ii) allocating responsibility for bank supervision and lending of last resort; and (iii) establishing mechanisms and procedures for making national fiscal policies consistent with the union's monetary objective.

**“As in the case of Asia, EU and West Africa having a Framework to guide the process is critical.”**

50. Fourth, SADC should regard the existing blocs as building blocks rather than stumbling blocks. The ECOWAS case indicates that smaller groupings within the region can progress faster than the whole region. Therefore, SADC should start with the Southern African Customs Union (SACU) or CMA, which is arguably an optimal currency area (OCA)<sup>23</sup> and then expand to the rest of the region.

51. Consultations among all stakeholders are critical to the success of regional financial integration and to monetary union: it will be recalled that the EU member States had to continually seek public support through elections and referendums before embarking on key EU projects. East Africa's consultation process seems to be a start to marshal the overall support for the integration efforts. SADC may want to embark on this process sooner rather than later. This is more so, as a monetary union inevitably involves ceding national policy space to a supra-national organ.

**“Consultations among all stakeholders are critical to the success of regional financial integration and to monetary union”**

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<sup>23</sup> An OCA, a.k.a. an optimal currency region, is a geographical region in which it would maximise economic efficiency to have the entire region share a single currency. It is one where similarities between the economic structures of countries make it feasible to adopt a single currency. OCA should be an economic unit where factors of production are mobile and whose regions are affected symmetrically by shocks. Is SACU an OCA?

**“SADC must address candidly the concerns of smaller Member States”**

52. SADC must address candidly the concerns of smaller Member States: the East African case shows that countries concerned that they will bear the disproportionate costs of integration can stall or derail the whole regional integration agenda. Whether or not the fears are well founded, Member States should marshal the means to compensate smaller and poorer Member States to secure their continued support of the agenda.

# Central Bank Autonomy in a Regional Financial Integration Context

## 4.1 Introduction

53. This chapter is devoted to the central institution in the regional financial integration agenda, the strengthening of national central banks and the shape of a regional central bank to which national central banks will cede their monetary policy making authority. Central banks need special attention for another reason: they are the ones generally tasked to manage most of the key financial integration projects such as harmonisation of laws and practices in national payment systems and bank supervision. Thus a careful reform of national central banks, and proper establishment of a regional central bank are cardinal to the deeper regional trade, enhanced regional savings and investments, and, through these and other activities, to higher employment and poverty alleviation.

**“Central banks are the ones generally tasked to manage most of the key financial integration projects”**

## 4.2 Defining Central Bank Autonomy

54. Central Bank (CB) autonomy is defined in terms of a *mélange* of political, economic and informal factors (Mfunwa, 1998). Political or goal autonomy is determined by the relationship between the CB and government in the formulation of monetary policy. This includes the authority to choose the final policy goal (for example, inflation and/or level of economic activity), procedures for the appointment and the removal of CB directors.
55. A CB is considered more autonomous if the objective of price stability<sup>24</sup> features prominently in its legal charter. Accordingly, if it is stated that price stability is its main or only policy goal, then such a CB is judged more autonomous in this respect than a CB with multiple objectives, even if the latter are not inconsistent with the former. Notably, such a CB is considered more autonomous than one with other explicit objectives (e.g. full employment) deemed to be in conflict with the price stability goal.
56. Economic (or financial) autonomy refers to the financial and budgetary relationship between the CB and the government. The main areas of economic autonomy that are considered important for the proper operation of a CB, are clearly defined provisions for credit to the government, authority over exchange rate policy in certain instances, the financial condition of the CB, and adequate monetary instruments. A CB that enjoys autonomy from government would (i) be protected from government policies that would limit the CB’s authority over monetary poli-

<sup>24</sup> Price stability refers to an economic condition in which price changes do not affect the decisions of economic agents

cy, (ii) control its own balance sheet, and (iii) have adequate means to manage the level of liquidity in the banking system and can affect key money market rates necessary to achieve its targets.

57. The informal determinants of CB autonomy include turnover of governors, credit to the government and political instability. Briefly, the more turnover of CB governors coincides with the turnover of government, the less autonomous the CB is considered to be, and vice versa. Political instability may work both ways however: an incumbent likely to lose an election may develop an apolitical CB to restrict the range of actions of the opposition when it comes to office. On the other hand, *“when the degree of polarisation is above certain threshold, the incumbent’s desire to use all available institutions to fortify its hold on power would tend to reduce CB independence.”*<sup>25</sup>

58. Several studies suggest that a high level of informal CB independence, as opposed to legal, or formal, CB independence is a pre-condition for macroeconomic stability in developing countries (Presnak, 2005). This is more so in the context of Africa where many CBs have no formal autonomy in their legal charter but are deemed autonomous. Ultimately, granting CB autonomy is a political decision, and whether or not a CB will enjoy a *de jure* autonomy it may have, hinges critically on political leadership’s, and the general public’s, willingness to allow such autonomy to thrive.

**“Regional CBs tend to enjoy an explicit *de jure* and *de facto* autonomy, adopting a stricter version of CB autonomy to insulate the institution from national governments’ interference”**

59. From a regional perspective, regional CBs tend to enjoy an explicit *de jure* and *de facto* autonomy, adopting a stricter version of CB autonomy to insulate the institution from national governments’ interference. In this regard, the regional CB objective tends to have a singular objective, gets assurances of apolitical appointment of key managers and directors, and enjoys other tight safeguards against interference. An example of a strict clause that assigns such autonomy is Article 7 of the Protocol on the Statute of the European System of Central Banks and of the European Central Bank (ECB), which states that:

*“...neither the ECB, nor a national CB nor any member of their decision-making bodies shall seek or take instructions from Community institutions or bodies, from any government of a Member State or from any other body. The Community institutions and bodies and the governments of the Member States undertake to respect this principle and not to seek to influence the members of the decision-making bodies of the ECB or of the national CBs in the performance of their tasks...”*

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<sup>25</sup> Mfunwa 1998, *ibid*



### 4.3 Justification and Modalities for Central Bank autonomy at Regional Level

60. Central banks in a sub-regional context are an important vehicle for achieving a monetary union through financial integration. As strategic institutions at the pinnacle of the financial sector, national CBs should strive to harmonise their financial instruments, policies, regulatory regimes and frameworks in order to strengthen their capacity to deliver on good economic governance. There is, therefore, a need for collaborative efforts couched in regional policy dialogue and actions between and among national CBs to support regional financial integration.
61. National CBs, in a number of monetary unions, have used a plethora of policy instruments to support regional financial integration. With a strong political and public backing, these national CBs have taken measures to harmonise their policies and approaches in their management of interest and exchange rates; definition and combating of inflation; ascertaining appropriate levels of reserve ratios; conducting bonds, equities and loans issues; and in their management of other matters under the purview of CBs. Once again, the efficacy of their actions depends on the degree of autonomy that each CB enjoys *vis-à-vis* government control.
62. Importantly also, advanced monetary unions have established supra-national or regional central bank designed to oversee the monetary policy and implementation in the Community, as well as the activities of national CBs. In fact, the Delors Report on EU monetary union argues that “*a single monetary policy is an inescapable consequence of monetary union and constitutes one of the principal institutional changes*” (Delors Report, 1989) (authors’ emphasis). The Report further elaborates on the new regional CB’s role, saying:
- “A new monetary institution would be needed because a single monetary policy cannot result from independent decisions and actions by different central banks. Moreover, day-to-day monetary policy operations cannot respond quickly to changing market conditions unless they are decided centrally”.*<sup>26</sup>
63. In this new monetary union setting, the regional CB would be responsible for formulating and implementing monetary policy as well as managing the community’s exchange rates *vis-à-vis* third currencies. The role of the national CBs would be subservient to that of the supra-national CB, and they will be “*entrusted with the implementation of policies in conformity with the guidelines established by the [regional CB decision-making body] and in accordance with the instructions from the central institution*”.<sup>27</sup>

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<sup>26</sup> Delors Report, *ibid*

<sup>27</sup> Delors Report, *ibid*

**“For regional CB and national CBs to earn their political and public support and thus earn their autonomy, they need to be governed by rules of good governance”**

64. An international norm is that the supra-national CB should be granted full autonomy to conduct monetary policy. Indeed, this is not only the feature of the European System of Central Banks, but also of the two supra-national central banks in Western and Central Africa, where the latter two’s independence has benefited from the existence of a fixed exchange rate rule and from the associated constraints in the expansion of credit to governments (Sacerdoti, 1991). Legal and regulatory frameworks governing national CBs have harmonised, as necessary, their mandates with that of the regional CB, stating explicitly their autonomy and price stability objective.<sup>28</sup> This requirement protects national CBs from having to finance government spending.<sup>29</sup>

65. To conclude, for regional CB and national CBs to earn their political and public support and thus earn their autonomy, they need to be governed by rules of good governance. In this regard, they need to be accountable and transparent in their activities. As a starting point, sustaining their autonomous status should be made subject to the pursuit and achievement of policies that are broadly acceptable to the general public and their representatives in parliament.

66. In this regard, CBs would have to work hard to get rid of the public perception that they are secretive organisations, operating behind closed doors, and not always in the interest of the respective nations as a whole. Hence, they should conduct monetary policy independently but with due regard to the economic conditions of the Member States. After all, *“a political decision to grant CB autonomy to a greater or lesser extent should be aimed at improving the management and administration of government affairs”*.<sup>30</sup> As part of accountability, the CB should be required, posited on clearly stated objective, to prepare reports on monetary policy performance, and be subject to well-specified sanctions in the event of non-performance. The entire regional central bank system should also be accountable and transparent with respect to its operations, including on staff remuneration, procurement processes, and appointment of external auditors and reporting obligations to Parliament.

**“A political decision to grant CB autonomy to a greater or lesser extent should be aimed at improving the management and administration of government affairs”**

<sup>28</sup> All European countries aspiring to join the EU were required to grant autonomy to their national CBs before these banks could join the European System of Central Banks. All of them now contain explicit reference to their autonomous status (see <http://www.ecb.int/ecb/legal/1341/96647/html/index.en.html>).

<sup>29</sup> It is well to note, however, that this measure is insufficient to prevent fiscal imprudence as *“individual governments have had large recourse to external assistance”* (Sacerdoti 1991, *ibid*)

<sup>30</sup> Mfunwa 1998, *ibid*

#### 4.4 Contribution of autonomous Central Banks to regional financial integration

67. The potential benefit for SADC of autonomous regional central bank system (both the supra-national CB and the national CBs) in the context of Regional Financial Integration (RFI) is largely the same as elsewhere. In particular, the CB autonomy in the manner described above should contribute to the RFI by reducing, somewhat, the bias toward monetary expansion because fixing the exchange rate between MU members reduces the scope for any one member to employ 'beggar-thy-neighbor' monetary policies.
68. Moreover, such autonomous status may solve credibility problems that bedevil some of the existing central banks. As for fiscal discipline, African countries have a history of high inflations largely due to the diversion of spending and taxes to purposes that do not reflect social needs. These diverted funds "*may just serve the private objectives of the government in power, which may tolerate corruption as a way of rewarding its supporters, for instance*" (UNECA, 2005). If so, establishing a regional central bank that is independent and exerts greater discipline over fiscal policies than national central banks, do may enable it to become an agency of restraint.
69. The CB autonomy can, however, only succeed if supported by other institutions and arrangements and does not emerge directly from monetary union alone, as mentioned above. It further helps that peer pressure may instill fiscal discipline. To be sure, a disciplined country would not want a MU with a country that had much less disciplined fiscal policies since the latter would cause the regional CB to produce higher inflation, with consequences on the first country's welfare.
70. Considerable controversy will, however, surface given that shocks would impact economies (especially those of SADC countries) differently from time to time (that is, the so-called 'asymmetry of shocks'), raising questions about political viability of a strictly autonomous central bank. Here, the composition of the MU is crucial. A country would not want to join a MU with another country facing very different external shocks—for example, to its terms of trade—at least if that country was large enough to matter. The issue for debate will be how Member States will manage this eventuality, and what other reform measures (on trade, infrastructure development, and other areas) are needed to minimise the 'asymmetry of shocks' among the Community member countries.

## 4.5 SADC activities to reform central banks

71. A snapshot of current governance situation of SADC central banks, depicted in Annex 1, indicates that presently, the CB laws, especially prior to year 2000, do not contain an autonomy/independence clause. Of the 15 SADC Member States, only 7 of them (Angola, Congo DR, Mozambique, Mauritius, Seychelles, South Africa, Tanzania) contain an independence clause either in CB law or constitutions. It is noteworthy that revisions to CB laws after 2000 in the case of Mauritius (2004), Mozambique (2003), and Seychelles (2004) have been progressive, while that of Lesotho (2000) has chosen not to incorporate the independence clause.
72. In various forms, virtually all national CBs have price stability as the primary objective, albeit it is one of many objectives in the majority of SADC Member States. Admittedly, the accompanying objectives cannot be deemed inimical to the objective of price stability. Nonetheless, ambiguities may arise about what is meant exactly by phrases such as “*consistent with the government’s economic policy*” (Mozambique). What if the government seeks to achieve a certain employment level, a goal that may be inconsistent with the price stability objective?
73. Only with the exception of the Congo DR, all SADC national CBs laws allow credit to government with various restricting conditions. It may well be that even though the laws allow this, a number of Member States may have refrained from exercising their legal prerogative in this regard. Still others may have over-stretched it, especially where there are ambiguities, and during elections. The exemplary case of the Congo DR comes from lessons of past hyper-inflations in that country, and hence a received wisdom that the fact that a government can force the CB to print money does not mean that it should. As the move towards MU gains momentum, Member States are likely to revisit this area as it is critical to endeavors to restore and maintain macroeconomic stability.
74. With only a few exceptional cases, (Swaziland, Zimbabwe) all national CBs determine their own budgets, approved by their boards of directors. As discussed in the previous sections, this is an area that governments may use to influence the activities of a CB by say, depriving it of resources to punish it for not following cue from politicians. It may also be noted that since members of the Board are largely appointed by the Head of State and/or Prime Minister or Minister of Finance, a determined government will still exert its influence on a CB.
75. Finally, in all Member States, the members of the Board of Directors, including governors and their deputies, are appointed by the Head of State, in line with practices in most international CBs. South African Reserve Bank, with private shareholders, is an exception to the rule in the ownership of central banks around

the world. In terms of this peculiar ownership structure, of the 14 directors of the SARB, seven are elected or appointed by private shareholders.

