

The franc zone

The franc zone is an economic, monetary and cultural area that is equivalent to none other in the world. It is made up of very diverse states and territories and results from developments and changes in the former French colonial empire. After attaining their independence, most of the newly-created African states decided to remain within a homogenous group characterised by a new institutional framework and a common exchange rate mechanism.

The franc zone is made up of France and 15 African states: Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger, Senegal and Togo in West Africa, Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea and Gabon in Central Africa, and the Comoros.

The franc zone is a rare example of close institutionalised cooperation between countries from two continents that share a common language and history.

The Banque de France has developed close ties with the franc zone central banks, with which it works towards ensuring the smooth functioning of the area's shared institutions.

This Fact Sheet describes the franc zone's institutional structures and the changes they are undergoing, and brings to the fore the franc zone countries' determination to forge ahead with regional integration in order to support growth and reduce poverty.

The franc zone annual report provides detailed information on the economic and financial situation of the franc zone. It is published by the Banque de France and available on its website

www.banque-france.fr

n° 127

April 2002
updated
July 2010

Communication
Directorate

1. HISTORY OF THE FRANC ZONE

1.1. The colonial period

Although it acquired its name relatively recently, i.e. in 1939 with the setting up of foreign exchange controls, the franc zone was in fact created well before the Second World War. In the French colonial empire, the currencies of the various African territories were pegged to the franc used in Metropolitan France, forming a monetary area¹.

Initially, France exercised its sovereignty in its colonies by imposing the French franc as legal tender. In the second half of the nineteenth century, it decided to progressively organise local banknote issuance and entrusted private banks such as the Banque de l'Algérie, Banque de l'Indochine, Banque de l'Afrique occidentale and Banque des Antilles with this task. Generally, special tokens were issued in return for the withdrawal of local currencies (such as manillas and cowrie shells) or foreign currencies circulating in these territories.

By doing this, the French government acknowledged the need to adapt the distribution of credit to the local environment rather than grant additional privileges to the Banque de France.

In order to guarantee the quality of currency circulation, local issuing banks were strictly supervised by the French government. This supervision was strengthened as trade between Metropolitan France and its colonies expanded.

After World War I, issuing banks acquired new bank statutes which subjected them to more stringent requirements and mechanisms were set up to exchange banknotes with those issued by the Banque de France at a rate of one to one. French banknotes progressively replaced colonial tokens and remained the only currency in circulation in sub-Saharan Africa and the Pacific territories. The first *comptes d'opérations* or « operational accounts »

were thus created at the start of the 1920s; they were to play a key role in the organisation of financial relations within the franc zone.

Nonetheless, the area only attained a high degree of cohesion during World War II. The inconvertibility of the franc and the setting up of foreign exchange controls in 1939 helped define an area within which currencies were convertible and shared common rules vis-à-vis third countries. The Decrees of 1939 made the franc zone official, while the monetary reform of 26 December 1945 led to the creation of the CFA (for France's African colonies) and CFP (for France's colonies in the Pacific) francs — which were higher in value than the French franc — making it necessary for these countries to mint their own coins. Up until 1967, a country was considered to belong to the franc zone if it was on the official list of territories that were not subject to French foreign exchange controls.

Following the interruption of trade relations between France and a number of its colonies during the war, General De Gaulle entrusted the *Caisse centrale de la France libre*, set up in 1941, with the task of issuing banknotes, in particular in French Equatorial Africa and Cameroon. This marked the start of a move towards the transfer of the responsibility for issuing banknotes from private banks to public banks. This trend gained momentum after World War II, spurred by the nationalisation process in Metropolitan France. The Banque de l'Algérie was nationalised in May 1946 and the Banque de Madagascar et des Comores became a semi-public banking institution in 1950. The issuing bank of French West Africa and Togo and that of French Equatorial Africa and Cameroon were set up in 1955.

The move towards the rationalisation of the franc zone also led to the creation, under Article 30 of the Act of 24 May 1951 concerning the special Treasury accounts, of a technical liaison committee in 1951, officially named the franc zone Monetary Committee in 1955. It was in charge of monitoring monetary relations between member territories and co-ordinating the activities of the various issuing banks. However, its role diminished as from 1958 as a result of the changes in the issuance

arrangements in French West Africa and French Equatorial Africa and the fact that some overseas territories had been granted internal autonomy.

Therefore, just before the French colonies attained independence, the franc zone was a highly centralised area characterised by common foreign exchange controls, the pooling of foreign exchange reserves and the free convertibility of the currencies in the area on a fixed peg basis.

The exchange rates of the CFA and CFP francs were fixed at FRF 1.7 and FRF 2.4 respectively, reflecting the differentiated price developments during the war, and later increased to FRF 2 for the CFA in October 1948 and FRF 5.5 for the CFP franc in September 1949: these parities were then adjusted following the changeover to the new French franc, to stand at FRF 0.020 and FRF 0.055 respectively.

1.2. Independence

The attainment of independence by France's former trust territories between 1954 and 1962 did not lead to the break-up of the area².

France's cooperation with its partners was considerably altered by the fact that France recognised the franc zone sub-Saharan African countries' right to have their own currency and issuing bank.

The agreements signed between 1959 and 1962 by the franc zone member countries laid down the principles governing the monetary organisation of the area up until 1972-1973. This phase was characterised by progress in the monetary integration of franc zone member countries.

In April 1959, six newly independent West African states (Côte d'Ivoire, Dahomey³, Upper Volta⁴, Mauritania, Niger and Senegal), subsequently joined by Togo in 1963, formed the Central Bank of West African States

1— In a broad sense, a currency area can be defined as the coexistence of an anchor currency and a number of satellite currencies. The unity of the area is ensured by the convertibility of all the currencies in the area on a fixed peg basis. Its cohesion vis-à-vis other countries or areas may stem from the application of harmonised or common foreign exchange controls. A multi-country currency area generally requires a broader framework with close political and economic ties.

