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# Possible Effect of a Common Currency on Nigerian Economic Sustainable Development

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## Abstract

*ECOWAS single currency 'ECO' is to be launched in year 2020 by five out of fifteen countries. A major problem to international business all over the world is identified to be currencies and the risk associated with currencies. The cost of doing business is high; transaction is difficult because sometimes the currencies involved in the business are not available. The objective of the study is to evaluate the viability of a monetary union on sustainable economic development. The study used descriptive explanatory survey design which involves the use of questionnaire. The population included 270 staff that have spent not less than five (5) years in the foreign exchange department and/ or the treasury department of twenty (20) banks in Nigeria out of the twenty one banks as at October 2013. The results showed that common currency had a positive impact on sustainable economic development (r = 0.193, p = 0.004). The study concluded that a common currency would improve bilateral trade because countries in the currency zone would not be engaged in exchange rates fluctuations and it will be easier to move monies from one country to the other in the zone without being scared of diversity in exchange values. The study recommended that regional trade policies should be made known to the general public as this will improve bilateral trade within ECOWAS community, the community should ensure equal pay and equal right for work of equal value, members should be encouraged to deal more with their local currencies instead of dollar as this will help improve trade in the region. It was also recommended that the community to address most of the issues of internal and external shocks before the commencement of common currency.*

**Keywords:** Common currency, International Trade, Sustainable Development.

## Introduction

The Economic Community of West African States (ECOWAS), a regional group of sixteen West African countries, founded on May 28, 1975 with the signing of the Treaty in Lagos, to achieve "collective self-sufficiency" for the member states by means of economic and monetary union creating a single large trading bloc. Its mission is to promote economic integration[1].

As part of the fast-track approach to integration, six West African Heads of States on 20th April, 2000 decided in Accra, Ghana, to establish a second monetary zone to be known as the West African Monetary Zone (WAMZ) in 2003. The 'Accra Declaration' was signed by Nigeria, The Gambia, Sierra Leone, Liberia, Ghana, and Guinea, defining the objectives of the zone as well as an action plan and institutional arrangements to ensure the speedy implementation of their decision. It is proposed that the new zone will eventually merge with the CFA Franc Zone to form a single West African monetary zone.

ECOWAS adopted a two-step approach in achieving a common currency convergence. The first critical step is to rapidly promote intraregional trade which is currently low at 12% of total trade through measures such as encouraging production integration in industry, cross border expansion of banking institutions and capital market instruments etc.

The introduction of the ECO was originally set for 1st January, 2003 was rescheduled to 1st July, 2005 so that member states will have more time to comply with the convergence criteria and has now rescheduled to fly up by 2020. The macroeconomic targets (convergence criteria) that WAMZ members are required to satisfy: The primary criteria are to: record single digit end period inflation rate by 2003 and 5% by 2004 (achieve and maintain price stability); reduce the ratio of budget deficit (excluding grants) on commitment basis to GDP to $\leq$ 4% throughout the period 2003-2005 (ensure sustainable government fiscal position), limit Central Bank financing of government budget deficit a percent of previous year's tax revenue to $\leq$ 10 % throughout the period 2003-2005 and maintain sufficient level of gross official foreign exchange reserves of at least 3 months of import cover throughout the period 2003-2005.

The secondary criteria are: "prohibition of new domestic arrears and liquidation of existing ones; tax revenue to GDP $\geq$ 20%; wage bill to tax revenue $\leq$ 35%; public investment to tax revenue $\geq$ 20%; maintain real exchange rate stability; and positive real interest rate".

fficient regional payments systems promote and support regional flows by increasing speed and convenience, reducing cost, lowering payment risks and ensuring a high degree of finality[2]. The use of local currencies in intra-regional trade through the WAMA multilateral mechanism has not been successful[3].

A major problem to international business all over the world is identified to be currencies and the risk associated to currencies. The cost of doing business is high; transaction is difficult because sometimes the currencies involved in the business are not available. The thrust of this study then is to examine the nexus between common currency adoption in the ECOWAS countries and business factors. What is the impact of a monetary union on business factors?