76. Given these differences, there is scope for convergence among national CBs' legal and operational frameworks through the adoption of international best elements in central banking. Accordingly, the CCBG Legal and Operational Steering Committee finalised the draft Framework to enhance consultations and co-operation between CBs and Ministries responsible for National Financial Matters. A draft Model Central Bank Bill as well as the Green Paper have also been finalised and were approved by Governors in April 2008. In its explanatory note, the February 2009 draft version of the SADC Model Central Bank Law seeks to:

*“...promote the adoption of general principles, which will facilitate the operational independence of SADC central banks, create clear standards of accountability and transparency.... These key principles are also essential for the achievement of harmonised legislation and the establishment of a regional SADC Central Bank”.*

77. It is the central principle of the draft that the national CBs must be so constituted as to be independent of the political authorities and other influences that would compromise their main objective of achieving and maintaining price stability. In section 5 it states that *“the [national CB] is independent and, in pursuit of its primary objective and in the performance of its functions under this Act, shall act without fear, favour or prejudice or direction from any person, authority or institution.”*
78. As a corollary of this principle, schedule 4 of the draft asserts the independence of the national CBs' decision-making bodies, protecting them against *“any political influence in the performance of their duties.”* For an even higher safeguard, Member States are encouraged to amend their Constitutions to *“provide for the Bank's political and economic autonomy, taking cognisance of the necessary Bank's accessibility to Government where relevant.”* Section 72 makes it an offence for any person to interfere with the independence of the banks or *“who influences another person to interfere in the operations of the Bank.”*
79. Another key improvement being introduced by the SADC CB Law, which will also enhance the independence of national CBs, is to encourage a single primary objective, that is, *“to achieve and maintain price stability”* (section 4). The general support given to the country's other economic sectors is secondary to this primary objective.
80. Unlike in many other monetary unions, section 41 of the draft law still allows overdraft and other credit facilities in favour of governments. This is a surprise as

this lending has been a source of price instability all over the world and in some Member States of SADC, and is in direct conflict with the primary objective of the envisaged national CB. In a footnote to the section, this anomaly is explained: “*The SADC region recognises that the best practice is to prohibit lending to Government. However, the circumstances of the region currently dictate otherwise.*” It remains to be seen how many Member States will eventually follow the example of the Congo DR by proscribing lending to government altogether.

81. The other elements contained in the draft follow current practices. These include appointment of the Board of Directors, including the Governors by the Head of State, and the right of national CBs to determine their own budgets approved by the Board. However, there is a new innovation in that the Draft SADC CB Law requires that the parliament ratifies the executive’s nominee for the bank governor, as opposed to current practices where the executive, primarily the Head of State, has an unfettered prerogative over such an appointment. This innovation will indeed ensure “*participation by the public and transparency and openness of the process*” (section 11(1) (b)).
82. More on the good governance being introduced by the draft law, in order to balance the independence assigned to national CBs, section 64 calls on the governor to “*appear before Parliament at least twice a year and at any other time as Parliament or the Governor may request, to report on the current operations and affairs of the Bank.*” Furthermore the governor and members of the Board and of the MPC are required to sign an oath declaring integrity in carrying out their duties, while employees need to sign the oath of professional secrecy in dealing with sensitive information of the bank.
83. On net, the draft SADC Central Bank Law is a vast improvement to existing national CB laws. If emulated, or even strengthened, by Member States it will serve as a launch pad to a regional central bank law, with tightened elements that will greatly contribute to regional financial integration and to the SADC Monetary Union.

# Bank Supervision

## 5.1 Definition

84. Broadly, bank supervision can be referred to as the act of monitoring the financial performance and operations of banks in order to ensure that they are operating safely and soundly and following rules and regulations<sup>31</sup>. In this study, bank supervision refers to the role of central banks in providing oversight functions on all financial and non-financial institutions that fall directly under their purview. The bank supervision task entails taking care of the financial system's health, implemented through on-site and off-site inspections of the banks and non-banking financial institutions authorised to operate in a given territory<sup>32</sup>. Among others, bank supervision has also the function of analysing requests for licences to operate as financial institutions in the territory.
85. From a regional perspective, bank supervision entails developing a comprehensive Framework to guide and coordinate all activities relating to sound supervision and regulation. Such a Framework should have monitoring and evaluation mechanisms to facilitate easy reporting of progress. There should also be a higher-level authority or a supra-national body to ensure that international norms, codes and practices on sound bank supervision are complied with by all Member States.

***“There should be a supra-national body to ensure that international norms, codes and practices on sound bank supervision are complied with by all Member States”***

## 5.2 Modalities to harmonise bank supervision at regional level

86. Although the focus of this study is on the SADC region, it is worth noting that sufficient amount of work has already been done under the COMESA region in the area of regional bank supervision. For instance, the Fourth Summit of the COMESA Authority of Heads of State and Governments, which took place in Kenya in May 1999, decided that heads of banking supervision units should meet at least once a year to review and exchange ideas on banking supervision and make necessary recommendations.
87. Accordingly, the first meeting of bank supervisors was held in April 2001 during which the importance of safety and soundness of financial intermediaries was stressed, especially in view of increased financial liberalisation, and the need for all COMESA countries to improve bank supervision and regulation following initiatives to strengthen prudential regulation and supervision, bank governance, and market discipline. A COMESA Banking Supervision and Harmonisation Framework is now in place.

<sup>31</sup> [http://www.bc.gov.cu/English/bank\\_supervision.asp](http://www.bc.gov.cu/English/bank_supervision.asp)

<sup>32</sup> [http://www.bc.gov.cu/English/bank\\_supervision.asp](http://www.bc.gov.cu/English/bank_supervision.asp)

88. In another meeting, central bank governors agreed that in order to have a harmonised approach to bank supervision, a sub-committee should be set up to make proposals on the harmonisation of bank supervision and regulation. In this respect, the COMESA Secretariat would provide the necessary assistance and together, they would review Bank Supervision and Regulation Systems in COMESA; assess compliance with the 25 core principles for effective Banking Supervision developed by the Basel Committee on Banking Supervision and propose a harmonised approach to banking supervision for the COMESA region. The sub-committee was mandated to carry out a list of tasks over the short, medium and long-term.
89. Given that a lot of progress has already been achieved in this area, SADC should build on what COMESA has done in regional bank supervision by rationalising and harmonising its own work with that of COMESA for optimal results. This will ensure that the human and other forms of resources are prudentially applied and thus cut down on transaction costs associated with parallel programmes.

### **5.3 Contribution of harmonised regional bank supervision to regional financial integration**

90. The World Bank (2007) and the AfDB (2008) argue that multi-country regulation and supervision may be more efficient and, as a result, increase financial system stability while rigorous standards for financial reporting improve the transparency of financial institutions and instill confidence in the solvency of the system. The World Bank further states that bank supervision at a regional level has the potential to generate economies of scale in technology and the use of highly skilled human resources. A sound regulation and supervision of financial markets has a potential to attract capital from investors that would otherwise be deterred or ask higher returns from markets which lack transparency and where the enforcement of prudential norms is uncertain or inconsistent.
91. Thus, strong supervisory and legal enforcement frameworks provide the means for supervisors to correct instances of poor governance, and supply investors with the tools to exercise control over the institutions they own (World Bank, 2007). Indeed, good laws and regulations provide a framework for governance, transparent and accurate financial reporting and provide investors and regulators with an enhanced ability to determine if an institution is well governed and compliant with laws and regulations.
92. Although there is a COMESA Banking Supervision and Harmonisation Framework, mentioned above, its implementation is hampered by lack of capacity, both human and material across Member States. This is one area where SADC and COMESA could team up to build and enhance capacity if bank supervision



and regulation are to be effective in their respective sub-regions. In addition, there is need to enhance information flow between the region and national institutions charged with bank supervision.

#### **5.4 SADC activities to harmonise bank supervision laws and practices**

93. Article 10 of the SADC FIP urges Member States to “*facilitate co-operation between (amongst) regional banking supervisors and the harmonisation of banking supervisory standards and practices*”. In pursuit of this mandate, the CCBG established a (SADC) Sub-committee of Banking Supervisors (SSBS), which then compiled a MoU on Cooperation and Coordination in the Area of Banking Regulatory and Supervisory Matters. Much work of the SSBS has spanned areas of training and risk-based supervision, anti-money laundering issues, implementation of international accountancy standards, and harmonisation of banking supervision legal and regulatory reforms.
94. The latest annual reports of CCBG indicate that much has been achieved in this area. Heads of central bank banking supervision departments hold annual meetings to deal with regional banking supervision matters, share experiences, and ascertain progress in the implementation of regional targets. Frequent seminars and workshop are held by bank supervision officials on various issues, including on BIS Basel II.
95. A project on the compilation of country reports on the status of implementation of the international standards is already being carried out, in which Member States’ compliance with issues such as anti-money laundering and combating the financing of terrorism are being assessed.
96. The region has developed and verified financial soundness indicators, which are based on the IMF’s Compilation Guide on Financial Soundness Indicators.<sup>33</sup> These indicators, developed with a view to building a regional database, monitor the current financial health and soundness of the financial institutions in a country, and of their corporate and household counterparts.

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<sup>33</sup> See the 2007/2008 CCBG Annual Report.

97. The finalisation, due by December 2006, of a regional Framework for Bank Supervision as an Annex to FIP remains outstanding. On the other hand, cross-cutting issues such as training of personnel and ICT issues are ongoing. For example, on the latter, a Bank Supervision Application has been developed and finalised to support harmonised bank supervision processes in SADC central banks. Some central banks (*e.g. Banco de Moçambique*) have implemented the project.

# Harmonising Regional Payment Systems

## 6.1 Definition

98. A payment system encompasses all payment-related activities, mechanisms, institutions and users. *“The term national payment system thus refers to payment systems in the widest context and is not restricted to the operational and infrastructural aspects only”* (SADC, 2009).

## 6.2 Modalities to harmonise regional payment systems

99. A central bank is ultimately responsible for ensuring the overall soundness of a national payments system. It normally carries out this responsibility in collaboration with the banking industry, both of whom will accept joint responsibility and accountability for the smooth functioning of national payment systems.
100. There are certain pre-conditions suggested for a successful payment system integration process. First, this process must start with a broad-based and forward-looking business case for integration of national payment systems and well-specified objectives, constraints and expectations. Second, there should be harmonisation of key institutional and structural elements in participating national systems. Finally, a sustainable stakeholder commitment is crucial.
101. Regional payment mechanisms are said to require: (i) a greater standardisation and centralisation of clearing and settlement processes for intra-regional payments; (ii) settlement liquidity concentrated around fewer currencies – possibly a single currency; and (iii) a higher level of coordination among national payment systems and often among monetary or exchange rate policies. As in the case of regional bank supervision, there should, therefore, be a regional coordinating clearing and settlement agent.

## 6.3 Contribution of harmonised regional payment systems to regional financial integration

102. In addition to contributing to deeper intra-regional trade, harmonised regional payment systems are also central to regional financial integration. According to the World Bank (2002), they:
- Strengthen the financial sector and its support to the economic development of the region, including by reducing the clearing time for cheque payments;

***“This process must start with a broad-based and forward-looking business case for integration of national payment systems and well-specified objectives, constraints and expectations”***

***“In addition to contributing to deeper intra-regional trade, harmonised regional payment systems are also central to regional financial integration”***

- Facilitate economic and trade relations in the sub-region by helping avoid risky and costly transportation of large amounts of cash, while providing fast, secure, easy and low-cost payment instruments in each country and in the sub-region;
- Develop the supply of basic banking services (payments, remittances and small credits) to a significant share of the population, including the low income segments;
- Increase the efficiency and safety of payment mechanisms available to governments, businesses and the general population by promoting electronic payment instruments and electronic exchange of transactions. In particular, the costly and manual process of using cash for the payment of salaries, pensions, utilities services, etc., will be transformed into electronic processes.
- Facilitate the implementation of regional monetary policy. This is facilitated by the centralisation of the liquidities of financial institutions in a single account at the sub-region level and the real time processing and accounting of large value transactions;
- Support the development of the financial market and the swift and safe settlement of securities transactions. The new system's infrastructure should be designed in such a way as to permit a linkage with financial markets, once established, to provide for swift and safe settlement of all kinds of securities transactions; and
- Build a comprehensive and consistent payments system infrastructure that complies with international standards and in particular with the BIS CPSS Core Principles.

#### **6.4 SADC activities to improve and harmonise regional payment systems**

103. The SADC Payment System project was launched in 1996 to assist individual SADC countries define a domestic payment strategy, development and implement reforms, as well as to define a co-ordinated regional approach for cross-border payments. These measures should consider implications on trade, central bank policy, and foreign exchange positions and control. The project vision wants each SADC country to have an efficient and effective payment system that is internationally acceptable and that would ultimately be interlinked within the region to support the SADC aims of free trade.

104. The approach to modernisation adopted by the SADC Payments System project team (the project team) was a pure strategic approach, where the modernisation of the payment systems was based on vision and strategic development within each individual country that would be followed through to implementation to meet the needs of the respective countries (*see for example the case of Zambia in Box 2 below*).
105. The project team played a facilitating role in the process. The strategic process included the formal launch of the project followed by a sensitisation workshop in which all stakeholders were involved, an information gathering and stock-taking process, the formulation of the vision and strategy, the conceptual design, business process specification and technical specifications, leading to a procurement or development process for identified solutions and finally implementation, thereof, in the individual countries.
106. In the procurement development and implementation phases, a joint request for proposal was developed according to common requirements, and bids were sought from vendors. The project team facilitated the analysis and selection of vendors. In the selection of vendors, time, cost and strategic requirements were used as criteria. The outcome of this process was a recommendation of two vendors to the CCBG that could be used by involved Member States.
107. The individual countries were responsible to procure and implement their Real-Time Gross Settlement (RTGS) systems. The project team facilitated training workshops and courses on clearing, payment system principles, strategic management and business analysis during the entire process. Training sessions at the time were recorded on video and distributed to the countries for further information sharing.

## Box 2: Model Payment Systems Act: Impact in Zambia

The SADC Payment Systems Project developed a model Payment Systems Act in 2002 for use by member countries in developing their own Payment System Legislation. This model Payment Systems Act was to a large extent used by the Bank of Zambia in developing the National Payment Systems Bill. The key areas of the model Payment Systems Act which were incorporated in the Bill include the following:

- Granting of authority to the Bank of Zambia to regulate/oversee the payment system;
- Providing for the finality and irrevocability of settlements;
- The requirement for a winding up order for any participant in the payment system to be delivered to the Bank of Zambia;
- Protection of netting of payment obligations in the event that a participant is subsequently wound up; and
- Safeguarding of collateral provided by a participant in a payment system for use for settlement purposes where such collateral is provided prior to issue of the wind up order.

The National Payment Systems Bill was subsequently enacted into Law in April 2007 and was operationalised in June 2007.

108. To keep the broader payments community informed on the progress of the projects, the project team publishes its annual newsletter, *Vulindlela*, on the CCBG website. The team also published a SADC Guide to Developing a Strategic Framework for Payment Systems Modernisation on BIS website.
109. The project team has over the past ten years held annual regional conferences. These conferences discuss current trends in the global payments environment, common regional payment issues, and set out the programme for the project's

activities for the following year. Participants at these annual conferences are payment system representatives from the central banks in the region, commercial bank representatives and other stakeholders in the region, and international experts who provide a global perspective. Individual countries have been required, after a period of operation of their RTGS systems, to carry out self assessments on their payment systems based on international standards such as the BIS Core Principles for Systemically Important Payment Systems (SIPS).