2— The following countries left the franc zone: Lebanon (1948), Morocco, Algeria and Tunisia (between 1956 and 1962), and Guinea-Conakry (1958). The states of former Indochina were provided with their own currency under the terms of the Agreements of December 1954.

3— Dahomey became Benin on 30 November 1975.

4— Upper-Volta became Burkina Faso on 4 August 1983.

(Banque centrale des États de l'Afrique de l'Ouest – BCEAO) — which was to replace the *Institut d'émission d'AOF et du Togo* — to manage their common currency, the CFA franc (CFA: *Communauté financière africaine*).

The Treaty establishing West African Monetary Union (WAMU) essentially covers the rules governing monetary issuance, the centralisation of foreign exchange reserves, the free circulation of currency units and the free movement of capital within the Union.

Following serious financial difficulties, Mali, which had opted to set up its own issuing bank and currency, applied to join WAMU in 1967. Its entry into WAMU came into effect on 1 June 1984 when Mali transferred its issuing rights to the BCEAO following a process of financial consolidation.

In Central Africa, five states (Cameroon, Central African Republic, Chad, Congo and Gabon) formed the Central Bank of Equatorial African States and Cameroon (*Banque centrale des États de l'Afrique équatoriale et du Cameroun – BCEAEC*) in 1959. It replaced the *Institut d'émission de l'Afrique équatoriale et du Cameroun* and was put in charge of managing the issuance of the CFA franc (CFA: *Coopération Financière en Afrique Centrale*), whose parity with the French franc was identical to that of the West African currency. As in the case of the BCEAO, an operational account was opened at the French Treasury for the BCEAEC.

Cooperation agreements signed between Madagascar and France in June 1960 led to the creation of the Malagasy franc, whose exchange rate with the French franc was the same as that of the CFA franc. In 1962, issuing rights were transferred to the Malagasy issuing bank. In 1973, however, Madagascar left the franc zone.

The lifting of foreign exchange controls in France in 1967 marked a new phase in the history of the franc zone. Applying common foreign exchange controls was no longer a criterion for belonging to the franc zone. Since 1968, the franc zone has been limited to countries that have signed monetary cooperation agreements with France and whose issuing banks therefore hold an operational account at the French Treasury.

The member countries' desire to change

**1 euro =
655.957 FCFA**

**1 euro =
491.96775 FC**

the distribution of power within the franc zone and to extend the remit of central banks led to the signing of new monetary cooperation agreements in 1972 and 1973.

France's presence on the Boards of the BCEAO and the BEAC (*Banque des États de l'Afrique centrale*, Bank of Central African States), which followed on from the BCEAEC, was thus significantly reduced.

Likewise, the headquarters of the BEAC and the BCEAO were effectively transferred to Africa (Yaoundé, Cameroon, for the BEAC and Dakar, Senegal, for the BCEAO) in 1977 and 1978 respectively, and a large number of managerial posts in each bank's head office and national branches were assigned to African executives.

In both issuing areas, the 1972-1973 reforms strengthened the powers of the Boards of Directors in terms of bank lending, in particular regarding medium and long-term loans to the economy and loans to general government, and gave central banks the means to play a more decisive role in the economic development of member countries.

The parity of the CFA franc remained unchanged up to 11 January 1994 when it was devalued by 50% against the French franc (1 CFA franc = FRF 0.010).

The independence of the Comoros in 1976 was accompanied by the maintenance of the issuing rights of the Issuing Bank of the Comoros (*Institut d'émission des Comores*), replaced by the Central Bank of the Comoros on 1 July 1981. The parity of the Comorian franc was equivalent to that of the CFA franc. In 1994, this parity was annulled with the 33% devaluation of the Comorian franc (1 Comorian franc = FRF 0.0133).

1.3. Pegging the CFA franc to the euro

On 1 January 1999, the euro became the currency of 11 European Member States of Economic and Monetary Union (EMU) and the French franc became a non-decimal subdivision of the euro. The euro replaced the French franc as the monetary anchor of the CFA and Comorian francs. This substitution automatically determined the euro parity for the CFA and Comorian francs. It in no way affected franc zone monetary cooperation mechanisms⁵.

Pegging to the euro did not result in a change in parities for the CFA and Comorian francs. On 31 December 1998, the Council of the European Union fixed the irrevocable conversion rate between the euro and the French franc (1 euro = FRF 6.55957). This rate automatically determined the value of the euro to the CFA and Comorian francs. As the CFA franc was previously exchanged at the rate of FCFA 100 to FRF 1, the parity of the CFA franc became 1 euro = FCFA 655.957. Similarly, as the Comorian franc was exchanged at a rate of FC 75 to FRF 1, its parity became 1 euro = FC 491.96775.

⁵— The Council Decision of 23 November 1998 concerning exchange rate matters relating to the CFA franc and the Comorian franc confirmed that France may continue its present agreements concerning exchange rate matters with the UEMOA (*Union économique et monétaire ouest-africaine*), the CEMAC (*Communauté économique et monétaire de l'Afrique Centrale*) and the Comoros (Article one of this Decision).

2. FRANC ZONE INSTITUTIONS AND MECHANISMS

2.1. The institutions

The management of monetary unions is reliant on a structured institutional organisation that makes it possible to centralise monetary transactions while taking into account the economic and political imperatives of each of the Union's member countries.

2.1.1. West African Economic and Monetary Union

The Treaty on West African Economic and Monetary Union (WAEMU) was signed by the Heads of State of Benin, Burkina Faso, Côte d'Ivoire, Mali, Niger, Senegal and Togo meeting in Dakar on 10 January 1994. It was conceived as an addition to the Monetary Union that was set up in 1973⁶. A Provision was made for the possible enlargement of the Union from the eight core member countries⁷ to other countries of the sub-region. The WAEMU Treaty has four main strands: harmonisation of the legal and regulatory framework, setting up of a common market, multilateral surveillance of macroeconomic policies and coordination of national sectoral policies in the major economic areas.

The institutions of the WAEMU

The Conference of Heads of State, the Council of Ministers, the Central Bank of West African States (BCEAO) and the Banking Commission (see Appendices 1 and 3).