The objective of this study is to evaluate the impact of a proposed monetary union on Nigerian economic sustainability. By evaluating the anticipated impact of the proposed monetary union on sustainable economic development

## Review of Literature

**Monetary Union:** Monetary union is defined as "agreement between countries in an economic union to have a common currency, fixed exchange rates and free movement of capital between countries"[4]. In economics, a monetary union, also known as a unitary or common currency, is a situation where two or more countries have an agreement to share a single currency among them. A good example is the East Caribbean dollar that is used among Caribbean economies.

"Even though the introduction of a common currency brings numerous benefits, it also has its disadvantages that result in certain costs. A currency union should be introduced when the benefits of the union are greater than the costs. Whereas the benefits of a common currency arise mostly at the microeconomic level, the costs are mostly related to the macroeconomic management of the individual members of the currency union"[5].

The main setback of a common currency is the absence of autonomy over monetary and exchange rate policy. In total monetary union, the national central banks of member countries either windup or are powerless. When a country abandons its national currency and joins a monetary union, the following tends to occur, protection from economic by devaluation and revaluation is not possible and the amount of national money in circulation or change in short term interest rate cannot be known [6]. Common policy response is appropriate as its allows or give room for symmetric shock that are minimal, this is attributed to cost of common currency, however, asymmetric shock affect members differently as a result of the inability to use the exchange rate to make relevant adjustment and as such greater volatility in output and employment. Mundell[7] affirmed how flexibility of exchange rate helps to adjust to fluctuations caused by an asymmetric demand shock in a two- country model.

Countries in a monetary union have contrasting economic cycles, or are at various economic stages in the cycle between boom and recession. Critics of monetary union say that the introduction of a single currency will destroy the policy of setting interest rates separately at the relevant levels for each economy. Experts advocate that monetary union can only be accomplished if the total region bounded by the single currency has the same legal framework (taxation, labour laws etc.) and a labour force that is highly mobile (BBC online, 1998).

**Sustainable Economic Development:** Sustainable development (SD) is a "pattern of economic growth in which resource use aims to meet human needs while preserving the environment so that these needs can be met not only in the present, but also for generations to come"[8].

Sustainability can also be defined as a process indicating the development of all aspects of human life affecting sustenance ion[9]. This involves resolving the conflict between the various competing goals and the concurrent pursuit of economic growth, environmental attribute and social justice also referred to as three amplitude (triple bottom line) with the outcome being technology, thus it is a constant emerging procedure[10].

The devising of social and economic system through sustainable development ensure improvement in health of nation, increament in real income, standard educational status and general quality of life advancement[11]. Development is about realising capable possibility; sustainable development of replenishable natural resources denotes respecting cap to the evolvement process, although these limits are modifiable by technology.

The construct of economic sustainability differ in input and output at all subject levels. The economic sustainability of a farm is subjective to the viability of, and markets for, an enterprise or product while of a nation is subjective to the whole economy on local, national and international levels. For most societies to achieve economic development means to secure higher standards of living, now and for future generations. They also make effort to protect and enhance their environment for present and future generation. Sustainable development attempt to settle these two objectives.

Economics is about the active use of resources, frequently indicated in monetary terms. Therefore, the theories about sustainable use of resources can be adapted to economic sustainability, besides monetary terms, one resource can regularly interchanged for another. One of the objectives of sustainable development is to advocate a balanced economy so as to bring about the ability to meet people's needs and improve environmental quality[2]. Economic indicators constitute but are not restricted to arrangement of the economy, pollution abatement expenditure, consumer expenditure, Gross Domestic Product, spending components of GDP and personal savings, employment, government borrowing and debt, inflation, imports and exports, infant mortality, and life expectancy.

## Methodology

Both quantitative and qualitative research design was used with the use of descriptive explanatory survey design which involves the administration of questionnaire to obtain information directly from respondents.

The population of the study are respondents who are experts in the area of monetary policy, foreign exchange and international business. The population include 270 staff that have spent not less than five (5) years in the foreign exchange department and / or the treasury department of twenty (20) banks in Nigeria out of the twenty one commercial banks as at October 2013 and the Central Bank of Nigeria.

Staff that spent not less than five years in the foreign exchange and or the treasury department of the commercial banks in Nigeria including the Central bank of Nigeria was chosen for this study because they are directly involved with foreign currency transactions overtime and they have expert knowledge of currency movement. Heritage Banking Company Ltd was exempted from the study because it reopened in 2012 after collapsing for years.