110. The project team continuously interacts with relevant international bodies and ensures the region adopts international best practise. These bodies include the World Bank and BIS. The project team has made contributions towards the development of the SIPS publications “General Guidance for NPS Development”, “SIPS” and “Core Principles for SIPS”.
111. The project team is currently focussed on the integration of the region’s payment systems and the development of the cross-border settlement system. It does also have shorter-term focus areas. These areas relate to the evolving nature of the payments environment and to immediate regional issues, including collecting and publishing accurate payment system statistics for the region, developing adequate oversight of the payment systems in the individual countries, capacity building, mobile payments, and worker remittances. At this stage, three SADC countries have still not implemented RTGS systems. These are the Democratic Republic of Congo, Madagascar, and Seychelles. The project team would schedule visits to Seychelles and Madagascar to hold sensitisation workshops and review their progress in the course of 2010.
112. At its meeting in May 2009, the CCBG gave the project team its approval to proceed with the design of the SADC settlement system and with the SADC payments system integration project. However, the project team has not yet met with the payment systems leaders of the individual SADC countries to map out the payment systems integration project. A workshop in this regard, with the individual country (payment system) leaders, will be held in early 2010. At this workshop, teams comprising the country leaders will be identified to address the different aspects of the integration. The teams will be required to interact with role-players in the region to develop the various components. It needs noting that the payment system integration project has no definite procedures, processes or infrastructure at this stage.
113. With regards to regional cross-border settlement, the programme will be influenced by the region’s goals of a single currency and a single SADC Central Bank (by 2018). Accordingly, the design of the regional settlement system will be based on a single currency, and payment transactions in the SADC region will be settled

at a central location on a single system. The need for correspondent banking to facilitate transactions between SADC countries will, therefore, fall away.

114. The SADC payment system integration project and the implementation of the SADC cross-border settlement system is aligned with the SADC dates. The payment system project is scheduled for completion in 2018. This could be extended if the approach is to include countries in the system in phases. However, a shortage of funds could stymie faster implementation of the work scheduled for completion in 2010. The project team has had most of its operational work funded from two World Bank grants in the past. However, this funding has now over the last five years dried up. The project team has again submitted an application recently.



## Securities Markets

### 7.1 Definition

115. Securities markets are defined holistically to include money and capital markets. These markets comprise stock markets, pension funds, and other financial services such as banking and insurance. From a regional perspective, the aim is to develop the securities markets in SADC so that they can enhance the sub-region's ability to mobilise private resources in support of the sub-region's development (UNECA, 1997).

### 7.2 Modalities for unifying securities markets in SADC

116. Technological advances have made it easier to link the operations of securities markets (Honohan and Beck, 2007). As explained in the next sub-section, if the time is not ripe for a general liberalisation, limited forms of liberalisation – allowing for example, long-term investments by approved institutional investors – can be a viable halfway measure. Technical, legal and administrative efforts are required for governments to establish and maintain a jointly controlled and fully integrated multilateral regional exchange, suggesting that it may be wise to adopt a less costly step-by-step approach towards a regional exchange.
117. Furthermore, in order to achieve regional economies of scale, liquidity and risk pooling, out-sourcing of some services to a common service provider may be more effective than insisting on building a new, jointly-owned multinational provider. For example, back-office clearing and settlement services might be efficiently provided to a number of different exchanges by a single entity, even if those exchanges remained otherwise unlinked. Hammering out common regional software and technology standards might be unnecessary when satisfactory existing standards can be taken off the shelf.
118. Experiences from other regions show that the use of linked trading platforms across several countries can be envisaged even if regulation and supervision remains national. A small country could exploit the existence of a well-functioning exchange in a larger neighbour (for example, South Africa and Kenya), thereby bringing the advantages of better technology to the home market at lower costs. This hub-and-spoke approach is much less demanding of political and administrative coordination than the multilateral approach, and it could be seen as a potentially promising path toward wider market integration. Furthermore, this approach can be designed in such a way as to prevent the danger of medium-size companies from poorer countries getting lost among the numerous listings on the larger exchanges.

***“The aim is to develop the securities markets in SADC so that they can enhance the sub-region’s ability to mobilise private resources in support of the sub-region’s development”***

However, it does nothing to restrain the dominance of a smaller number of exchanges, which can seem unattractive for non-economic reasons.

119. Cross-market listings in different countries are another, more limited, alternative to full regionalisation. Such listings are already being tried, for example, with the cross-listing of Nairobi-based East African Breweries and Kenya Airways in Dar-es-Salaam and on the Uganda exchange. An available alternative for larger companies seeking a wider and more liquid market is simply to cross-list on a large international exchange, whether that of Johannesburg or elsewhere. The use of this option will certainly continue to grow.

### 7.3 Contribution of unified securities markets to regional financial integration

***“Organised securities markets could play a key role in facilitating the flow of long-term and risk finance from institutional investors to productive enterprises”***

120. Organised securities markets could play a key role in facilitating the flow of long-term and risk finance from institutional investors to productive enterprises in manufacturing, agribusiness, services, utilities, and house buyers. By forming multi-country regional markets, existing exchanges could expand their volume of business and the number of market participants.
121. Benefits could flow from this expansion: (i) larger markets are more likely to gain from the vertical and horizontal integration of services and products; (ii) regional securities markets could provide larger economies of scale and increase firms’ access to debt and equity; and (iii) from an investors’ perspective, regionalisation would ideally offer opportunities to diversify risk by allowing investment in a wider range of instruments and debt and equity issuers.
122. Cross-border cooperation and technology transfer can be helpful, especially if they help contain operating and regulatory costs (for example, inevitable fixed costs of establishing a simple, small trading platform are very high). Cross-listing (as a first step towards eventual integration) can allow issuers to access a wider pool of investors. Therefore, the main operating advantage of integrating the functioning of securities market is to improve liquidity on an hour-to-hour and day-to-day basis.
123. Commentators have argued that in the African context, however, it is not clear how much would be gained by pooling all the smaller African securities markets, as the result would still be a small and illiquid market. They further argue that, exchange controls currently in place between participating countries would eliminate most of the short-term liquidity advantages. Therefore, any proposal for regional securities exchanges must deal effectively with exchange controls and other restrictions on cross-border investments in securities. These restrictions are, in any event, often imposed for policy and political reasons that trump the objectives of securities market integration.

## 7.4 SADC activities to harmonise regional securities markets

124. Annexure 11 of the SADC FIP outlines the steps to be taken by Member Exchanges to build and enhance cooperation and to communicate and coordinate their efforts for their mutual benefit and that of the sub-region. Therefore, in order to facilitate the unification of regional securities markets, SADC has developed an action plan that addresses the following issues:

- Requirements for licences and approvals in respect of broker-dealer and investment managers: establish the requirements for licences and approvals in respect of broker-dealer and investment managers within member countries with the view to coming up with minimum requirements in the SADC region.
- Listing requirements: develop minimum requirements for companies raising capital (listing requirements) in the SADC region.
- Prospectus requirements: develop minimum prospectus requirements for the SADC region.
- Collective investment schemes: develop minimum requirements for the licensing of collective schemes in the SADC region.
- Code of conduct: develop a code of conduct for broker-dealers and investment managers for the SADC region.
- Central Securities Depository (CSD) participants: develop minimum requirements for licensing/approval of participants in the SADC region.
- Formal qualifications for brokers-dealers, investment managers and compliance officers: develop minimum qualification requirements for the SADC region.

125. Issues regarding the unification of regional securities markets in SADC are being handled by the Market Development Sub-committee of the Committee of Insurance, Securities and Non-Banking Financial Authorities (CISNA). In 1997, a Committee of SADC Stock Exchanges (COSSE) was established “*with a strategy to keep autonomous national markets and explore ways of using technology, skills-sharing, dual-listing and cross-border investment within the region to facilitate financial integration.*”<sup>34</sup>

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<sup>34</sup> See 2006/2007 CCBG Annual Report.

126. The work programme of COSSE incorporates;<sup>35</sup> first, the harmonisation of listing requirements. Here, the committee has finalised a review of the potential benefits for harmonising listings requirements, using the Johannesburg Securities Exchange Limited's (JSE) listing requirements as a base comparing these with the other regional exchanges. It is now up to each COSSE member to assess the recommendations resulting from the review and decide what to implement, considering individual needs. Second, the COSSE has been tasked to come up with a list of requirements for the integration of SADC exchanges, including investigating and developing a suitable model of interconnectivity of stock exchanges.

127. The FIP also provides for closer cooperation in the development of money and capital markets, the CCGB established a Financial Markets Sub-committee in 2008. This Sub-committee will contribute to the development of regional financial markets and encourage cooperation among members. Some of the activities the organ intends to undertake in the SADC region include the following:

- The promotion of sovereign credit rating;
- The improvement and harmonisation of market infrastructure;
- The facilitation of the increased availability of instruments in financial markets and financial innovation;
- The development of market trading practices that are in line with international best practices;
- The development of knowledge and skills on the use of alternative financial instruments;
- The development and harmonisation of regulation of financial instruments;
- The development of capacity in liquidity forecasting and reserves management;
- The development and broadening of the investor and issuer base in the domestic markets; and
- The establishment of a Credit Information Bureau.

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<sup>35</sup> See 2006/2007 CCBG Annual Report.

# Corporate Governance

## 8.1 Definition

128. The basic principles of corporate governance are: transparency, accountability, fairness, independence, discipline and sound responsibility in all aspects (social, economical, ethical, environmental, etc.). Corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed, administered or controlled. Corporate governance also includes the relationships among the many stakeholders involved and the goals for which the corporation or institution is governed.
129. From a broader regional perspective, SADC RISDP defines good economic and corporate governance in terms of sound macroeconomic management; transparent public financial management and accountability; first-class banking supervision and financial regulation; and rigorous, best practice corporate governance. The RISDP places a high premium on accountability and transparency coupled with enforcement of internationally accepted codes and standards as the hallmark of good corporate governance.

***“The RISDP places a high premium on accountability and transparency coupled with enforcement of internationally accepted codes and standards as the hallmark of good corporate governance”***

## 8.2 Modalities to unify corporate governance principles and practices at regional level

130. To “account” entails (i) providing full information about one’s actions and (ii) responding to concerns about one’s actions (Lefort, 2006). For a central bank to account, for example, it must explain and justify its actions and decisions made in the execution of its responsibilities. In this case, Lefort <sup>36</sup> argues that the central banks’ accountability responsibilities should be ‘diversified’ to include accounting to national parliaments, as well as subjecting central banks’ acts and decisions to judicial reviews to ensure their legality.
131. Continuing with the example of central banking, whose corporate governance structures would as appropriate be applied to other national and supra-national organisations, such a regional central bank law should prescribe monetary goals and targets so that Member States can be held accountable for their performance and actions. The mandates and objectives of national central banks in the sub-region would be aligned with those of the regional central bank. Importantly, these mandates and objectives should be communicated well so that citizens understand them. This understanding would then enable people to hold a regional monetary authority (or the regional system of central banks) accountable.

<sup>36</sup> Lefort 2006, ibid

132. Transparency entails providing, at all times, sufficient information to enable the public understand that, for example, the central bank's actions match set monetary policy objectives. In general therefore:

*Transparency refers to an environment in which the objectives of policy, its legal, institutional and economic framework, policy decisions and their rationale, data and information related to monetary and financial policies and the terms of agencies' accountability, are provided to the public in a comprehensive, accessible and timely manner.*<sup>37</sup>

**“SADC ICT Forum allows central banks to exchange vital information on issues of accountability and transparency in their quest to improve the governance of the institutions”**

133. In a number of central banks across the sub-region, there are mechanisms through which these institutions provide information about their actions to the general public. For instance, a number of central banks hold media briefings, have interactive websites and publish bulletins, which provide different pieces of information about their activities. There are also innovative platforms such as the SADC ICT Forum that allows central banks to exchange vital information on issues of accountability and transparency in their quest to improve the governance of the institutions.

### **8.3 Contribution of harmonised corporate governance practices to regional financial integration**

134. There is some shared understanding that the unification of the region's economies through the SADC free trade area and the quest to achieve deeper levels of integration will not be realised in the absence of good economic and corporate governance. Without doubt, there are benefits to be derived from the principles of transparency and accountability. An important benefit of transparency is that it earns the national and regional institutions the public trust that is necessary to forward the regional integration agenda. Accountability and transparency increase the public's confidence and credibility — two essential ingredients for sound central bank policy-making, for instance. Transparency allows decisions to be better informed, while better accountability imposes firmer discipline on decision-makers. Together, they will contribute to higher-quality decisions in the proposed regional institutions in the SADC region.

### **8.4 SADC activities to harmonise corporate governance practices**

135. Economic and corporate governance is a cross-cutting area that should be mainstreamed in virtually all SADC integration efforts (see box 3). As the move towards a monetary union, more transparency and accountability should be embedded in all decisions and projects. For example, the process of shaping the

<sup>367</sup> Lefort 2006, *ibid*

envisaged regional institutions should receive public feedback. There should be no confidential matters, including the shape of the envisaged regional central bank. Bringing 'fait accompli' decisions and policies just for the citizens' information will earn the integration process neither support nor endorsement nor induce the regional cohesion that is envisaged in the SADC founding documents.

### **Box 3: Corporate Governance Efforts by SADC Countries**

#### **Individual Efforts**

Zambia has, through the Financial Sector Development Plan (FSDP), been making efforts to address matters of corporate governance in the financial sector. In this regard, Zambia has been developing a corporate governance code and corporate governance guidelines for the financial sector. The Corporate Governance working group of the FSDP has already prepared a draft sector-wide code which awaits approval by the FSDP Steering Committee.

#### **Regional Efforts**

SADC countries have developed a FIP. The FIP has been developed as a tool for achieving regional integration through the harmonisation of financial and investment policies in Member States. One of the objectives of the FIP is the promotion of SADC as an attractive investment destination leading to increased levels of domestic and foreign investment in SADC.

Already, the SADC CCBG has developed a Model SADC Central Bank Law aimed at harmonising the legal and operational frameworks of SADC central banks. Issues of Good Corporate Governance have been taken into account through the provisions in the Central Bank Model Law drafted by the CCBG. The Model Law embodies the key principles that are contrived to promote the adoption of general principles which will facilitate the operational independence of SADC central banks, create clear standards of accountability and transparency in the legal and operational frameworks of central banks. The long term objective is to promote the principles of operational independence, transparency and accountability that will form the cornerstone for a future regional central bank in SADC

136. This secrecy appears to permeate the SADC integration activities. The processes seem to be the preserve of central banks, banks and ministries of finance with virtually little media commentary and civil society participation.



## Inter-Central Bank Communication

### 9.1 Rationale for institutionalised communication mechanisms among monetary authorities

137. The need for regional collaboration among the SADC Central Banks is seen as an important spur to improve ICT infrastructure that will contribute to financial sector development.