The Conference of Heads of State and Government

The Conference is the supreme authority of the Union and settles all issues that have not been resolved by unanimous agreement within the Council of Ministers. It decides on the accession of new member countries and takes cognizance of the withdrawal or exclusion of participants. It meets at

least once a year and takes its decisions unanimously. The Conference is held for one calendar year and in alphabetical order in each member country. The presidency is conducted by the head of the member country in which the Conference is held.

The Council of Ministers

It is charged with monitoring the implementation of the guidelines and decisions laid down by the Conference of Heads of State and Government. It defines the regulatory environment for banking and financial system activity and for the Union's exchange rate policy. It also defines the guidelines for bolstering the monetary and financial integration of member countries and establishes the Union's exchange rate policy, in consultation with the BCEAO.

Each member country is represented by two ministers, including the finance minister, and has only one vote, which is cast by the finance minister. The Commission, the BCEAO and the West African Development Bank (BOAD) organise the meetings of the Council of Ministers and its secretariat. The Governor of the BCEAO attends Council meetings and has an advisory vote. The Council meets at least twice a year and takes its decisions unanimously. The Council appoints one of the finance ministers to chair its meetings. This minister shall serve a two-year term. The persons appointed in their quality of finance minister shall chair the Council on a rotating basis.

The WAEMU Commission

The Commission was established on 30 January 1995 pursuant to the WAEMU Treaty. Its head office is in Ouagadougou (Burkina Faso).

The Commission transmits, to the Conference of Heads of State and the Council, recommendations and opinions that it deems useful for the upholding and development of the Union. It has, by delegation from the Council, the power to carry out the acts taken by the latter. It executes the budget of the Union. It may refer member countries' non-compliance with their obligations to the Court of Justice in accordance with the WAEMU Treaty.

The Commission forms part of the institutional architecture of the multilateral surveillance of macroeconomic policies. It carries out an assessment of the convergence process semi-annually (See 3.1.1. below).

The commission is made up of eight members, appointed by the Conference of Heads of State for a renewable four-year term. Its President is appointed among the commissioners by the Conference of Heads of State. The Governor of the BCEAO participates as of right, with an advisory vote, in the Commission's meetings.

The Central Bank of West African States (BCEAO)

The BCEAO is an international public institution whose head office is in Dakar (Senegal).

The BCEAO defines and implements monetary policy in the WAMU, ensures the stability of the Union's banking and financial system, implements the WAMU's exchange rate policies under the terms set out by the Council of Ministers and manages the official foreign exchange reserves of member countries. The Bank has the exclusive right to issue currency units in the member countries of the Union.

The primary objective of the BCEAO's monetary policy is to ensure price stability. Without prejudice to this objective, the Bank supports the WAEMU's general economic policies.

The Governor is at the helm of the central bank. He is appointed by the Conference of Heads of State for a renewable six-year term. He is assisted in his tasks by Deputy Governors, appointed by the Council of Ministers, for a renewable five-year term.

A Monetary Policy Committee (MPC), chaired by the Governor, is charged with defining monetary policy and its instruments in the WAMU. In addition to the Governor, the MPC includes the Deputy Governors of the BCEAO, a member from each of the governments of the Union, a member appointed by France and four members who are nationals of WAMU countries appointed on an *intuitu personae* basis by the Council of Ministers.

⁶– The texts governing Monetary Union (in particular the treaty on West African Economic and Monetary Union (WAEMU), the statutes of the BCEAO and the agreement concerning the Commission bancaire) were revised under the institutional reform of 1 April 2010.

⁷– Guinée-Bissau joined West African Monetary Union in January 1997.

The Executive Board is responsible for issues relating to the management of the central bank. It includes the Governor of the BCEAO, a member appointed by each government of the Union and a member appointed by France. The Executive Board is chaired by the Governor and, when he is unable to attend, by one of the Deputy Governors.

The BCEAO has in each member country a branch to which is attached a National Credit Council. Chaired by the finance minister, the National Credit Council examines, in each member country, the functioning of the banking and financial system and the conditions for the financing of economic activity.

The Banking Commission

Set up in 1990, the Banking Commission has its head office in Abidjan (Côte-d'Ivoire). It carries out on and off-site inspections of the Union's authorised credit institutions. It must be consulted, and its assent obtained, for the authorisation or the revocation of authorisation, of a credit institution. It contributes to defining the prudential regulations applicable to the Union's credit institutions.

The member of the Banking Commission are:

- the Governor of the BCEAO, who chairs the Commission;
- a representative chosen or appointed by each of the WAMU member countries; this representative is the Head of the Treasury or the head of the institution responsible for supervising credit institutions;
- a representative of the French State;
- nine members appointed by the Council of Ministers of the Union, on the proposal of the Governor of the BCEAO, selected for their expertise in the banking arena.

2.1.2. In the Central African Economic and Monetary Community (CEMAC)

The treaty instituting the Central African Economic and Monetary Community (CEMAC), signed on 16 March 1994, resulted in the creation of two entities: an economic union and a monetary

union. The aim was to enable member countries to advance from the existing cooperation arrangements to a union, thus completing the regional integration process.

Four institutions attached to the CEMAC were set up (see Appendix 3):

- Central African Monetary Union (CAMU);
- Central African Economic Union (CAEU);
- the Community Parliament;
- the Community Court of Justice.

The main bodies of the Community

- the Conference of Heads of State;
- the Ministerial Committee of the CAMU;
- the Council of Ministers of the CAEU;
- the Commission of the CEMAC;
- the Bank of Central African States (BEAC);
- the Central African Banking Commission (COBAC).

The Conference of Heads of State

The Conference defines Community policy and steers the actions of the Council of Ministers of the CAEU and the Ministerial Committee of the CAMU. It decides on the accession and withdrawal of new members. It establishes the head offices of Community institutions and bodies and appoints their managers. It is chaired by each member country in turn in alphabetical order for one calendar year. The Conference meets at least once a year on a consensus basis.