The census sampling technique was used for data collection. This sampling technique was used because the entire population is small, and the researcher included the entire population in the study. The sample for this study include all 270 staff that have spent not less than five (5) years in the foreign exchange department and / or the treasury department of twenty (20) banks in Nigeria out of the twenty one commercial banks as at 30$^{th}$ October 2013 and the Central Bank of Nigeria.

**Data Source:** The researcher collected data through the primary source and secondary source in order to obtain adequate empirical study to form the basis for which useful findings, conclusions and recommendations for the study were drawn.

The primary source of data were collected by the researcher through direct contact with the respondent. The data obtained from primary source were used to support the result from the secondary source. The data were used to ascertain expert's view of the proposed currency "ECO" from the Nigeria's perspective. This major source of data were used for the study and comprised of the use of copies of questionnaire. Questionnaire constructed in line with the research hypotheses helped draw information directly from the field.

**Research Instrument:** The main research instrument for the study is a structured questionnaire as a means of primary data collection. The market research method was adopted in the collection of primary data and these were done through direct administration of questionnaire on the target respondents coupled with in- depth interview. In-depth interview schedule was done on a one on one basis with experts who may be too busy to fill copies of the questionnaire.

**Model Specification:** The primary data were analysed using simple linier regression to determine the relationship between the dependent and the independent variable. The independent variable (monetary union) was measured. Hence, the accessed the relationships that exists between the identified variables in the following equations

The Models Equation are as follow:
$Y = f(X)$
$Y$ = *dependent variable*
$X$ = *independent variable*

$Y = f(y_1)$
$X = f(x_1)$

$Y_1 = b_0 + b_1x_1 + \varepsilon$
$Y_1$ = *sustainable economic development*
$\varepsilon$ = *error*

**Method of Primary Data Collection:** Two hundred and fifty eight 258 copies of questionnaire were distributed to staff that have spent not less than five (5) years in the foreign exchange department and / or the treasury department of twenty (20) banks in Nigeria out of the twenty one banks as at October 2013 and the Central bank of Nigeria out of which all were returned.

The copies of questionnaire were distributed to the staff who indicated they had spent more than 5years in the department.

## Data Analysis Techniques

The questionnaire consists of items that generated data to be analysed. Bivariate analysis was used to determine the empirical relationship between two variables X and Y to see if the variables are related to one another. Simple linear regression used when two variables are thought to be systematically connected by a linear relationship. Linear regression was used to check the relationship between the dependent variable and independent variables.

The Pearson product-moment correlation coefficient was used to measure the strength and intensity (dependence) between two variables X and Y, giving a value between +1 and −1 inclusive, where 1 is total positive correlation, 0 is no correlation, and −1 is negative correlation.

**Data analysis: Restatement of Research Hypothesis:** Monetary union will have no significant impact on the sustainable economic development of Nigeria.

**Table-1**
**Summary showing relationship between monetary union and sustainable economic development**

| | | Constant |
|---|---|---|
| R | .193[a] | |
| R Square | .037 | |
| Adjusted R Square | .033 | |
| F | 8.593 | |
| Sig. | .004[b] | |
| T | 2.931 | 18.893 |
| Sig. | .004 | .000 |

Source: Field Survey, February, 2014

**Interpretation:** The regression table which is the model summary shows the regression result of 0.193 which is 19.3%, this shows a low positive linear relationship between the dependent variable (sustainable economic development) and independent variable (monetary union). The R squared of 0.037 which implies that about 3.7% variation in dependent variable (sustainable economic development) is explained by independent variable (monetary union) this is low.

The p-value of 0.004 is statistically significant in the ANOVA table. From the regression coefficient table, the column labelled "Unstandardised Coefficients" reveals the unstandardised regression coefficient for the independent variable, as 0.159. The test explains to us whether the regression coefficient is different enough from zero to be statistically significant at the level (0.004). According to above analysis, the p-value (0.004) is less than the alpha value (0.05) we therefore accept the alternative hypothesis and reject the null hypothesis and conclude that monetary union will have no significant impact on the sustainable economic development of Member states

From the coefficient table the simple linear regression equation can be written as:
$SD = b_0 + b_1 MU$
$SD = 42.669 + 0.159MU$

The above equation implies that a unit change in monetary union will propel an increase of 0.168 in sustainable economic development while if monetary union is held constant it will propel an increase of 42.669 in sustainable economic development.