### 9.2 Modalities to boost inter-central bank communication at regional level

138. SADC central banks have therefore, decided to look at the feasibility of implementing a regional collaboration platform and Wide Area Network infrastructure to inter-connect the 14 SADC Central Banks. The initial cost indication of the project proved to be expensive and was subsequently put on hold by the CCBG. However, the IT Forum recommended that in the meantime, individual central banks will proceed to make improvements to their internal infrastructure such as by implementing video conferencing while the IT Forum would establish a collaborative approach for the development of uniform standards for video conferencing.
139. The SADC central banks IT Forum had also embarked on the IT Governance (ITG) project aimed at implementing the Control Objectives for Information and related Technology (COBIT) framework. All central banks have received the necessary training and implementation is at varying stages.
140. Through collaborative efforts, the IT Forum developed and maintains an application for bank supervisors - the Bank Supervision Application (BSA) with a support office in Mozambique. The application has gone through several revisions. Currently, the BSO is developing BSA version 3.0 and the portal for support.
141. The IT Forum is engaged in the development and implementation of the framework for business continuity management (BCM). The IT Forum is currently working on a checklist to guide the ICT directors on the ICT component of BCM.

### 9.3 Some benefits of enhanced inter-central bank communication flows

142. The IT Forum supports the SADC Central Bankers website and a project has been initiated to upgrade the site. Occasionally the Forum organises customised courses for its members through the SADC Training Committee. These courses are aimed at providing a skill-base within the region from which member countries can source for needed human resources for consultancy thereby, reducing consulting costs.
143. All processes of RFI need to be communicated to wider societies to ensure that there will be no backlash at the end of the process. Most SADC RFI activities are conceived, implemented and finalised in secrecy. Participants are restricted to the executive (governments, central banks), to some extent the financial sector, and international financial institutions (BIS, IMF, WB). Far less effort is expended to engaged national parliaments, as a conduit for civil society participation. There is thus a danger that work could unravel later on when citizens start impugning some decisions taken on their behalf. This could also happen when political leadership, seeking to renege on agreements, may invoke the ‘need to consult constituencies’ at the implementation stage.

***“All processes of RFI need to be communicated to wider societies to ensure that there will be no backlash at the end of the process”***

### 9.4 SADC activities to improve inter-central bank communication

144. The SADC Central Banks IT Forum (the Forum) holds annual conferences during which a progress review is made on information and communication technology (ICT) projects, update the ICT component of the RISDP and discuss different ICT disciplines, such as business continuity and security, as well as start planning for SADC Central Banks ICT architecture to ensure inter-operability between different systems between central banks. An important feature during the conference is a presentation by each member central bank’s ICT infrastructure update. This enables member states to harmonise infrastructure technologies and applications where possible.
145. The Forum embarked on a project to harmonise the software licences for commonly used applications. To this end, a project on ICT Software Group Licence was initiated culminating in the signing of the memorandum of understanding (MoU) with Microsoft in September 2008. The Banco de Moçambique signed the MoU with Microsoft on behalf of SADC central banks. The MoU enables central banks to access Microsoft licences at government level of pricing. Negotiations with Reuters and Oracle were ongoing as follows:

- Reuters – General Reuters observed that the collective subscription rate in the central banks was below the minimum requirement for Group Volume Licensing discount. A new survey has therefore, been instituted to collect the required up-to-date information; and
- Oracle – A survey was conducted in all central banks to establish the extent to which Oracle products were used. The information gathered had been transmitted to Oracle and feedback was awaited.

146. In conclusion, Member States may want to consider compiling a mapping of current communication flows (meetings, exchanges, etc.) of the actors in the financial system within countries and between countries. This will enable them to identify possible ways for future communication and coordination; that is apart from the technicalities of RFI knowing where and when the crucial decision are likely to be taken.

***“Member States may want to consider compiling a mapping of current communication flows of the actors in the financial system within and between countries to identify possible ways for future communication and coordination”***

## Capacity Building

### 10.1 Introduction

**“Member States should address the special needs of poorer members not only in human resource area but also in financial and infrastructure areas”**

147. Capacity building in the context of regional financial integration is another cross-cutting matter addressed in all focus areas dealt with in previous chapters, and will be critical to the success of the SADC monetary union and a regional central bank. Human-resource is central to the operationalisation of all the frameworks put in place so far and those slated for completion at a later date. The ongoing sharing of information in the form of workshops, seminars, training or secondment of personnel should be enhanced.

148. Member States should address the special needs of poorer members not only in human resource area but also in financial and infrastructure areas. Here, SADC could enroll the participation of the regional private sector and international development partners to leverage on the technical know-how and financial resources to deliver on key capacity building areas.

### 10.2 Capacity building efforts in the CCBG activities

**“Building capacity within Member States is an ongoing exercise that has been mainstreamed in all focus areas”**

149. Building capacity within Member States is an ongoing exercise that has been mainstreamed in all focus areas discussed. Taking into account the importance of an integrated and systematic approach for the training and development of central bankers in the region, the CCBG has approved a project to coordinate training for central bank officials in SADC, and has created a Training and Development Forum. This Forum’s Steering Committee was established in 1998 “to coordinate, provide, promote and facilitate human resources development in central banks of the SADC region, through the optimum use of resources.”<sup>38</sup> Projects under this area are hobbled by lack of funding.

150. The central banks in SADC have over the years established regional capacity building institutions which include the following:

- The SADC Training and Development Forum under the CCBG: The aim of this Forum, whose Secretariat is at the South African Reserve Bank, is to implement training programmes for member countries. Activities so far including training that was provided to about 40 Bank of Zambia employees in the following areas:
  - Anti-money Laundering
  - Research Methodology

<sup>38</sup> See 2007/2008 CCBG Annual Report.

- Financial Stability & Reports
- Financial Markets Fundamentals
- Payments Systems
- Monetary Policy
- Bank Supervision
- Talent Management
- Executive Development
- Business English for Non English speaking countries
- Project Management
- Information Technology Governance
- Macroeconomic & Financial Institute Management for Eastern & Southern Africa (MEFMI): MEFMI is a thirteen-member regional body comprising Angola, Botswana, Kenya, Lesotho, Malawi, Mozambique, Namibia, Rwanda, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe. The aim of MEFMI is to build sustainable capacity in identified key areas in ministries of finance, planning commissions and central banks, or equivalent institutions. MEFMI strives to improve human and institutional capacity in the critical areas of macroeconomic and financial management; foster best practices in related institutions; and bring emerging risks and opportunities to the fore among executive level officials. MEFMI seeks to achieve, within its member states, prudent macroeconomic management, competent and efficient management of public finances, sound, efficient and stable financial sectors and stable economies with strong and sustained growth. The long-term objective is to contribute to the poverty reduction process among people in MEFMI's operational zone of the Eastern and Southern Africa.

MEFMI also offers a competitive fellows development programme to employees who demonstrate ability in specialised areas. Over the past five years, a total of 150 Bank of Zambia employees have undergone various MEFMI capacity building programmes in a number of areas including the following:

- Domestic Debt Management
- Domestic Debt Market Development & Management
- Data Requirement for Economic Management
- Economic Modeling & Forecasting

- Monetary Policy Operations
- Fiscal Policy & Management
- Foreign Exchange Reserves Management
- Eastern & Southern African Management Institute (ESAMI): ESAMI is a Pan- African regional Management Development Centre owned by ten (10) member countries: Zambia, Zimbabwe, Swaziland, Mozambique, Namibia, Malawi, Tanzania, Uganda, Seychelles and Kenya. ESAMI offers management development programmes, consultancy, education services and management research. The aim of the courses offered by ESAMI is to strengthen management capacities and engender best practices  
A total of 160 employees from the Bank of Zambia have undergone various management development programmes including post graduate courses. The following are some of the broader areas of ESAMI capacity building programmes that the Bank has participated in:
  - Environmental Management
  - Transport and Logistics
  - Management Development
  - Information Technology

151. The need to develop ICT skills in the region is recognised. An initiative to assess the status of ICT skills in SADC central banks has been started and a strategy has also been completed to improve these skills. Due to resource constraints, the role of international development partners has been, and will continue to be, critical in certain key areas. Already, the World Bank, through its International Development Fund, is involved in the compilation of the Model National Payment Systems Act. The International Labour Organization (ILO) is also involved in the promotion of micro-business in the region, including gathering data on micro-finance in the SADC region. The ILO's involvement will expand to assist in the development of a framework to regulate this sector and render technical assistance to SADC central banks on how to monitor micro-finance activities.<sup>39</sup>

152. As the process of SADC financial integration is not an isolated one, efforts are made to align the region's efforts with continental and other regional areas to share ideas and for mutual learning. In this regard, the CCBG supports the African Action Plan and other programmes of New Economic Partnerships for Africa's Development (NEPAD). Cooperation with the EAC is being nurtured. Accordingly,

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<sup>39</sup> See 2002/2003 CCBG Annual Report.

the East and Southern Africa Banking Supervisors Group (ESAF) has been reporting on its banking supervision activities at the CCBG meetings, including on such matters and anti-money laundering efforts

153. As the CCBG structures are necessarily becoming more and rather unwieldy in light of numerous areas needing focused attention, the cooperation among the CCBG sub-structures is increasingly becoming important. In this regard, the CCBG developed the Rules of Engagement framework to guide the relationship between itself and the SADC Banking Association (SADCBA), for example. This serves to encourage sharing of ideas and dialogue in areas of mutual interest, and to resolve conflicts.

## Summary and Conclusions

### 11.1 Summary of issues

154. This paper has noted that the SADC region has made some notable progress towards its goal of a monetary union. This goal is congruent with the continental goal of using various RECs integration achievements as a building block towards an African Monetary Union and a continental single currency. The continent therefore, proffers a resounding endorsement to SADC regional financial integration efforts.

155. SADC's regional unity seeks to enable Member States to leverage on one another's strength and to overcome disadvantages of small populations, tiny geographical areas and lack of access to sea routes. In addition to nurturing a SADC based on democratic principles, it also aims to build economies of scale, deepen intra-regional trade, induce regional self-reliance and eradicate extreme poverty in the long term. The objectives and strategies towards monetary union and an introduction of a single currency in the sub-region are succinct and have received embrace across the region.

***“The timetable towards a monetary union in 2016 and a single currency in 2018 is however proving increasingly tight”***

156. The timetable towards a monetary union in 2016 and a single currency in 2018 is however proving increasingly tight as Member States contemplate the vast amount of work still to be done. The latitude to adjust SADC's timeframe is further constrained by the African monetary union, slated for 2015. In this regard, this paper has suggested that SADC Member States need to reflect how best to fulfill their obligations in the next seven years, assuming that the set dates are 'cast in stone'. This reflection will greatly benefit from an overarching Framework for Regional Financial Integration to guide each step of the way towards a SADC single currency.

157. Experiences from other regions indicate that this Framework is critical to defining the process leading to the creation of a single monetary zone and the introduction of a common currency. By compiling it, Member States would be seeking to have a clear understanding of the opportunities available and the challenges they face, as well as see the resource gap, which may need external support. The Framework should further set out criteria for measuring progress towards full regional financial integration, capturing all issues of financial policies, financial infrastructure, and financial institutions. Finally, it should contain key milestones and timeliness up to the launch of the monetary union and the single currency.



158. If the proposed Framework is developed and diligently followed, potential Member States need to be aware that they do not need to be all founding countries of the monetary union. Indeed, in many monetary union differences in countries mean that other Member States can join later as they develop requisite institutions and capacities, while others may wish to 'wait and see' if there are benefits accruing from the monetary union for those already inside. However, as many Member States as possible should be part of the launch to give credibility to the process. Hence, concerted efforts should be expended to ensure a state of readiness of as many SADC countries as possible.
159. Much work has been done to set up institutional structures to take decisions and implement projects that inject life to the SADC vision for regional financial integration. Necessarily, these structures have to be numerous to accord ponderous attention to minute and complicated financial integration focus areas. As outlined in this paper, some of these areas are: central banking, banking supervision, and national payment systems. Cross-cutting areas include harmonisation of legal frameworks and regulations across the region, adherence to uniform corporate standards, developing and retaining human resource skills that support the sub-region's political and technical needs.
160. In terms of achievements so far, the reform of the pinnacle institutions for regional financial integration, namely central banks, has attracted the attention it deserves. The draft SADC Model Central Bank Law contains most of the international best standards in modern central banking. Undoubtedly, this law will unify and modernise the diverse national central bank laws, the majority of which lack the disciplining autonomy clause. However, Member States may wish to rescind the provision, and even actively proscribe the practice, that allows central banks to extend credit to governments lest the effectiveness of the strong independence clauses of the law is undercut.
161. Regional central banks have done commendably well to modernise national payment systems with virtually all Member States (except the Democratic Republic of Congo, Madagascar, and Seychelles) having adopted the RTGS systems. Besides advancing regional financial integration, modernised national payment systems will make the implementation of a regional monetary policy possible. These systems will also be important spurs to deeper regional trade and easier convergence of banks in the region. Finally, a SADC Guide to Developing a Strategic Framework for Payment System Modernisation and a model National Payment Systems Law have been completed and published. Some SADC countries (for example, Zambia), have amended their related national laws accordingly.

**“There is need to inject some haste in developing various frameworks and model laws in a number of other focus areas, as outlined in the SADC TIFI programmes.”**

162. The harmonisation of bank supervision is ongoing, but there are delays in developing the Framework for Bank Supervision as an annexure to the FIP, as planned in the SADC Trade, Industry, Finance and Investment (TIFI) operational plan of 2006/07. Vast structural differences (such as the still undeveloped banking systems in some countries and advanced ones in others) among Member States in this area threaten to upend the legal and regulatory harmonisation plans if not addressed forthwith. SADC countries further need to attend to the cost implications of complying with international best practices. The salient issues of corporate governance and the fight against money laundering are a critical part of bank supervision. Given the global nature of the latter issue, the SADC global approach to dealing with it is wise.
163. The work on cross-cutting areas such as on human skills and ICT is moving swiftly, even if it is contingent on resource availability. Therefore, in this specific area, private sector participation and the sustained support of international partners are important. There is need to inject some haste in developing various frameworks and model laws in a number of other focus areas, as outlined in the SADC TIFI programmes. Some were slated for completion as far back as 2006, but progress remains anemic. These include the frameworks for exchange control policy, financial and capital markets development, and monitoring and surveillance mechanism.