The Ministerial Committee of the CAMU

It examines the broad guidelines of the different economic policies conducted by the member countries of the Monetary Union and ensures their consistency with the common monetary policy.

Each member country is represented in the Ministerial Committee by two ministers, and has only one vote, which

is cast by the finance minister. The Ministerial Committee has a rotating presidency. It is held by ministers of finance for one calendar year and in alphabetical order of the member countries. The Ministerial Committee meets at least twice a year.

It is charged with applying the CAMU agreement and transmitting to the Conference of Heads of State any recommendations that may result in amendments. It decides on the increase or reduction of the capital of the BEAC, gives its assent to proposals on the modification of the statutes of the BEAC, ratifies its accounts and decides, on the proposal of the Board of Directors, on the appropriation of income. Decisions on such issues must be taken unanimously.

The Council of Ministers of the CAEU

It manages the Economic Union in accordance with the CAEU agreement.

In particular, it has jurisdiction to rule on matters related to the functioning of the common market and those concerning the harmonisation of tax laws in the area of financial and economic activities. Charged with the coordination of national policies, it defines the common policies to adopt in the following sectors: agriculture, livestock, fisheries, industry, energy, trade, tourism, transport and telecommunications, environmental protection, education, research, and vocational training. Lastly, the Council of Ministers is responsible for conducting the exercise of multilateral surveillance (See 3.1.2. below).

The CEMAC Commission

The treaty instituting the CEMAC sets out the structures underpinning the creation of a sub-regional common market and specifies the multilateral surveillance methods, which are monitored by the Executive Secretariat of the CEMAC. The Executive Secretariat has its head office in Bangui. It is responsible for the smooth functioning of the Economic Union. It may make proposals to the Council of Ministers and is in charge of supervising the application of the Treaty and community decisions, managing the budget of the CAEU and community action programmes.

In the framework of the reform of regional institutions undertaken in March 2006, the Executive Secretariat became the CEMAC Commission, in accordance with the decisions taken on 25 April 2007 by the Conference of Heads of State at its N'Djaména meeting. The Commission comprises one Commissioner per member country and is managed by a President and a Vice-President, both appointed by the Conference of Heads of State. The President of the Commission is appointed for one renewable five-year term.

The Bank of Central African States (BEAC)

The BEAC is an international public institution whose head office is in Yaoundé (Cameroon).

The main tasks of the central bank are to define and steer the Union's monetary policy, manage exchange rate policy and the official reserves of the member countries, and to promote the smooth operation of payment and settlement systems. It has the exclusive right to issue currency units in the member countries of the Union.

The primary objective of the BEAC is to ensure the currency's stability. Without prejudice to this objective, the BEAC supports the general economic policies of the Union.

In the framework of the reform of CEMAC institutions, a new organisation of the BEAC and the amended statutes were adopted in September 2007 by the Ministerial Committee of the CAMU and the Board of Directors of the central bank.

The Bank's governing authorities are made up of six members: the Governor, the Deputy Governor, the Secretary General and three Directors General.

The Governor is appointed unanimously by the Conference of Heads of State, on the proposal of the Ministerial Committee of the CAMU and with the assent of the Bank's Board of Directors acting unanimously. He serves a non-renewable seven-year term. The other members of the Bank's governing authorities are appointed under the same conditions as the Governor, for a non-renewable six-year term.

A Board of Directors made up of 14 members, i.e. two directors from each member country and two from France, administers the central bank and ensures its smooth functioning. The directors are appointed by their respective countries for a three-year renewable term. Following a reform of the statutes of the central bank agreed on in March 2010, the presidency of the Board of Directors of the BEAC is held by the incumbent President of the Ministerial Committee of the CAMU.

The Monetary Policy Committee (MPC) is responsible for the BEAC's monetary policy and the management of foreign exchange reserves. Chaired by the Governor of the BEAC, the MPC counts 14 voting members, i.e. two per member country, including the national director of BEAC, and two from France. The chairman of the MPC only votes in the event of a tie.

The BEAC has a national branch in each member country to which is attached a national Monetary and Financial Committee, made up of the ministers representing the member country in the Ministerial Committee, representatives of the member country in the Board of Directors of the BEAC and the MPC, a prominent personality appointed by the government of the member country and the Governor. Each Committee is chaired by the finance minister of the member country.

Supervised by the MPC and the Board of Directors of the central bank, the national Monetary and Financial Committee makes proposals regarding the coordination of the national economic policy with the common monetary policy and proposes to the MPC monetary and credit targets and the maximum level of refinancing of the member country.

The Central African Banking Commission (COBAC)

The COBAC was set up in January 1993. It is charged with ensuring that credit institutions comply with the legal and regulatory provisions laid down by the national authorities, the BEAC or by itself, and with sanctioning any violations. In this respect, the COBAC carries out on and off-site inspections of credit institutions and contributes to

defining the prudential regulations of the area's banking system.

The COBAC is chaired by the Governor of the BEAC assisted by the Deputy-Governor. It also includes: the three censors of the BEAC; seven members selected for their expertise in banking, finance and law, appointed for a three-year term, twice-renewable on the proposal of the Governor, by the Board of Directors; a representative of the Prudential Supervisory Authority appointed by the Governor of the Banque de France. Decisions are taken at a two-thirds majority of votes cast. Changes in the statutes of the COBAC are made by a unanimous decision of the Board of Directors. The General Secretariat of the COBAC is in Yaoundé (Cameroon).

2.1.3. In the Comoros

The Central Bank of Comoros (BCC) is a public institution. Its head office is in Moroni. In the economic policy framework defined by the government of the Union, its tasks are to formulate monetary and credit policy, exercise the surveillance and supervision of banking activities and ensure the enforcement of foreign exchange controls. It has the exclusive right to issue currency in the Union of the Comoros.

The BCC is administered by a Board of Directors made up of no more than eight members, half of whom are appointed by the Comorian government and the other half by the French government. They serve a renewable four-year term. The President of the Board of Directors is chosen by the Board amongst its own members on the proposal of the government of the Union of the Comoros. The Board's deliberations are adopted by absolute majority.