**Discussion:** Some literature supports the hypothesis that monetary union will have no significant impact on the sustainable economic development of Member states. Sustainable economic development is viewed by some authors as economic growth, fiscal policy, current account deficits, external shocks and macroeconomic policies.

The arguement that in an economic union is that national policies should be tailored towards strong and sustainable economic growth and employment at same time promoting social cohesion, an integrated financial framework to ensure financial stability particularly in the euro area and reduce the cost of bank failures to European citizens[13]. This framework raise responsibility for supervision to the European level provides for common mechanisms to settle banks and guarantee customer deposits. An all inclusive budgetary framework ensure sound fiscal policy at the national and European levels, sound coordination, joint decision-making, greater enforcement and corresponding steps towards common debt issuance. This framework could include also different forms of fiscal solidarity which allows necessary democratic legitimacy and accountability of decision-making within the EMU, based on the joint exercise of sovereignty for common policies and solidarity.

The traditional argument of the OCA theory is that a prospective monetary union will not be sustainable under the following two conditions: Either its members face asymmetric (or asynchronous) shocks and/or they respond asymmetrically to uniform shocks (a difference in reactions which itself may be due to their different economic structures since varying degrees of price and wage flexibility, for example, induce asynchronous shocks). Empirical studies that look at the optimality of a monetary union have not explicitly distinguished whether such shocks originate from within the monetary union or from its outside. Prominent examples include Alesina, Barro and Tenreyro[14] which study the impact of currency unions on the pattern of covariance of shocks, but do not distinguish shocks according to their origins (external or internal) and simply consider the impact of all the shocks (whatever their natures are) on a union's member macroeconomic indicators. Some authors, Nitsch[15] and Rose[16], emphasize inflationary shocks as the most important determinant for the dissolution of monetary unions, their arguments do not contradict the possibilities that the gap in inflation rates between monetary union members may be induced by external shocks and the following member economies' reactions to such shocks Farvaque, Hammadou, and Stanek[17].

The reduction of current account deficits with achieving more sustainable growth by Kazandziska[18] indicates that foreign economic policy and the industrial policy should be given high priority. The functionality of the economic development in emerging countries which are on their way of joining a currency union based on the concept of macroeconomic policy regimes (MPRs) were examined by this paper. The consideration of functional MPRs are the delivery of sustainable economic growth, employment and more equitable income distribution. The economies are embedded in a macroeconomic policy regime consisting of foreign economic policy, industrial policy, wage policy, monetary policy and fiscal policy, the financial system and the institutional framework.

Latvia will be analysed using a Post Keynesian approach as candidate of emerging countries for currency union. It will be argued that the institutional changes in Latvia have paved the way for a dysfunctional policy mix, such that led to high current account deficits, capital flow fluctuations, large employment losses and instable economic development.

The issue of fiscal sustainability is very important for macroeconomic management. Oshikoya and Tarawalie[19] focus on empirically assess the sustainability of fiscal policy in the countries of the WAMZ using annual time series data for the period 1980 to 2008 and results shows that fiscal policy was weakly sustainable for all the countriesm except Sierra Leone whose fiscal policy was found to be unsustainable. The results support the hypothesis of tax-and-spend for Gambia, Guinea and Sierra Leone, while a bi-directional causality was established for Ghana and Nigeria.

## Summary

Considering the pattern of growth of international trade and bilateral trade among West African countries, the purpose of financial integration in which ECOWAS was created has not been achieved over the years. Instead, ECOWAS countries have more trade with the rest of the world than among member states due to the influence of environmental factors on their foreign exchange market coupled with the major problem to international business all over the world which has been identified to be currencies and the risk associated to currencies. To fill this gap, West African countries have developed a monetary unit called the “Eco” to flag up in 2020 so as to eliminate some of these environmental factors and improve intra-regional trade. The proposed “ECO” currency is expected to be the common currency for countries of West Africa.

The potential rise in trade is considered as one of the conspicuous benefit of a currency union. A country’s advantage and disadvantage from benefiting from a currency union rely on how their economies are joined with those of its future partners. Research shows that the greater two countries trade with each other and the more identical their business cycles are the better choice for a currency union. Recent studies focus on increase in trade as a major effect of joining a currency union with the assumption that increase in trade will boost the growth and development of member countries. Not much has been said about the effect of a currency union on other economic statistics, organisations and the entire population. Empirical studies generally find that the cost of adopting a single currency is too high for most regions and most research focus on either existing currency union or on developed countries.