## 11.2 Key outstanding issues

**“The recent trend in central banks is for these institutions to attempt to lift the veil of secrecy associated with monetary policy-making”**

164. Lessons culled from Europe’s integration processes leading to the European Union indicate an extraordinary length of time is needed to secure political buy-in to complete the monetary union. Such a political buy-in is buttressed by popular participation, not only on broader integration issues but also on the shape of the institutions to which all nationalities will cede sovereignty. The question for SADC is whether or not democratic processes are fully entrenched and mainstreamed into the regional financial integration agenda. There is little indication that this is the case.
165. To be sure, the various model laws ought to be debated in national parliaments before being imported into domestic laws. This imperative begs more questions: if these model laws are indeed debated in parliaments, how open, to the general public, are these debates? And, do national parliaments invite non-state actors to proffer opinion? The recent trend in central banks is for these institutions to attempt to lift the veil of secrecy associated with monetary policy-making. In SADC, the regional Model Central Bank Law was never subjected to public scrutiny before it was finalised. Indeed, the entire process so far has been done in the inner sanctum of the executive (various government ministries and central banks), some selected private sector participants (mostly banks) and international financial institutions.

166. In sum, there is an urgent need to pierce the opacity of the regional financial integration process in the SADC region. The regional financial integration agenda in SADC needs to entrench good governance to ensure popular awareness of the process in order to secure regional ownership and support. This calls for encouragement of debates and an active search for public opinion. Transparency of the process is critical to public participation. If draft national laws are often subjected to heated public debates, then surely, those at regional level should not be allowed to stray from this democratic tack. Getting public support on regional policies and programmes, also has a buffering power against narrow political whims of the day. Lacking political will, incumbent leaders may sabotage the process by belatedly 'seeking constituent approval' as a way of evading politically unpalatable integration decisions. Finally, constant communication of the integration agenda can help assuage the fears of short-term costs of integration, especially if this communication is characterised by candor.

***“There is an urgent need to pierce the opacity of the regional financial integration process in the SADC region”***

### **11.3 Issues for further consideration**

167. This paper does not claim to have all the answers to questions and challenges that the regional financial integration process imposes. Nor does it claim to address all pertinent issues related to the establishment of a monetary union. It merely flags some of the issues that could be considered for incorporation into a regional Framework to systematically guide the process towards a monetary union. Importantly, it further draws the attention of policy-makers to the fact that regional financial integration is not a mere technical issue to be resolved and finalised behind closed doors, but rather should be adopted in an inclusive approach to ignite regional enthusiasm, and promote legitimacy and ownership. The regional financial integration process must embrace the good governance properties of a transparent process, leadership accountability, and popular participation and inclusiveness all of which should be mainstreamed in the agenda. The Framework should therefore, mainstream this participatory element in the entire process

168. Finally, since this paper is only a start, a number of forums will be set up to take the proposition of the SADC Framework on Financial Integration further. For example, in an *Ad Hoc* Expert Group Meeting on this subject, which took place in Johannesburg from November 19th to 20th 2009, the experts were requested to consider issues highlighted in this paper. The experts were further requested to suggest the roles that various stakeholders could play in the regional financial integration agenda. Some of these stakeholders are individual Member States themselves, the SADC Secretariat and other regional organisations, the non-state actors such as the civil society and trade unions, and international co-operating partners. By these efforts, it is hoped that the proposal will reach key decision making process of the SADC.

# ANNEXURE 1

## SADC CENTRAL BANKS: SELECTED GOVERNANCE ISSUES

Central Bank	Date established	Current Governing Legislation	De jure autonomy?	CB main or principal or primary objective	Law allows credit to government	CB sets own budget?	Appointment of Governors & Directors
Banco Nacional de Angola (BNA)	1976	Organic Law of BNA No. 6/97	Yes. “...The independence of the BNA is guaranteed by the Organic Law (4/91), reviewed by the Law (06/97)...” (www.sadcbankers.org)	“...the main objectives of MP in Angola, consistent with the goal of the Govt’s economic policy, are to achieve stable national currency unit, & stability...”	Yes. “...The BNA must grant Govt up to the amount of the Govt deficit as approved by the Parliament...” (www.sadcbankers.org)	Yes; own Board approves	President appoints Governors & Deputy Governor; the Cabinet appoints 3-5 General Directors on the Board
Bank of Botswana (BoB)	1 July 1975	BoB Act 19 of 1996	No. - “...the Bank shall have & may exercise all the powers generally conferred upon a CB [sic]...” - Section 4(2). - BoB “...has considerable	The BoB shall “...first & foremost... promote & maintain monetary stability, an efficient payments mechanism &	Yes. “...the Bank may grant temporary advances to Govt subject to repayment within 6 months following the end of the FY in	Yes; own Board approves	President appoints Governor & Deputy Governors; MoF & Devt Planning appoints other 7 members of Board
Banque Centrale du Congo (BCC)	30 July 1951	BCC Law 005/2002	Yes. - The BCC Law ensures “...the independence of the Bank in its implementation of the MP...” - “...This independence is further strengthened	“The ultimate objective of the MP in the DRC remains the control of inflation, so as to facilitate the stability & external value the ” (www.sadc bankers.org)	No. The BCC Law strictly prohibits “...advances or any other form of loan by BCC to the State, its administrative branches & Govt-owned organizations or	??? “... ”	President appoints Governor, Deputy Governor & 5 Directors

Central Bank	Date established	Current Governing Legislation	De jure autonomy?	CB main or principal or primary objective	Law allows credit to government? Law allows nî credit to government	CB sets own budget?	Appointment of Governors & Directors
			by article 176 of the Constitution... (www.adcbankers.org)		enterprises... (www.sadcbankers.org)		
Central Bank of Lesotho (CBL)	1980 - MA 1982 - CB	CBL Act 2000	No. "The CB enjoys a fair amount of independence in formulating & implementing MP" (http://www.centralbank.org.ls/about/default.htm)	"...The objective of the Bank is to achieve and maintain price stability... Section 5 of CBL Act 2000	Yes. CBL "...make advances on overdrafts & loans to the Govt on such terms as the Board may determine..." to be "...repaid within 93 days from the end of the Govt's FY to which it relates..." Section 42 of CBL Act 2000	Yes. CBL "... has its own budget for purposes of its operations..." (www.sadcbankers.org)	The King appoints Governor & Deputy Governors; MoF appoints other Directors
Banque Central	1973	1994 BCM Act No. 94-004	?? [Statute in French] "...Once macroeconomic objectives are set [with Govt], the CB defines, in all independence, the implementation strategy of MP..." (www.sadcbankers.org)	"...new statute of BCM and its main objective as to ensure internal & external stability of the national currency..." ariary...	Yes. "The Bank ...has the legal power to grant advances to the Treasury within the limits defined by its status..." (www.sadcbankers.org)	???	President appoints Governor, Deputy Governors
Reserve Bank of Malawi (RBM)	23 July 1964	RBM Act 1989	No. "...the RBM Act of 1989 provides for full independence [sic] of the bank in the areas of MP & the issuance of Malawi " currency..." www.sadcbankers.org)	Act lists 10 principal objectives, incl. "to maintain external reserves as to safeguard the international value of the Malawi currency," Part III (c)	Yes. The RBM "...may make short-term advances to the Govt in respect of temporary shortfalls in budget revenues..." Section 40 of RBM Act 1989	Yes; own Board approves	President appoints Governor, Deputy Governors & other Board members

Central Bank	Date established	Current Governing Legislation	De jure autonomy?	CB main or principal	Law allows credit to government	CB sets own budget?	Appointment of Governors & Directors
Bank of Mauritius (BoM)	August 1967	BoM Act 2004	Yes. “...Subject to this Act, the Bank shall, in the pursuit of its objects, perform	“...to maintain price stability & to promote orderly & balanced omnic development...” Part II(4)(1)	Yes. “...the Bank may grant advances to the Govt to cover negative net cash flows of the Govt at such rate as may be agreed with the Govt...” Section 58 of BoM Act 2004	Yes; own Board approves	The President appoints Governor & Deputy Governors; MoF & Econ Devt appoints other Directors
Banco de Moçambique (BM)	17 May 1975	Law No. 1/92 (January 2003)	Yes/No [What does Portuguese law say?] “...The independence of the BM is guaranteed by Law No. 192....” (www.sadcbankers.org)	“..The main objective of the MP... consistent with the goal of the gov't economic policy, is to reduce inflation...” (www.sadcbankers.org)	Yes. “...the CB is allowed to extend credit to the Govt to an amount not exceeding 10% of Govt's ordinary revenue collected in the previous 2 years...” (www.sadcbankers.org)	?	President appoints Governor & Deputy Governor; Prime Minister appoints other Board members
Bank of Namibia (BN)	1 August 1990	BN Act 15 of 1997	No. “...The BN operates as an independent & autonomous institution, accountable to the Govt & the People of the Republic of Namibia...” (www.sadcbankers.org)	Act lists 5 objects of BN, incl. “...to foster monetary, credit & financial conditions conducive to the orderly, balanced & sustained economic development of Namibia...” Section 3 (c)	Yes. BN“...may grant loans to the Govt on such terms & condition as the Board & the Minister may agree upon, but every such loan shall be repaid to the Bank within 6 months from the date on which the loan in question was granted...” Section 43 of BN Act 15 of 1997	?? “...The financial relationship between the Govt & the Bank are defined in a MoU...” (www.sadcbankers.org)	President appoints Governor, Deputy Governor & Board members

Central Bank	Date established	Current Governing Legislation	De jure autonomy?	CB main or principal	Law allows credit to government	CB sets own budget?	Appointment of Governors & Directors
Central Bank of	1978 - MA 1983 - CB	CBSc Act 12 of 2004	Yes “...The Bank shall, in discharging its functions, act independently & no person shall seek improperly to influence the Board or any of the Bank’s officers or employees, in the discharge of his or her functions or interfere in the activities of the Bank...” Section 3(2) of CBSc Act 12 of 004	Act lists 7 objectives of CBSS, incl. “...to promote price stability & the maintenance of both domestic & external value of the Seychelles currency...” Section 4 (b)	Yes; “to be repaid within 6 months after the end of the FY...” Section 40 (3)	Yes; own Board approves	President appoints Governor, Deputy Governor & Board members
South African Reserve Bank (SARB)	1921	SARB Act 90 of 1989	Yes. SARB shall “... perform its function independently & without fear, favor or prejudice, but there must be regular consultation between the SARB & the Cabinet member responsible for national financial matters...” Section 224(2) of RSA Constitution 1996	“The primary objective of the Bank shall be to protect the value of the currency of the Republic in the interest of balanced & sustainable economic growth in the Republic.” Section 3 of SARB Act 1989	Yes; SARB may not “...hold in stocks of the Govt of the Republic which have been acquired directly from the Treasury by subscription to new issues, the conversion of existing issues or otherwise, a sum exceeding its paid-up capital & reserve fund plus 1/3 of its liabilities to the public in the Republic...” (Sec. 13(1), SARB Act)	Yes; own Board approves	President appoints Governor, Deputy Governors & 3 other Directors; Shareholders appoint or elect 7 other Directors

Central Bank	1973 - MA 1979 - CB	Current Governing Legislation	De jure autonomy?	CB main or principal	Law allows credit to government	CB sets own budget?	Appointment of Governors & Directors
Central Bank of Swaziland (CBSw)	1973 - MA 1979 - CB	King's Order-in-Council 1979	No. “... There is no specific law guaranteeing independence. Functionally, the bank falls under the Ministry of Finance, but has its own structure which is independent of	The CBSw mission is “To contribute to Swaziland’s national economic development through promotion of monetary stability & by fostering an environment which ensures a	Yes. The CBSw “... does not directly extend any form of credit to the Govt, but on certain occasions, it does hold govt securities & Treasury bills & also allows for limited overdrafts to govt...” (www.sadcbankers.org)	? “... Clause 3(2) of the MA Order gives the bank Statutory powers;	King appoints Governor; MoF appoints Deputy Governor & 5 other Directors
Bank of Tanzania (BoT)	1966	BoT Act of 2006	Yes. “... In the pursuit of its objectives & performance of its tasks, the Bank shall be autonomous & accountable ...” Section 5(3) of BoT Act	“The primary objective of the Bank shall be to formulate, define & implement MP directed to the economic objective of maintaining domestic price stability conducive to a balanced & sustainable growth of the national economy” Section 7(1) of BoT 2006	Yes. “...the Bank may, for the purpose of offsetting fluctuations between receipts from the budgeted revenues & payment of the Govt, purchase, hold & sell negotiable stocks, bonds or similar debt obligations or other securities issued by the Govt which shall bear interest at such market rate as determined by the Bank & which mature not later than 12 months from the date of issue...” Sect 35	Partial. President sets Governor’s & Dep. Governors’ remuneration; MoF approves Board members’ allowances; Board determines staff conditions of employment (Sections 14 & 15 of BoT Act)	President appoints Governor & Deputy Governors; MoF appoints 4 non-executive Directors; 2 other Directors are highest ranked public officials



Central Bank	Date established	Current Governing Legislation	De jure autonomy?	CB main or principal	Law allows credit to government	CB sets own budget?	Appointment of Governors & Directors
Bank of Zambia (BoZ)	1965	BoZ Act 43 of 1996	No.	“The Bank shall formulate & implement monetary & supervisory policies that will ensure the maintenance of price & financial systems stability so to promote balanced macro-economic development...” Section 4(1) of BoZ Act	Yes. BoZ may advance funds to Govt “...in special circumstances & on such terms & conditions as may be agreed upon between the Bank & the Minister.” Section 49 of BoZ Act	Yes. “...The Bank has its own budget & decides on its own finances...” (www.sadc bankers.org)	President appoints Governor & 2 Deputy Governors; MoF appoints other Board members
Reserve Bank of Zimbabwe (RBZ)	1964 - NB of Rhodesia 1980 - RBZ	RBZ Act of 1964	No. The RBZ “...enjoys a limited degree of autonomy with which it performs its statutory functions...” (www.sadc bankers.org)	The primary goal of RBZ is “... the maintenance of the internal & external value of the Zimbabwean currency. In this regard, the Bank is responsible for the formulation & implementation of MP, directed at ensuring low & stable inflation levels. ( <a href="http://www.rbz.co.zw/about/functions.asp">http://www.rbz.co.zw/about/functions.asp</a> )	Yes. The RBZ “...makes short-term advances to Government...” (www.sadcbankers.org)	No. MoF “... determines the budget of the Reserve Bank...” (www.sadcbankers.org)	President appoints Governor, 3 Deputy Governors & ≤ 7 Board members

**Abbreviations:** CB = Central Bank; MA = Monetary Authority; MP = Monetary Policy; NB = National Bank; MoF = Minister of Finance; Govt = Government; FY = financial year

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## Annexure 2

### **A Workshop on Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence Framework for Regional Financial Integration in SADC.**

**19-20 November 2009, Johannesburg, South Africa**

#### **Report**

### **Background**

It is now less than a decade before the SADC becomes a Monetary Union. According to SADC's RISDP, the overarching goal of the Community is to attain a monetary union through the creation of a regional central bank by 2016 and adoption of a single currency by 2018 in a systematic and progressive manner. In the SADC region, the increasing interest and momentum for the creation of a monetary union revolves around two main considerations.