The Governor of the Bank is appointed by the President of the Union on the proposal of the Finance minister and with the assent of the Bank's Board of Directors. He holds a renewable five-year term. He has an advisory vote on the Board of Directors.

The Governor is assisted by a Deputy Governor appointed by the Board of Directors for a renewable four-year term.

Two censors, appointed for a four-year term, one by the French government and the other by the Comorian government,

attend Board meetings and have an advisory vote.

2.2. The mechanisms

The Monetary Union formed by franc zone countries functions according to principles inherent to this type of association, to which may be added specific features arising from the implementation of monetary cooperation between France and the countries concerned.

2.2.1. Principles of monetary cooperation between France and the African countries of the franc zone

These principles were set out in the monetary cooperation agreement of 23 November 1972 signed by the member countries of the issuing area of the Bank of Central African States and France, and also in the cooperation agreement signed by the member countries of the West African Monetary Union and France on 4 December 1973.

There are four core principles:

- unlimited convertibility guarantee from the French Treasury: the convertibility of currency issued by the various franc zone issuing banks is guaranteed with no limits by the French Treasury;
- fixed parity with the anchor currency: the parity of the currencies of the area with the euro is established and defined for each sub-area. The currencies of the area are convertible among themselves, at fixed parities, with no limit on amounts;
- in principle, transfers are free within the area;
- pooling foreign exchange reserves: foreign exchange reserves are pooled at two levels, (i) the states pool their reserves in each of the two central banks; (ii) in return for the unlimited convertibility guaranteed by France, central African banks

are obliged to deposit a proportion⁸ of their foreign exchange reserves⁹ with the French Treasury, on the operational account held for each bank. Since 1975, these assets have enjoyed an exchange guarantee vis-à-vis SDR¹⁰.

2.2.2. Operational accounts

The previously defined principles are implemented via the application of a specific mechanism, the operational account, whose operating procedures are laid down in agreements signed by the French minister of Finance and the representative of each of the issuing banks of the franc zone.

Their functioning

Operational accounts are sight accounts held with the French Treasury for each of the three issuing banks. These accounts are interest-bearing and offer unlimited overdraft facilities.

Safeguard mechanism

While the central banks may have unlimited recourse to advances from the French Treasury, in the spirit of the agreements, this facility must be used on an exceptional basis. Certain measures, some of which are preventive, have been defined to prevent the operational accounts from being permanently in debit:

- the statutes of the BCEAO specify that when the liquid funds available on the operational account are projected to be insufficient to meet future settlements, the central bank must replenish the operational account by drawing from the liquid

8– This proportion was reduced from 65% to 50% for the net external assets of the BCEAO, in accordance with the amendment of 20 September 2005 to the operations account agreement of 4 December 1973. In accordance with the new operations account agreement of the BEAC signed on 5 January 2007, this proportion has been gradually lowered and has stood at 50% since 1 July 2009.

9– With the exception of sums necessary for their cash flow and those relating to their transactions with the International Monetary Fund.

10– The SDR is the unit of account for the International Monetary Fund. Its value is determined daily on the basis of a basket of four currencies (the US dollar, the euro, the British pound and the yen).

funds that it has constituted in foreign currencies, requesting that foreign currencies held by public or private institutions of member countries be transferred to the central bank in exchange for CFA francs (known as *ratissage*), and calling upon member countries to make use of their drawing rights on the International Monetary Fund. Similarly, a *ratissage* clause is provided for in the operational account agreements of the BEAC and the BCC;

- the statutes of the BEAC state that when the operational account is in deficit for three consecutive months, maximum refinancing amounts should be reduced by 20% in the countries with a deficit on the operational account and 10% in the countries with a surplus of less than 15% of currency in circulation as a ratio of this position. The MPC of the BEAC is immediately convened to decide on the appropriate recovery actions to implement in the deficit countries;
- lastly, the statutes of the central banks (BEAC and BCC) specify that their advances to national treasuries may not exceed 20% of the ordinary budget revenues received in the last fiscal year. In the WAMU, direct monetary assistance to member countries is henceforth unauthorised, in accordance with the amended statutes of the BCEAO.

2.2.3. Cooperation with France

In addition to frequent informal meetings between French and African officials, franc zone ministers of Finance and central bank Governors meet on a half-yearly basis.

The first such meeting was held in Paris in March 1965. It was decided on this occasion that the ministers would meet twice a year, in April, just before the IMF's International Monetary and Financial Committee (IMFC) and the World Bank's Development Committee, and in September-October just before the annual meetings of these two institutions.

3. REGIONAL INTEGRATION

3.1. Convergence and multilateral surveillance of macroeconomic policies

The convergence of macroeconomic policies aims to ensure the consistency and effectiveness of national economic policies within monetary unions, with a view to fostering sustainable and balanced growth. Convergence is therefore one of the guarantees of the stability of the single currency.

3.1.1. Convergence within WAEMU

Pursuant to Articles 63 to 75 of the WAEMU Treaty of 1994, multilateral surveillance was based, up to 1999, on directives¹¹ adopted by the WAEMU Council of Ministers. By virtue of these directives, member countries were to meet five indicators of convergence ensuring the compatibility of fiscal policies with the monetary objectives of the Union, particularly price stability. This process was strengthened with the coming into force in December 1999 of the Convergence, Stability, Growth and Solidarity Pact between WAEMU member countries, whose proceedings were adopted during the Conference of Heads of State and Government on 8 December 1999 in Lome, and the WAEMU Council of Ministers held in Dakar on 21 December 1999. The enactment of a community regulation on 21 December 1999 completed the arrangements.

The convergence programme

The Pact distinguishes two separate phases: a convergence phase and a stability phase.

During the convergence phase, member countries define a multiyear convergence programme, which is subject to approval by the WAEMU Council of Ministers. The convergence process is gradual, with each country having to work towards, at its own pace, meeting the Community standards set out for the final phase.