The study used quantitative and qualitative design and a descriptive explanatory survey design which involves the use of questionnaire. The population of the study include staffs that have spent not less than five (5) years in the foreign exchange department and / or the treasury department of twenty (20) commercial banks in Nigeria out of the twenty one banks as at October 2013 including the Central bank of Nigeria. The data were used to ascertain expert’s view of the proposed currency “ECO” from the countries perspective. The primary data were analysed using simple linier regression to determine the relationship between the dependent and the independent variable. Bivariate analysis and The Pearson product-moment correlation coefficient was used to measure the strength and intensity (dependence) between two variables X and Y.

Based on the results of the empirical analysis, adoption of a common currency in ECOWAS zone would have a positive significant impact on sustainable economic development.

The theory of the optimal currency area was pioneered by economist Robert Mundell describes the optimal characteristics for the merger of currencies or the creation of a new currency. The theory is used often to argue whether or not a certain region is ready to become a currency union, one of the final stages in economic integration and the theory is used as a foundation of a common currency.

## Conclusion

In conclusion, ECOWAS has proposed to start a common currency between five member states in 2020. One of the main reasons for the instigation of this currency is to reduce the problem of low intra-trade. Since 1995, West Africa Monetary Agency (WAMA) has been preparing member states for this proposed currency.

A common currency can improve bilateral trade because trades in the currency zone would not have to worry about exchange rates fluctuations. As such it will be easier to move monies from one country to the other in the zone without being scared of currency fluctuations. Common currency also increases intra regional transactions because the currency is implicit to be more stable than individual country currency.

**Recommendations:** The study has investigated common currency adoption in ECOWAS countries and its impacts on sustainable economic development Based on the finds, conclusions were drawn. These recommendations are then made to towards improving bilateral trade in ECOWAS region:

Regional trade policies should be made known to the general public as this will improve bilateral trade within ECOWAS community. This is because the study showed that most experts did not know much about the trade policies available. The availability of trade policies will encourage traders to exploit more trade opportunities in the community. The community should encourage member countries to strive to meet both the primary and secondary criteria of the monetary union as soon as possible so that member countries would have had a stable economy long before transiting into a monetary union as a stable economy will aid smooth transition into a currency union.

The community should ensure equal pay and equal rights for work of equal value for all so as to aid labour mobility and encourage the growth of all member states. The level in which labor forces are mobile can influence how fast an economy can adjust to technological fluctuations, how rapid competitive advantages can be used and how innovative industries flourish. This study recommends the community to address most of the issues of these internal and external shocks before the commencement of the common currency as these shocks may have adverse effects on business factors.

**Contributions to Knowledge:** This study has provided meaningful and valuable insight into the proposed common currency and its impact on international business. It has contributed to knowledge and expanded the current literatures on ECOWAS proposed currency, monetary union and international business. Stated below are the specific contributions to the existing body of knowledge in the area of monetary union and international business and finance in general.

The study contributed to the comprehension of the concept of international business in the area of bilateral trade. This study also contributes to scholars' better understanding of the development of the monetary union or an optimum currency area, and of the structure of knowledge within connections between theories and authors. The study also shed some light on the concept of sustainable economic development in the present time and in the near future, the concept of labour mobility and exchange rate volatility within countries and concept of economic indicators and business cycle.

The study reviewed some of the valuable additions to the theory of optimum currency areas of Mundell's[7] Many additional measures have been brought in and the theory has served as a valuable aspect in creating any monetary union. This study therefore contributed to the theory of optimum currency by introducing the concept of sustainable economic development and by using bilateral trade, economic activities, labour mobility, business cycle synchronisation and sustainable economic development as variables that influence an optimum currency area.

Little work has been done on the impact of a proposed monetary union in developing countries. The study carried out analysis of the proposed currency using experts view to determine the impact of the currency. It also used the gravity model to predict the impact of the currency on international business. The researcher considered experts who are directly linked to foreign trade/ international business in Nigeria been the largest West African country accounting to about 60% of its total population. The study therefore contributed to the empirical studies in the body of knowledge on monetary union.

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