In supporting this effort, the UNECA-SA, based in Lusaka, Zambia has worked closely with the Secretariat of the SADC CCBG on a study to gauge progress, highlight hurdles and suggest solutions towards the SADC monetary union and a single currency. The study is also part of the UNECA-SA and SADC multi-year programme to improve the governance of financial institutions, and harmonise their legal frameworks and operational activities.

The aim of the study is to encourage SADC to develop an overriding Framework for Regional Financial Integration that would solidify the integration process. It will display all distinct processes of regional financial integration in a logically consistent format, sequencing key milestones and including timelines for each step of the way. Indeed, experiences from other successfully integrated regions show that such a Framework should be comprehensive, covering financial policies and the development of suitable infrastructure and institutions. The Framework will also set out the key criteria for measuring progress towards integration.

UNECA-SA and the CCBG see enormous benefits from such a Framework for SADC. It would identify slippages in the implementation of the various programmes and projects in a timely manner and allow for corrective measures. Some areas where countries have previously faced difficulties include; (i) inadequate support at the national level for the integration process, (ii) a dearth of human and technological

***“The aim of the study is to encourage SADC to develop an overriding Framework for Regional Financial Integration that would solidify the integration process”***

resources to implement some of the technical aspects, and (iii) the presence of weak regional policies and procedures. Indeed, a detailed Framework could identify resource requirements for each of the stages, and measures to assist resource-poor Member countries.

**“The proposed Framework would strongly encourage Member States to adopt a participatory approach to regional financial integration”**

The proposed Framework would strongly encourage Member States to adopt a participatory approach to regional financial integration. To secure regional ownership and support, the shape of regional institutions tasked with implementing various policies, including regional monetary policy, must be endorsed and supported by all stakeholders, not only the political leadership. Therefore, it is important to roll out public educational programmes about the SADC integration agenda, encourage the participation of non-governmental organisations, trade unions and the general public in the debates about regional policies, institutions and how these should impact national policies and institutions.

## **2. Attendance**

The workshop was attended by high-level officials from the central banks in Southern Africa. The African Union Commission (AUC), the African Union (AU) sub-regional office, the SADC Secretariat, international financial institutions and the ECA Headquarters in Addis Ababa, Ethiopia, were also represented. The list of participants is attached to this report as Annexure 3.

## **3. Opening remarks**

In his opening remarks, Senior Economic Affairs Officer, UNECA-SA, Mr. Alfred Latigo, thanked participants for heeding the organisers’ invitation. He gave a brief background and context of the meeting. In this regard, he mentioned that the meeting is an outcome of the ECA-SADC Multi-Year Programme (MYP) collaboration. The MYP, among other issues, outlines the ECA-SA work and the range of technical support it provides to SADC and the Member States in general. It also underscores the importance the ECA attaches to joint partnerships with SADC and other key stakeholders in the quest to realise regional integration and development in the sub-region. He requested the experts to discuss matters openly and candidly in the two days of deliberations, stressing the need for the experts to own the process if the workshop objectives were to be achieved.

In his opening remarks, the representative of the African Union, Southern African Regional Office, in Lilongwe, Malawi, Professor R. Omotayo Olaniyan, noted that the African Union has placed a high priority on regionalism for Africa’s development. This meeting therefore was significant for the AU as the debate on continental integration gathered speed. This is more so against the background of the aftermath of

**“The African Union has placed a high priority on regionalism for Africa’s development”**

global financial crisis, recession and the ongoing effects of environmental degradation on economic development in Africa.

The weak nature of most African economies, Professor Olaniyan said, implies weak capacity to cope with external shocks. African countries' inadequate and often unpredictable financial resources further remain a setback in capacity to cope with environmental degradation. Along with these, is the challenges posed by food insecurity and the threat of aggravation of hunger and stagnation of economic growth and development in some Member States.

Professor Olaniyan commended ECA-SA on its continuing efforts to monitor the integration and development process in SADC, as well as its convening of the meeting. He expressed satisfaction that efforts to achieve the goals of SADC RISDP are progressing well. For example, the FTA and protocols on investments have been adopted to lay the foundations for integration and development in the Community. Furthermore, issues in the area of free movement of people to facilitate trade and trade expansion are being considered.

All these efforts will greatly benefit from a monetary union and financial integration. Reaching regional financial integration and eventually a monetary union will not be easy. Hence the nature, objectives and processes leading to these outcomes need to be well articulated and accepted by all Member States. Hence, Professor Olaniyan, welcomed the study on 'Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence Framework for Regional Financial Integration.' He noted that a careful review of the draft will advance the integration process in Southern Africa.

Dr. Lufeyo Banda, representing the SADC Secretariat started by thanking the UN-ECA-SA for coming up with the study to address some policy gaps in the governance of financial institutions in the sub-region. According to him, the study was important for two main reasons: firstly, it blended well with the SADC work on financial integration within the context of the FIP. Secondly, it created an opportunity for SADC to refocus and sharpen its roadmap towards the monetary union as envisaged in the RISDP. Notwithstanding some implementation challenges, he informed the meeting that there was a lot of progress that SADC had made in-so-far as rallying Member States together to harmonise their policies and strategies to attain the various milestones leading to the creation of a monetary union was concerned.

The final opening remarks were made by Mr. Mshiyeni Belle: Head of the Secretariat of the SADC CCBG. He stressed the critical importance of stakeholder partnerships in the regional integration processes. In this regard, he mentioned the ongoing interactions with such regional and international institutions as the IMF, the AU, the

AfDB, and others. These interactions notwithstanding, he underscored that the ownership of the integration agenda remained firmly with SADC.

**“The ownership of the integration agenda remained firmly with SADC”**

Mr. Belle informed the meeting that not all Member States had signed all of the integration-related protocols such as the FIP. With respect to central banking issues, he mentioned that the guiding principles behind the setting up of regional and future national central banks will be autonomy, accountability and transparency- all of which have been agreed upon by Member States.

In conclusion, he conveyed the apologies from the central bank representatives absent from the meeting, noting that the time was less than propitious for them.

#### **4. Objectives and Expected Outcomes of the Workshop**

A representative of UNECA-SA, Mr. Alfred Latigo, outlined the objectives, and expected outcomes of the Workshop. The broad objective of the Workshop was to review the draft report on the Governance of the Financial Institutions in Southern Africa: Issues for an Institutional Convergence for a Regional Financial Integration. Specific objectives were (i) to review issues relating to the SADC framework that would guide the region towards a monetary union, and (ii) to determine the next course of action by the UNECA-SA, SADC and CCBG to support Member States as they develop a framework to guide the process of establishing a monetary union.

He mentioned that the meeting’s recommendations will then be consolidated into the draft report in order to trigger the formulation of a SADC RFI Framework and also assist in accelerating regional financial integration. The meeting should also discuss several presentations by various stakeholders on selected topics that directly contribute to the overall subject matter of the draft report.

Mr. Latigo informed the meeting that the expected outcomes of the meeting are to (i) identify issues for consideration by Member States as they formulate the Framework for a monetary union; (ii) clearly and precisely recommend how to strengthen governance of financial institutions in order to support the establishment of a monetary union; and (iii) fully identify the various capacity needs and come up with measures to address them across the sub-region.



## 5. Presentation and Adoption of the Agenda and Programme of Work

Mr. Jack Jones Zulu, Social Affairs Officer: ECA-SA, presented the agenda and programme of work.

## 6. Presentation of the Background Document

Day 1 Facilitator: Mr. Alfredo Cuevas, Senior IMF Resident Representative (South Africa)

Presenter: Mr. Mzwanele G. Mfunwa, Economic Affairs Officer, UNECA-SA

**Title:** *Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence for Regional Financial Integration in SADC*

In a presentation of the draft document entitled “*Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence for Regional Financial Integration in SADC*,” Mr. Mzwanele Mfunwa summarised a number of key issues raised in the document. He gave a brief overview of the origins of the SADC financial integration efforts and the reasons behind such efforts. These reasons were for Member States to leverage on each others’ strength to overcome disadvantages of small populations, tiny geographical areas and lack of access to sea routes. Economically, these reasons are to build economies of scale, deepen intra-regional trade, induce regional self-reliance and eradicate extreme poverty in the long term. The objectives of a monetary union and a single currency are advanced forms of regional financial integration.

In supporting this effort, he informed the meeting that the UNECA, pursuing a MYP it has with SADC, is proposing a SADC Framework for Regional Financial Integration. He mentioned that this suggestion stems from experiences of other regional monetary cooperation regions, and hence, nothing new. However, the Framework holds major benefits for the sub-region.

In highlighting key benefits of the proposed Framework, Mr. Mfunwa mentioned that it will help to consolidate the integration process. It will further display all distinct processes of regional financial integration in a logically consistent format, sequencing key milestones and including timelines for each step of the way. Indeed, experiences from other successfully integrated regions show that such a Framework should be comprehensive, covering financial policies and the development of suitable infrastructure

and institutions. The Framework will also set out the key criteria for measuring progress towards integration.

Moreover, such a Framework would help identify slippages in the implementation of the various programmes and projects in a timely manner and allow for corrective measures. Some areas where countries have previously faced difficulties include: (i) inadequate support at the national level for the integration process, (ii) a dearth of human and technological resources to implement some of the technical aspects, and (iii) the presence of weak regional policies and procedures. Indeed, a detailed Framework should identify resource requirements for each of the stages, and measures to assist resource poor Member countries.

Mr. Mfunwa acknowledged some of the key achievements that the SADC has made in various financial convergence areas. The pertinent areas where good progress has been made cover integration of banking and capital markets, the harmonisation of national payment systems, regulatory questions, as well as institutional aspects of central bank independence, corporate governance, capacity building and inter-central bank communication. While progress is discernible, some areas may need policy and institutional strengthening. In this regard, he suggested that the autonomy of regional and national central banks would greatly benefit, if the existing allowance for credit to governments is proscribed in both regional and national central bank laws. This prohibition would further strengthen the region's macroeconomic stability, making SADC attractive to both local and foreign investments.

Mr. Mfunwa lamented the absence of inclusiveness and public participation in the establishment of regional institutions, such as the regional central bank. He, therefore, proposed that the Framework being suggested should strongly encourage Member States to adopt a participatory approach to regional financial integration. To secure regional ownership and support, the shape of regional institutions tasked with implementing various policies must be endorsed and supported by all stakeholders, not only the political leadership. He, therefore, further suggested that Member States should roll out public education programmes about the SADC integration agenda, encourage the participation of non-governmental organisations, trade unions and the general public in the debates about regional policies, institutions and how these should impact national policies and institutions.

He requested participants to help identify other issues that the Framework should contain, including whether it should recommend extending the deadline for the SADC monetary union in light of the vast amount of work still outstanding. He drew the attention of the experts to the list of question in the draft document and implored them to help address them. These questions pertain to the roles in the integration process

of regional bodies such as the SADC Secretariat, SADC governments, international cooperation partners, and non-state actors.

In conclusion, he requested participants to suggest ways to ensure that the Workshop's deliberations and recommendations reach the policy-makers with a view to having them implemented at national and regional levels. In particular, that the CCBG Secretariat should take these recommendations to the next CCBG meeting in 2010.

## 7. Plenary discussions

Following the presentation, participants welcomed the UNECA-SA's initiative of proposing the Framework for Regional Financial Integration, arguing that such a Framework will help guide the path towards a SADC monetary union and the creation of a common currency. Moreover, given the vast number of ongoing and pending programmes and projects, and the proliferation of committees and sub-committees to implement them, and the possibility that there will be a lack of coordination among implementation agencies, such an all-encompassing Framework would indeed be welcomed.

Participants deliberated on a wide range of issues that arose from the presentation. On the concern about the loss of monetary policy as an instrument of economic management, some experts argued that in the same manner that countries have independent judiciaries, independent monetary policies serve to ensure efficiently run public administrations while also serving to counteract possible fiscal policy slippages. The experts sympathised with views relating to the 'asymmetry of shocks'. They, therefore, suggested that a dedicated study on the costs and benefits of regional financial integration should be undertaken by Member States.

The meeting was informed that the SADC Model Law was based on a MoU between Member States in, which emphasis has been placed on the autonomy, transparency and accountability of the planned regional central bank. Furthermore, to ensure that the envisaged regional central bank takes national issue into account in arriving at a monetary policy decision, the composition of such a regional policy-making body will be made of representatives from all Member States.

Participants agreed that not much was being done to publicise the financial integration process in particular and the entire SADC regional integration agenda in general. Participants, therefore, expressed the need for national political campaigns to raise the regional integration as an issue. This will get the public to engage more with its details, while debating on its pros and cons.

***“The Workshop’s deliberations and recommendations should reach the policy-makers with a view to having them implemented at national and regional levels”***

***“Experts argued that in the same manner that countries have independent judiciaries, independent monetary policies serve to ensure efficiently run public administrations while also serving to counteract possible fiscal policy slippages”***

**“Participants strongly urged Member States to consider whether the SADC monetary union and single currency timeframes remain feasible”**

The SADC regional financial integration, and indeed the entire regional integration agenda, needs to be as inclusive and participatory as possible. In this regard, Member States and the SADC Secretariat should actively engage the national parliaments, civil society, trade unions, private sector, and the general public when formulating regional policies and implementing regional programmes. Partnering with the media and universities, among others agents, would assist in igniting interest in the integration process and boost the sense of regional ownership and unity. Participants welcomed the increased engagement of the private sector in certain sectors such as the ICT, but that this engagement remains limited.

Participants strongly urged Member States to consider whether the SADC monetary union and single currency timeframes remain feasible. Such a consideration should incorporate issues pertaining to whether: the SADC common market will be deep enough on time to allow for a customs union to gain traction; whether the SADC FTA launched in August 2008 is fully functional; whether there is sufficient time to ensure that the Tripartite arrangement has been fully harmonised; whether the outstanding frameworks and model acts required under the FIP can be completed and mainstreamed into national laws on time; and whether capacity and resource constraints can be addressed to ensure smooth implementation of requisite regional and national programmes and regional institutions, including at the SADC Secretariat. Participants, however, cautioned that a decision to extend timelines for too long without clear time-bound milestones and a clear political will, will pose a threat to integration plans.

**“Participants encouraged Member States to consider adopting a ‘variable geometry approach’ in which a number of ‘lead countries’ could embark on a monetary union as scheduled”**

To inject momentum into the integration agenda, participants encouraged Member States to consider adopting a ‘variable geometry approach’ in which a number of ‘lead countries’ could embark on a monetary union as scheduled, while others can follow later based on their state of readiness. To illustrate this point, participants deployed the experience from formation of the European Union (EU) in which Germany and France played a leading role in getting the EU off the ground. As SADC Member States consider this recommendation, they should also ponder how strict the entrance criteria into the monetary union should be, especially in light of the state of economic development of SADC countries.

Finally, as a further effort to come up with creative ideas to move towards a monetary union a little faster, some participants wondered whether a ‘big bang’ approach to such a union could be an option. Here, Member States could introduce a single currency – an action that could instantaneously facilitate cross-border trading, among other benefits. Still other participants cautioned that even introducing a single currency is a lengthy process on its own, requiring setting up necessary institutions, reaching agreements on currency symbols, and attending to numerous other areas.