11– Union Directive of 15 January 1996 setting out the institutional arrangements; Union Directives of 20 September 1996, 11 September 1997 and 3 July 1998 on the definition of the criteria.

It is nonetheless specified that the levels of performance achieved by member countries in the process of compliance with convergence standards should not be undermined, except under exceptional circumstances. The state of convergence is assessed on a half-yearly basis by the WAEMU Commission, in accordance with the multilateral surveillance. The Council may adopt corrective measures on the basis of these reports and on the proposal of the Commission.

The Union shall enter the stability phase as soon as countries' critical mass¹² meets the four first-level criteria (see below) and that it is deemed to do so in a sustainable manner. The member countries shall continue to comply with the standards established to guarantee and consolidate the performances achieved. After postponing a number of times, the deadline for meeting the first-level criteria, marking the entry into the stability phase, was set at 31 December 2013.

Convergence criteria and related sanctions

The adoption of the Pact led to the implementation of new convergence criteria, enabling a better assessment of the control of public finances and the convergence of fiscal policies. A distinction was introduced between first-level criteria and second-level criteria.

The ratio of the underlying budget balance to nominal GDP is a key factor. The underlying budget balance measures the government's ability to cover its current expenditure (including interest payments) and its capital expenditure using total revenue (taking into account donations). When entering into the stability phase, this balance must be greater than or equal to 0%. If this criteria is not observed, sanctions may be imposed¹³.

12– This critical mass is deemed to have been reached when at least four member countries representing at least 65% of the GDP of the Union meet the four first-level criteria.

13– There are four types of sanction provided for in the WAEMU Treaty: a press release published by the Council, removal of positive measures from which a member country may have been benefiting, recommendation to the West African Development Bank (BOAD) to review its interventions in its favour, and suspension of WAEMU assistance.

The other first-level criteria include a inflation rate criterion, by which inflation must remain below 3% per year, a prohibition on accumulating internal and external arrears, and a debt ratio limiting the proportion of domestic and foreign debt outstandings to nominal GDP to 70%. Member countries that do not meet one of these criteria must define a programme of corrective measures in consultation with the Commission. In the convergence phase as in the stability phase, deterioration of performance regarding first-level criteria calls for the implementation of corrective measures, even if this deterioration does not result in non-compliance with the defined objectives.

The second-level criteria include four components: the wage bill must not exceed 35% of tax revenues, public investment financed with internal resources must represent at least 20% of tax revenues, the ratio of the current external deficit excluding donations to nominal GDP must not exceed 5% and tax revenues must be equal to or greater than 17% of nominal GDP.

3.1.2. Convergence within the CEMAC

CEMAC member countries have set up a multilateral surveillance system aimed at stepping up the regional integration process. It was accompanied by the collegial monitoring of macroeconomic policies, conducted by the Council of Ministers. Pursuant to Title III of the agreement of 1994 governing the Central African Economic Union, which was ratified in 1999, this monitoring function was transferred to the Executive Secretariat¹⁴ of the CEMAC in 2001.

The Directive of 3 August 2001 set out the criteria and the macroeconomic convergence indicators, which are identical to WAEMU's first-level criteria. The surveillance criteria thus defined must be met by CEMAC countries by a deadline initially established for 31 December 2007¹⁵, except for the inflation criterion that is immediately applicable.

14– The Executive Secretariat became the CEMAC Commission in April 2007 (see above).

15– This deadline was not met and will have to be put back.

In the event of non-compliance with surveillance criteria, the arrangements provide for a Directive addressed to the country concerned.

A country to which a Directive is addressed must define, in consultation with the CEMAC Commission, a multi-annual adjustment programme, aimed at ensuring compliance with the convergence criteria. Non-compliance with this programme may also result in sanctions.

Five second-level criteria have also been defined. They include the four criteria adopted by the WAEMU as well as an indicator of the external coverage rate of the currency by foreign exchange holdings (minimum threshold standing at 20%).

3.1.3. Coordinating convergence within the franc zone

The franc zone Convergence Committee was set up in September 1999 to strengthen the coordination of the convergence process in the two sub-areas. It is a technical forum for co-ordination between WAEMU and CEMAC institutions, the Comoros and France.

The Committee has a two-pronged objective:

- as a forum for consultation, it is charged with drafting a report for franc zone finance ministers on all issues relating to the organisation of convergence if they are of interest to all the franc zone African countries that are members of either of the two monetary unions;
- it is responsible for informing franc zone finance ministers of the multilateral surveillance findings in each area, of recent developments in convergence and programmes implemented to promote convergence especially with regard to the safeguard of franc zone mechanisms.

3.2. The implementation of customs unions

3.2.1. The WAEMU Customs Union

The principle of a customs union was laid down in the WAEMU Treaty. Initially scheduled for 1 January 1998, it actually came into force on 1 January 2000. This resulted in:

- the application of the Common Customs Nomenclature defined in July 1998;
- the adoption of a Common External Tariff (CET) based on four rates: 0% (essential commodities), 5% (primary commodities), 10% (intermediate goods), 20% (final consumer goods) to which may be added a statistical tax of 1% and a solidarity contribution of 1% applied to community institutions;
- the phasing out of customs duties on intracommunity trade of commodities and manufactured goods;
- the implementation of common safeguard measures: a tax applied to manufactured and agrifood products (regressive protection tax of between 2.5% and 5%), a special import tax of 10%, which is applied when international prices fall below the threshold set by the WAEMU Commission.

The CET has resulted in almost all the countries in a decrease in customs duties and the dismantling of non tariff barriers.

3.2.2. The CEMAC Customs Union

The Central African Customs and Economic Union (UDEAC) was set up in 1964 by the Brazzaville Treaty. It brings together six countries (Cameroon, Chad, the Central African Republic, Congo, Gabon and Equatorial Guinea) and aims to create a single market of 25 million inhabitants by facilitating the free movement of goods and factors of production. Nevertheless, the customs tax system remained highly heterogeneous in the different countries with an increase in the number of taxes and special derogation regimes, while 71% of imports enjoyed exemptions.