## 8. Plenary presentations

**Presenter: Dr. Lufeyo Banda, SADC Secretariat**

**Title: *Status of SADC Finance Protocol, Instruments and Declarations on the implementation of Regional Integration (SADC)***

Dr. Banda presented a paper on the Status of SADC Finance Protocol, Instruments and Declarations on the implementation of Regional Integration. This presentation highlighted some achievements under the FIP made under EU/SADC cooperation entered into with funding amounting to some 13.2 million Euros under the European Development Fund (EDF) 9 programme. He summarised the FIP results under a number of areas as follows: (i) strengthening of capacities at regional and national level to ensure a proper implementation and domestication of the FIP; harmonisation of national investment policies, legislation and practices drawing lessons from international 'best practices'; achieving progress in macroeconomic convergence; and coordination of SADC Member States' tax regimes.

Closer to the issues related to the regional financial integration, Dr. Banda reported on a number of 'result areas'. First, the implementation of monetary and supervisory policies that entail: (i) harmonisation of legal and operational frameworks of SADC Financial Institutions; (ii) enhance cooperation of payment, clearing and settlement systems of the SADC Financial System; (iii) enhance cooperation and coordination in the area of Banking Regulatory and Supervisory Matters.

Second, there are activities under the cooperation and coordination of exchange controls policies that comprise: (i) establishing a framework for cooperation and coordination with regard to the promotion of exchange in respect of current account transactions, and capital and financial account transactions of SADC Member States; (ii) reviewing exchange control policies to ensure exchange control convergence as SADC Member States move towards full exchange control liberalisation; and (iii) reviewing capital and financial accounting policies in all SADC Member States and facilitate the implementation of financial accounting liberalisation. In these areas, the legal framework for Central Banks of SADC Member States has been drafted; much work on SADC payment, settlement and clearing systems has been made; and the roadmap on exchange controls has been drawn and a study on exchange controls is underway.

On enhancing the Development Financial Institutions (DFI), Dr. Banda reported that the aims of the activities are (i) to enhance the relationship between the SADC Secretariat, SADC DFRC and DFI Network; (ii) assess the development of DFIs in SADC Member States with the aim of assisting those lagging behind; (iii) harmonise the policy framework among the DFIs of SADC Member States; (iv) building the capacity of

DFIs through hosting of training workshops; (v) facilitate the operationalisation of the Project Preparation and Development Facility (PPDF)-first window of SADC Development Fund; (vi) start working on the terms of reference (ToRs) for phase II study of PPDF (that is PPDF outside DBSA); and (vii) commission a study on the SADC Development Fund.

**“ FIP faces a number of challenges such as difficulties in getting stakeholders to assist in the FIP projects “**

The area concerning the framework for harmonising non-banking financial institutions, the CISNA and the COSSE has registered the following progress: (i) come up with the ‘Hub and Spoke’ project, which is currently being implemented by COSSE with an expected SADC support; and (ii) the COSSE is in the process of developing the policy framework, which will guide SADC in the development and harmonisation of the policy framework of Insurance, Securities and Stock Exchanges.

In concluding his presentation, Dr. Banda noted that the FIP faces a number of challenges such as difficulties in getting stakeholders to assist in the FIP projects, as well as establishing the priority needs of the main intervention areas of the FIP, namely: investment, macroeconomic convergence, taxation, development finance, lack of a clear implementation strategy for FIP, an absence of assessment of FIP impact on individual economies, weak coordination at national level, slow ‘domestication’ of the FIP, and limited resources and capacities.

## **9. Plenary discussions**

Following the presentation, participants discussed a wide range of issues. They wondered who they should propose to lead the draft of the proposed Framework. They took note of the severe institutional capacity constraints facing the SADC Secretariat, which would be an ideal drafter of such a Framework. Some participants proposed that the CCBG Secretariat should do the job, but others felt that since the CCBG resides in one of the central banks, it may give an impression that the process is driven solely by one particular Member State. Participants then decided to let CCBG sub-committees, who will review the recommendations from this Workshop, decide on the matter.

A brief deliberation on ways to strengthen the SADC Secretariat centred on legal/ protocol provisions that force a quota system for human resources. Participants noted that low remuneration is one of the main reasons why citizens from relatively developed Member States shun employment at the Secretariat. In this regard, participants suggested that Member States should consider improving the conditions of employment, review the quota requirement, and expand the secondment term for those sent by Member States to the Secretariat.

On specific issues, participants viewed favourably the idea of a bank supervisory supra-national authority to ensure an improved oversight of regional banks. They noted a similar trend emerging in Europe where this idea is deemed superior to one in which bank supervision is the prerogative of individual Member States. However, some participants argued that the SADC region should prioritise, at this juncture, compliance of banks with best international standards and norms, including compliance with the Basel II principles.

Finally, participants felt strongly that Member States should mainstream regional laws and protocols into national laws. They deem current efforts as inadequate in this regard, suggesting half-hearted support for the regional integration that the leadership professes to support. Moreover, the leadership should publicise the regional integration agenda as much as possible, even raising integration issues during election campaigns.

**“Participants viewed favourably the idea of a bank supervisory supra-national authority to ensure an improved oversight of regional banks”**

## 10. Plenary presentations

**Presenter: Mr. Mshiyeni Belle, Head: CCBG Secretariat**

**Title: *Roadmap towards Establishing Monetary Union in SADC***

Mr. Belle presented a paper on a Roadmap towards Establishing Monetary Union in SADC which seeks to draw Member States’ attention to key issues for consideration as SADC moves ahead with its monetary union ambitions. As a background to his presentation, he reminded participants of the SADC Treaty objective:

To promote the interdependence and integration of our national economies for the harmonious, balanced and equitable development of the region.” While Article 5(2) of the same Treaty requires Member States “to harmonize economic policies, improve economic management and performance through regional integration and create appropriate institutions and mechanisms for the implementation programmes and operations of SADC and its institutions.

**“Participants felt strongly that Member States should mainstream regional laws and protocols into national laws.”**

The related FIP instrument for integration calls for the “conclusion of Protocols to assist the process of cooperation and integration,” and underscoring the importance of macroeconomic stability, sound financial sector and investment environment to achieve monetary union and deeper regional integration. The RISDP, the key driver for regional integration, provides guidelines to achieve a FTA by 2008, a SADC Custom Union by 2010, a SADC Common Market by 2015, a SADC Monetary Union/Central Bank by 2016, and a Single Currency by 2018.

On legal issues facing SADC, Mr. Belle argued that a monetary union has to be properly embedded in the legal and institutional frameworks in which it is supposed to operate. He suggested a legally binding Monetary Union Agreement (MUA), preferably incorporated into the Treaty establishing the Community of Member States, and statutes of the relevant institutions, preferably annexed to such MUA/Treaty and made an integral part of them.

**“SADC MUA should lay down the roadmap and timetable towards a monetary union..”**

Mr. Belle suggested that a SADC MUA should lay down the roadmap and timetable towards a monetary union. Among issues to be decided are (i) whether a transitional body to carry out preparatory work should be set up, (ii) where and how the SADC Central Bank should be established, (iii) when and how should a single currency be introduced, (iv) when banknotes and coins would be introduced (if not simultaneously with the introduction of the single currency), (v) how to treat Member States and their national central banks (NCBs) which do not introduce the single currency from the outset, (vi) The MUA should also lay down the obligations for the fulfilment of economic convergence criteria as an entry requirement into a monetary union, and (vii) legal mandates.

The institutional plans towards the SADC Single Currency include a transition from the CCBG to a SADC Monetary Institute; a transitional body to carry out preparatory work to be formed. Thereafter, an additional transition from the SADC Monetary Institute to a SADC Central Bank, to formally adopt the regulatory, organisational and logistical framework prepared by the Monetary Institute will occur. A process will get underway in which a single currency will be introduced through the irrevocable fixing of the exchange rates of the currencies of the participating SADC Member States. This will be followed by the introduction of (physical) SADC banknotes and coins. He noted that care will have to be exercised to make a distinction between those central banks that are in the SADC currency system and those that are in the SADC System of Central Banks. The legal framework or SADC Central Bank Act will have to cater for other accountability mechanisms like Auditors, and hearings in the SADC Parliament for examination of the operational efficiency of the management of the SADC Central Bank.

**“ The relation between the SADC Central Bank and the National Central Banks should be established”**

On policy issues, critical decisions will have to be taken on (i) the scope of the central banks mandate, (ii) whether the SADC Central Bank should be responsible for monetary policy (exclusively) and financial stability (together with other competent parties), but not for prudential supervision or (iii) whether the mandate should be inclusive of prudential supervision. The relation between the SADC Central Bank and the National Central Banks (NCBs) should be established. In particular, the level of centralisation and decentralisation of the system should be decided upon. Another policy matter is whether the SADC Central Bank should formulate and implement the



SADC monetary policy, while the NCBs should execute such policy as the operational arms of the system. Lastly, a decision should be made about whether a body should be established for Governors and Minister's of Finance to coordinate policies.

Outlining financial issues, Mr. Belle discussed the status of the NCBs in the SADC system. A decision should be made whether these NCBs should bear the responsibility and carry expenses to execute their own, non-system related tasks (e.g. prudential supervision). Furthermore, decisions will have to be made, inter alia, about which operations will the SADC CB and NCBs be allowed to carry out and under which conditions (e.g. should credit operations be collateralised?). A number of financial matters will have to be addressed (e.g. capitalisation of the SADC Central Bank, allocation of monetary income, restrictions on operations with foreign reserves remaining with the NCBs); the size of a SADC Central Bank's capital and the amounts NCBs are obliged to transfer in foreign reserves to the SADC Central Bank in accordance with the capital key, whereby the SADC Central Bank has developed an elaborate financial regime for the system as a whole.

On political issues, he stated that countries should be ready to (i) surrender monetary policy to a central body, (ii) subject themselves to fiscal discipline, (iii) forgo their currencies, (iv) deal with representation issues in the Monetary Policy Committee of the regional central bank, (v) agree to gradually join the monetary union using the CMA as a basis and the Rand as an interim currency or convergence currency, and (vi) allow NCBs to be independent.

Prior actions leading to a single currency will involve countless activities, as discussed above. Importantly, actions should be carried out in a coordinated and well-monitored fashion by and between all stakeholders involved. These actions should be guided by a master plan drawn by the SADC Monetary Institute, and preferably in a committee structure involving both representatives of the SADC CB as well as the NCBs in order to ensure that the process is carried by all relevant parties. The process will take cognisance of timelines for different projects, and ensure participation of other competent authorities (e.g. community legislation relating to the introduction of a single currency) as well.

A change over to a single currency will entail numerous political, social, and technical matters involving community citizens, the financial markets, administrations and others. All parties will have to be timely and properly informed and where appropriate consulted in order to ensure a smooth and undisturbed changeover. This changeover will require Member States to make decisions and take actions in a large number of areas some of which are:

***“A change over to a single currency will entail numerous political, social, and technical matters involving community citizens, the financial markets, administrations and others”***

Firstly, a changeover scenario will have to be defined (big bang or staggered). In the SADC area Member States, can introduce the (scriptural) SADC currency first and introduced the (physical) banknotes two or three years later.

Secondly, in the interim period, the principle of no prohibition, no compulsion can be applicable, i.e. the SADC currency could be used where possible, for example in bank transfers, but there should be no obligation to use or accept SADC payments.

And thirdly, the name of the single currency and its sub-divisions will have to be chosen and a uniform and consistent use of such name will have to be ensured. One SADC currency unit is sub-divided into hundred cents.

The conversion rates, i.e. the rates at which the national currencies of the participating member states will be converted into the single currency, will have to be determined and announced well in advance of the start of monetary union to avoid speculation. He mentioned that the SADC Treaty requires the initial value of the SADC currency to equal the value of a particular currency, say the Rand. The Rand to be defined as a basket of fixed quantities of the currencies of SADC Member States. When the basket is introduced, its initial external value of prevailing exchange rates could be made equal to that of the International Monetary Fund's Special Drawing Rights (SDR). The conversion rates should be adopted by the SADC Council of Governors and Ministers.

The legal implications of the changeover will have to be organised covering issues such as the substitution of the single currency for the national currencies, conversion and rounding rules, continuity of contracts, exchange and redemption of banknotes and coins, as well as redenomination of securities.

The changeover in the financial sector will have to be well prepared. For example, the market infrastructure for scriptural payments will have to be adapted. The SADC Monetary Institute may start at an early stage to inform and, where appropriate, consult market participants. The cash changeover will have to be prepared. All logistical arrangements need to be prepared well in advance to ensure a smooth changeover. For example, vending machines will need to be adapted.

The SADC CB should communicate the relevant technical specifications of SADC banknotes well in advance of their introduction to the relevant parties, and the SADC banknotes (and coins) should become available everywhere across the single currency area punctually at a chosen date. Old banknotes and coins could still be used as legal tender for payments up to a pre-determined date after the introduction of SADC banknotes and coins.

Mr. Belle concluded his presentation by outlining some of the challenges facing the process, including the following: (i) a monetary union occurs in an environment that favours an optimal currency area, and questions arise about whether SADC is such an area, (ii) the size of benefits and costs may delay implementation, (iii) adherence to fiscal discipline may be difficult for countries still emerging out of debt relief, (iv) monetary discipline targeting low inflation may not be practical in growing economies, (v) acceptance of a hegemony in the region may cause problems, and its currency or monetary discipline may be rejected, (vi) can the CMA be utilised as a basis for a SADC monetary union? and (vii) the limited private sector participation.

## 11. Plenary discussions

Participants welcomed the emphasis that the SADC Model Central Bank Act puts on central bank autonomy, but urged that this autonomy must be grounded on political reality. Some participants thought that transitional arrangements may be needed towards allowing full central bank autonomy. They expressed concern that Member States, particularly the resource-poor ones, may resist the measure citing the need for short term financing to close budget gaps, particularly in light of unpredictable donor flows, and heavy reliance on globally-traded commodities with volatile prices. Some participants however thought that a gradualist approach can be adopted in which some national central banks could be granted full autonomy, while others can do so later as national economic conditions allow.

In calling for a solid arrangement towards a SADC monetary union, some participants suggested that the CMA could be expanded gradually to non-Member States of the Area, starting possibly with Mozambique and Zimbabwe – that is, countries immediately adjacent to the CMA. Some participants expressed anxiety that the origins of the CMA may deter others from joining it. Therefore, in the same vein as the proposed COMESA Monetary Institute, some participants thought the idea was good for SADC as well, namely a SADC Monetary Institute. They deemed this Institute as a natural progression from the CCBG Secretariat to a stand-alone institute that would drive the financial integration agenda.

Good policies are grounded in good and rigorous academic studies. Participants acknowledged the urgent need for strong intellectual and fact-based studies to guide policy-makers' decisions. They argued that this task of producing studies could be placed under the SADC Monetary Institute that some participants were proposing.

The issue of multiple memberships came up with several participants expressing fears that SADC resources, meagre as they are, could be used for purposes of other

***“Participants welcomed the emphasis that the SADC Model Central Bank Act puts on central bank autonomy, but urged that this autonomy must be grounded on political reality”***

***“ Participants acknowledged the urgent need for strong intellectual and fact-based studies to guide policy-makers’ decisions”***

RECs by those countries belonging to others. Accordingly, some participants called for Member States to implement some restraints on multiple memberships. Nonetheless, participants welcomed and commended the Tripartite Agreement that has been made by the SADC, the EAC and the COMESA to harmonise their activities. However, some participants expressed concern that it is unclear who will drive the tripartite harmonisation agreement. As it stands, it appears to be an open-ended process that does little to resolve the multiple memberships' dilemma.

Participants stressed the need for 'champions for regional integration' on the path to a SADC monetary union and a single currency. They argued that the success of the EU is partly attributed to the leadership of Germany and France. In this regard, they commended the example set by Mozambique in financing and adopting the Bank Supervision Application that will eventually be adopted by all Member States.

**“Participants stressed the need for ‘champions for regional integration’ on the path to a SADC monetary union and a single currency”**

On matters of compensating poorer Member States to enable them to buy-in into the integration process and meet some of the integration costs, some participants argued that too much emphasis should not be placed on this compensation. Indeed, Member States are, or should be, aware that integration entails sacrifices at least in the short-term. Compensation could very well hide structural problems that countries may not want to deal with. Hence the earlier proposed 'variable geometry' approach becomes even more relevant to enable countries to be truly ready before joining the monetary union.

Participants broached the matter of a dedicated ministry responsible for regional integration affairs. However, other participants thought that currently SADC Member States have too many ministries and thus expanding the bureaucracy further will not be cost effective. Besides, a regional integration agenda is multi-dimensional, dealt with in various ministries (finance, trade, infrastructure, etc.). In the end, participants decided that this option should be placed before decision-makers, and possibly a deeper study on these issues may be undertaken.

**Day 2 Facilitator: Mr. Daniel A. Tanoë, Economic Affairs Officer, UNECA-NRID**

## **12. Plenary presentation**

**Presenter: Dr. Leonard Nkole Kalinde, Bank of Zambia**

**Title: *Harmonisation of Central Banks Laws in Southern Africa: What are the Issues and Challenges around Harmonization?***

The presentation of Dr. Kalinde covered a number of areas comprising of policy and legal issues, surveillance imperatives, and matters related to multi membership of SADC Member States. He stressed at the onset that the harmonisation of central bank laws in SADC will require the design of appropriate legal convergence criteria that should be subjected to frequent and effective multilateral surveillance.

He noted that Southern Africa is home to three distinct legal families, i.e. Common Law, Civil Law and Roman Dutch Law – all of which will pose a policy challenge when the process of harmonising of central bank laws commences. Indeed, despite sharing common functions, central banks in SADC have widely differing powers and different legal regimes. The region comprises of countries that are characterised by strong disparities in their economic and social background and facing critical development challenges. Similarly, the central bank legislations vary widely across different countries, especially in respect of the relationships between governments and central banks in the operation of monetary policy.

Dr. Kalinde further noted that most of the existing central bank statutes were enacted in the 1990s, and provide for multiple objectives for a monetary policy. Hence, these statutes further lack clarity in relation to the powers and functions of a central bank. Importantly too, is that, there are no autonomy provisions, but allowance is explicitly made for the Minister responsible for national financial matters to issue directives to the central banks. Therefore, an important pre-requisite for harmonising central bank laws in the region is sufficient consensus on (i) the role and objectives of a central bank; (ii) the relationship between the government and the central bank; and (iii) accountability and transparency of a central bank. In the absence of a basic consensus on such fundamental monetary policy issues, diverging policy preferences and views on the functioning of the central bank in an economy may lead to conflicts.

He argued that an effective tool for monitoring and assessing legal convergence requires the designing of an appropriate set of legal convergence criteria. Such criteria could address issues surrounding: (i) independence of central banks; (ii) minimising central bank financing of the government budget; (iii) central bank transparency; and (iv) the central bank accountability.

He noted that when defining convergence criteria, decision-makers face a number of fundamental policy choices with regard to three basic aspects: (i) the purpose of convergence criteria must be clarified (i.e. what role they are to play in the harmonisation process); (ii) their content must be decided (i.e. the underlying set of legal principles and the policy areas that are to be covered); and (iii) choices have to be made concerning the specific design of the criteria.

***“ An effective tool for monitoring and assessing legal convergence requires the designing of an appropriate set of legal convergence criteria”***

Dr. Kalinde observed that the role of the legal convergence criteria tends to be strongest if it serves as a disciplining device for policies and weakest if it serves as a mere information tool to assess policies. The potential impact of the criteria on the convergence process can, therefore, be expected to correlate with the consequences a country faces in the event of non-compliance as this determines the incentives to gear policies towards fulfilling the criteria.

The design of the time horizon during the harmonisation phase should consider whether the legal convergence criteria are entry criteria or permanent criteria, and whether the criteria are designed as selection criteria for participation in the regional central bank or as mere indicative targets. In addition to being just entry criteria, convergence criteria can also serve as an anchor for policies after the establishment of a regional central bank, to be fulfilled by Member States on a permanent basis.

Potentially, the strongest sanction for failing to meet the entry criteria is non-admittance to the club, provided the entry criteria are designed as selection criteria. Convergence criteria can be designed as selection criteria with the aim of helping to determine which countries are suitable to form a regional central bank. Selection criteria, obviously, provide a stronger incentive for compliance, as the potential sanction in the case of non-compliance is denial of access to the regional central bank. Accordingly, the disciplining effect of selection criteria on legal principles and/or norms can be regarded as high and thus they may also serve as an effective anchor for expectations

He argued that particular attention should be paid to the sustainability of legal convergence with a view to the establishment of a regional central bank. The concept of sustainability requires the reference period for assessment of the compliance with the criteria not to be too short. In the design of any legal convergence criterion, thresholds, or reference values, have to be chosen to decide at what point the criterion is considered to be fulfilled, as well as to determine when it has not been fulfilled.

He cautioned that when designing legal convergence criteria, Member States need to decide to what extent these criteria should be open to interpretation. A certain degree of discretion may be warranted to avoid too mechanistic an application of the criteria, which may not allow for due consideration of the overall economic picture. However, the more room is left for a political interpretation of such criteria, the less effective they are as an anchor for policies and expectations and as a disciplining device.

On the multilateral surveillance of legal convergence criteria and institutional underpinnings, the monitoring and assessment of such criteria needs frequent and effective multilateral surveillance. This surveillance, will in turn, require a suitable legal framework and institutions that provide fora to exchange information and discuss the relevant legal developments and policies, and may consist of the CCGB and/or Treasury Ministers Forum.

***“When designing legal convergence criteria, Member States need to decide to what extent these criteria should be open to interpretation”***

With regard to the institutional underpinnings of multilateral surveillance, a key issue relates to enforcement mechanisms in case national policies deviate from commonly agreed legal convergence criteria. This requires the process of multilateral surveillance to be transparent to the public, as well as the commonly agreed legal convergence criteria. This is a precondition for the public to be able to monitor the compliance of national policies with the supra-national community's interests. While peer pressure may potentially be strong, its effectiveness in disciplining policies is likely to fall short of that of the potential sanction imposed on a country that does not comply with the legal convergence criteria. Therefore, further enforcement mechanisms may be contemplated to ensure compliance with commonly agreed objectives, rules and standards, such as fines.

He concluded his presentation by shifting to multiple memberships in several RECs of SADC countries. These memberships have generated problems, inter alia, of rivalry and lack of commitment to Pan-African economic integration due to divided loyalty, and poor funding due to inadequate resources for the several organisations. The effective implementation of economic integration arrangements is further constrained by another set of problems that revolve around the lack of clarity regarding the functions, responsibilities and powers of the different organs involved in various regional economic communities.

In this regard, Dr. Kalinde proposed that the concept of 'variable geometry' and the 'principle of subsidiarity' should be applied to allow for effective implementation of economic integration among countries that are at varying stages of development. The 'principle of subsidiarity' could be applied to provide a clearer basis for distributing powers and responsibilities across the several layers, from national to regional level, of the organisational structure of a regional economic community 'according to the comparative advantage of each in respect of the different functions'. Overarching these issues, this paper recommends that there should be a strong political commitment to the economic and monetary integration project in Southern Africa.

***“The concept of ‘variable geometry’ and the ‘principle of subsidiarity’ should be applied to allow for effective implementation of economic integration”***

## **13. Summary of key discussions and recommendations**

### **13.1 Theme: Policy and institutional issues**

#### **Summary of key discussions**

- The issue of costs and benefits associated with establishment of the SADC Monetary Union was raised by a number of participants given the different levels of

development of participating countries. Participants considered a study on costs and benefits as necessary to improve the understanding among all stakeholders.

- The meeting recognised that some loss of monetary policy sovereignty is inevitable. However, the fear of losing monetary policy control at national level should be allayed by the fact that the decision-making body of the envisaged SADC CB will follow a participatory approach involving all the NCBs. In this regard, the principle of transparency, accountability and inclusiveness should underpin monetary policy formulation specifically, and the financial integration agenda in general.
- The issue of ‘asymmetry of shocks’ across countries was discussed. In this regard, efforts should be made to expedite the establishment of a SADC Development Fund as a matter of priority.
- The meeting noted the progress made in macroeconomic convergence and stressed its importance for the rapid attainment of the monetary union.
- There was a discussion on the need to avoid duplication of instruments and efforts in establishing the monetary union in view of overlapping membership of SADC countries with other RECs, such as the COMESA and the EAC.
- It was generally noted that there was inadequate political commitment for implementing decisions taken at regional level.
- It was noted that the process towards a monetary union was complex and that there is a considerable amount of work to be done before attaining this objective. For example, the model frameworks and other milestones such as the SADC FTA and customs union processes have not been completed.
- In relation to the harmonisation of banking supervision, the meeting took note of the work being done by the SADC sub-committee on banking supervision in terms of defining and implementing a regional banking regulatory and supervisory strategy based on international standards. The issue for a supra-national body was also raised.
- Participants noted the need for greater inter-central bank communication and coordination in order to address common external threats to regional economic stability.
- Participants noted that not all countries might be ready at the same time to join the SADC Monetary Union for different reasons.



## Summary of recommendations

- The SADC Committee of Central Bankers, the SADC Secretariat and partners under the FIP should undertake a cost/benefit study to inform the process of establishing the SADC Monetary Union, including the extent of ‘asymmetric of shocks’ across countries, and the possibility of adopting a gradualist approach towards the monetary union [example, the use of the CMA as a building block].
- The fear of losing monetary policy control at the national level could be addressed through a transparent and participatory approach to a monetary union involving all national central banks and ministries of finance.
- A compensatory facility should be considered to address adjustment costs for adversely affected economies. There is a further need to reassess the macroeconomic convergence parameters in the context of SADC members’ economic realities, especially in light of current global environment.
- Against the backdrop of the recent political decision of SADC/EAC/COMESA to harmonise policies, SADC should strive to avoid duplication of efforts but instead should draw on the experiences of these other RECs such as on Financial Stability Indicators being considered by COMESA.
- Political commitments should be shown by drawing up and implementing an action plan for attaining the monetary union. This action plan should include the provision of adequate resources, including strengthening human capacity of the SADC Secretariat. Furthermore, such a political commitment should go beyond the mere signing of protocols and treaties, to actual domestication of these instruments into national laws.
- Given the complexity of the process towards the monetary union, and the amount of work still to be done between now and the targeted completion date, there is need for Member States to develop national strategies, structures and programmes to implement the monetary union agenda.
- On harmonisation of bank supervision and regulation, the meeting advocated the need to promote adherence to international norms and standards by banks as well as share information regarding banking regulatory and supervisory matters. In addition, consideration could be given to the establishment of a regional supra-national supervisory authority
- Inter-central bank communication and coordination should be enhanced to include devising a common policy approach in order to deal with external economic shocks collectively.

- The ‘variable geometry’ approach should be followed in the process of establishing the monetary union.
- There is need for a Monetary Union Agreement to be developed and signed by Member States

## **13.2 Theme: Capacity building and resource issues**

### **Summary of key discussions**

- Participants noted that the monetary union agenda requires strengthening the capacities of key players to drive and manage the process at both regional and national levels. In this regard, the meeting noted that there were some institutional capacity challenges that needed to be addressed within the SADC Secretariat for it to play its leadership role in this process.
- The meeting acknowledged the tremendous contributions of ICPs to the regional integration process in general and to the monetary union in particular. However, it was noted that there was a need for the ICPs to coordinate their assistance and SADC Member States to be more proactive in contributing towards the monetary union to reflect the regional ownership.

### **Summary of recommendations**

- There is an urgent need to address capacity at different levels: human, financial, institutional and technical.
- In the spirit of the Paris Declaration on Aid Effectiveness of 2005, there is a need for SADC to harmonise and coordinate the ICPs’ support to the monetary union process.

## **13.3 Theme: Participation issues**

### **Summary of key discussions**

- Participants noted that the monetary union process, in particular, and the integration agenda in general, has tended to be government-driven without adequate involvement of various stakeholders such as civil society, the private sector, the trade unions and others

- Participants further noted that the SADC Secretariat and Member States are not doing enough to popularise and educate the general public about the entire SADC integration agenda.

## **Summary of recommendations**

- The SADC Secretariat and Member States need to come up with a strategy such as domesticating the regional integration process to involve the public in the monetary union process in particular and the integration agenda in general.
- The SADC Secretariat and Member States should sufficiently sensitise the objectives, costs and benefits of the monetary union and regional integration agenda to the wider public.

## **14. Follow-up actions and closing remarks**

### **14.1 Follow-up actions**

- The ECA will revise the document to incorporate comments and recommendations emerging from the meeting.
- The ECA, CCBG and the SADC Secretariat will finalise the document and meeting report for publication.
- The CCBG and SADC to facilitate the discussion of the recommendations in the relevant subcommittees
- The CCBG and SADC to facilitate the tabling of the recommendations to the CCBG meeting in April/September 2010.

### **14.2 Closing remarks**

The representative of ECA-SA, Mr. Alfred Latigo, closed the meeting by thanking the participants for their active participation and attendance. He implored participants to do all they can to ensure that the recommendations of this meeting will reach decision-makers for action, noting that too many good plans in Africa remain un-implemented.

In conclusion, Mr. Latigo invited the participants to join a think-tank group (group of expert) to discuss various issues on macroeconomic convergence, financial and monetary integration through e-discussion and in some instances through meetings similar to this one.

## Annexure 3

### **A Workshop on Governance of Financial Institutions in Southern Africa: Issues for an Institutional Convergence Framework for Regional Financial Integration in SADC.**

#### **List of Experts**

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