The CEMAC (which replaced the UDEAC) Treaty of 1994 recalls the objective of setting up a common market

based on the free movement of goods, services, capital and persons and that was to be subsequently completed by, at latest, the end of the second phase of construction of economic union¹⁶. It included a customs reform based on the implementation of a common external tariff and a preferential tariff applicable to trade between the countries of the area.

Initiated in 1994 by the UDEAC, the customs reform resulted in:

- the adoption of a Common External Tariff (CET) applicable to imported goods classified into four categories (5%, 10%, 20% and 30%);
- the adoption of a generalised preferential tariff for trade between countries in the area for products manufactured in the CEMAC countries, reduced to 0% from 1 January 1998;
- the harmonisation and simplification of indirect taxes and the implementation of a tax on turnover.

In addition, the investment codes were brought into line with UDEAC rules, which prohibit customs exemptions.

¹⁶– An amended agreement governing the CAEU was adopted in June 2008, which significantly extends the field of competence of the Community and redefines the schedule of the two-stage completion of the CAEU.

4. GENERAL ASSESSMENT AND PROSPECTS

Fifty years after these African countries attained independence, the assessment of the advantages and constraints arising from membership of the franc zone is to a large extent positive.

For member countries and their partners, franc zone membership brings with it numerous advantages:

- the CFA franc enjoys the guarantee of stability and security, which are positive factors for foreign investors. This aspect was strengthened by pegging to the euro, which did not affect the cooperation agreements between France and the franc zone countries. These countries benefit from the credibility of the European currency, thus helping to reinforce the discipline effects stemming from the franc zone mechanisms, which have hitherto made it possible to contain inflation;
- monetary union has strengthened regional solidarity. The existence of a common currency, combined with free capital flows, is a factor that promotes the development of trade within both the WAEMU and the CEMAC. Intra-regional trade however is still not sufficiently developed, mainly due to the structure of the region's economies. Furthering the regional integration process and harmonising national tax systems should nevertheless underpin intra-area trade;
- a significant offshoot of monetary cooperation within the area is the development assistance provided by France. France provided over one-quarter of the development assistance received by the franc zone countries in 1990-2008.

The franc zone's prospects therefore remain closely hinged on the strengthening of economic unions, which can draw on an ongoing harmonisation process of convergence instruments and the improvement of the coordination of economic policies.

APPENDIX 1 – TEXTS OF CONSTITUTION

Texts relating to the WAEMU

- Treaty of 14 November 1973 establishing the West African Monetary Union (WAMU).
- Cooperation agreement signed by the member countries of the West African Monetary Union and France on 4 December 1973.
- The West African Economic and Monetary Union Treaty of 10 January 1994.
- Statutes of the Central Bank of West African States (BCEAO).

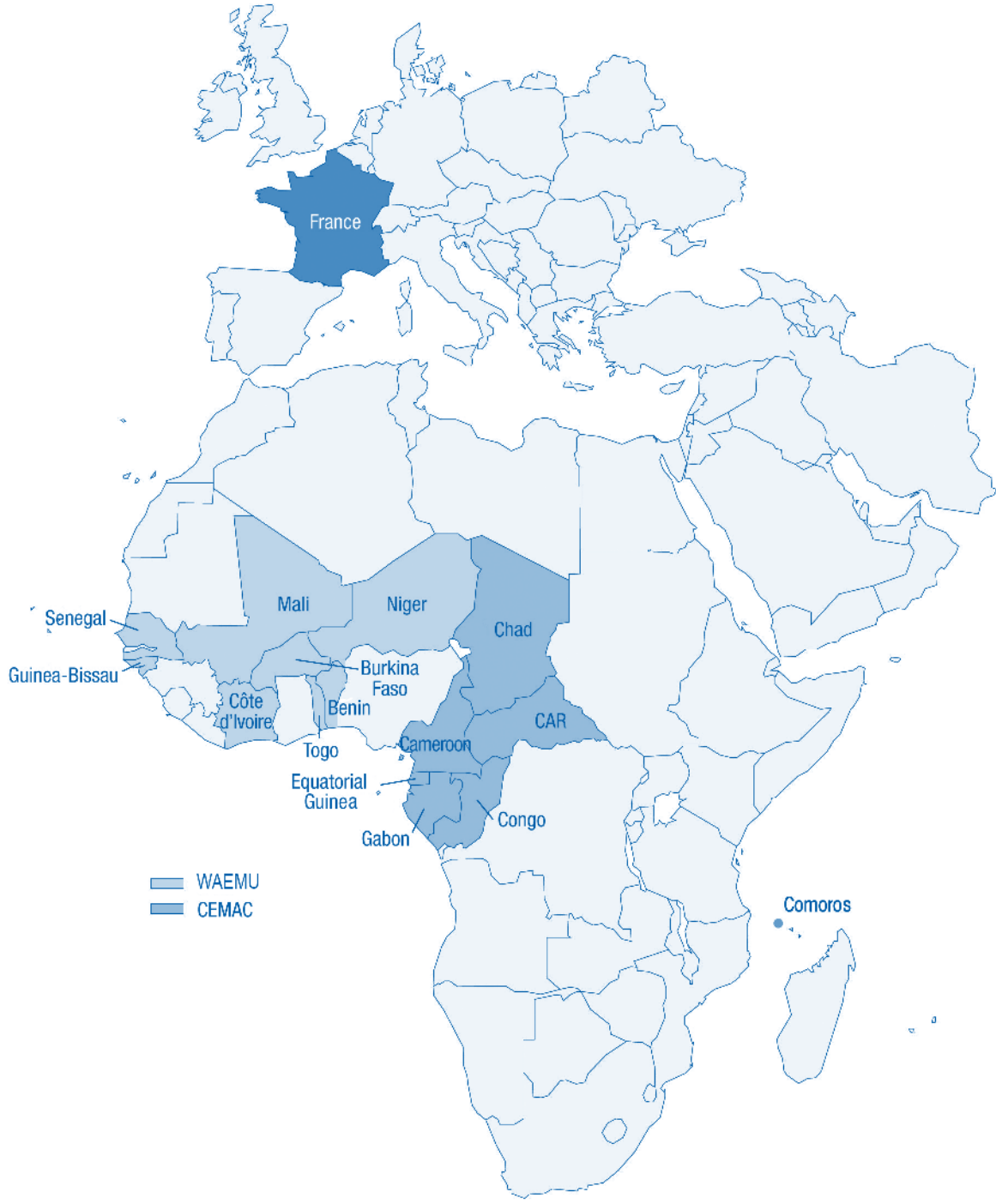
Texts relating to the CEMAC

- Monetary cooperation agreement of 22 and 23 November 1972.
- Treaty of 16 March 1994 establishing the Central African Economic and Monetary Community (CEMAC).
- Agreement governing the Central African Economic Union (CAEU).
- Agreement governing the Central African Monetary Union (CAMU).
- Statutes of the Bank of Central African States (BEAC).

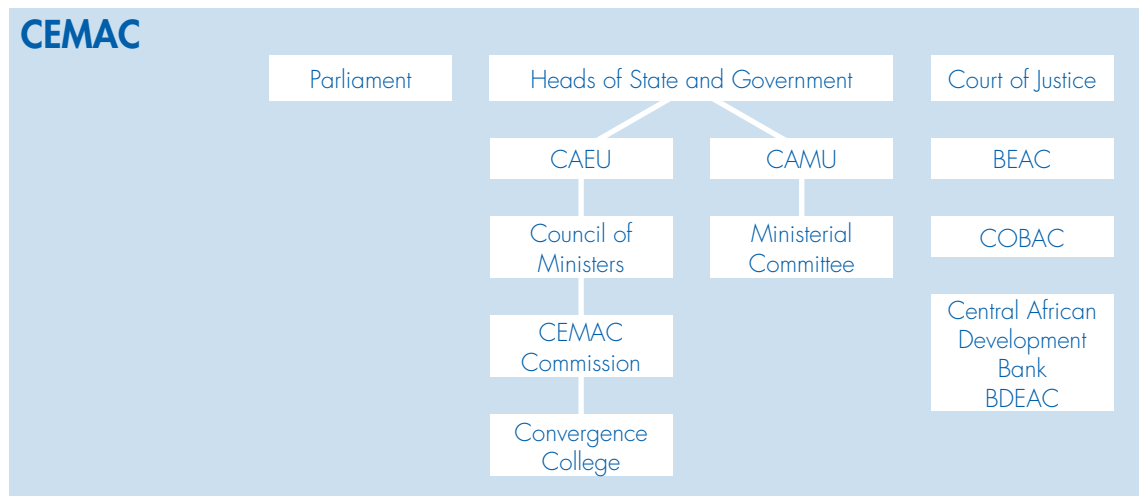
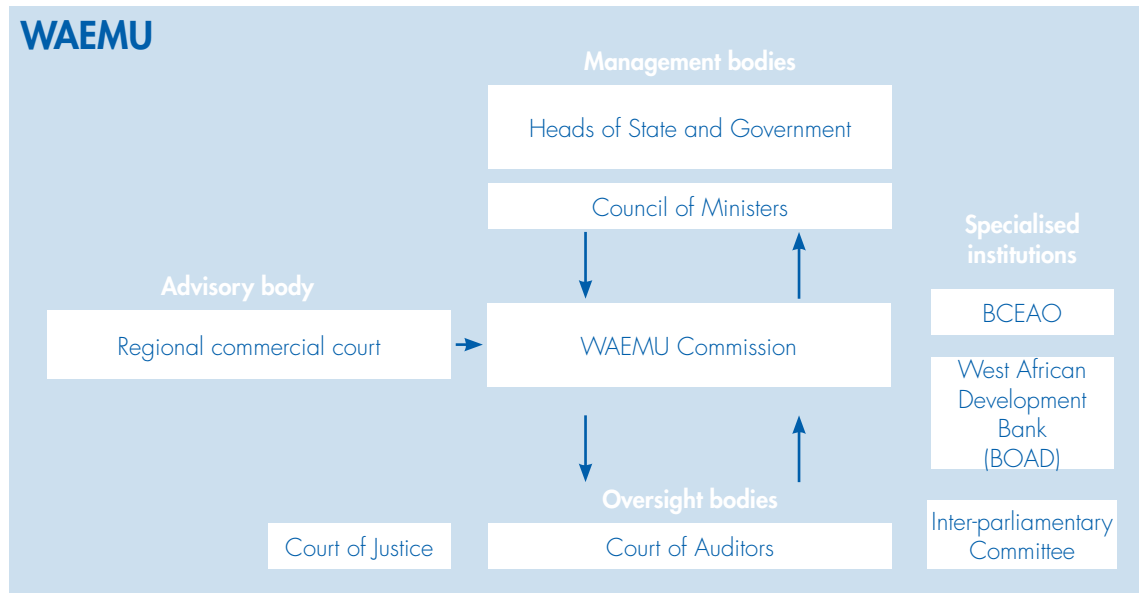
Texts relating to the Comoros

- Monetary cooperation agreement between France and the Federal Islamic Republic of the Comoros of 23 November 1979.
- Statutes of the Central Bank of Comoros.

APPENDIX 2 – FRANC ZONE MEMBER COUNTRIES



APPENDIX 3 – OPERATING FRAMEWORKS



Editor in chief : François de Coustin,
Head of Press and Communication Department

WWW.banque-france.fr
> Europe & international
 > Franc zone

infos @ banque-france.fr

«The present publication may not be represented or reproduced, in whole or in part, without the express permission of the Banque de France, except as provided for under Article L.122-5 2° and 3° a) of the French Intellectual Property Code, or where relevant, within the limits of the terms and conditions laid down in Article L.122-10 of said Code.»

© Banque de France – 2010