CARIBBEAN CENTRE FOR MONETARY STUDIES
XXVII ANNUAL CONFERENCE OF MONETARY STUDIES
ECCB, ST.KITTS
NOV. 8-11, 1995

CURRENCY CONVERTIBILITY, MONETARY MANAGEMENT AND THE DEVELOPMENT OF CAPITAL MARKETS: SOME PARADIGMS FROM SOUTHERN AFRICA

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November 1995

Mr. Chairman, Distinguished Ladies and Gentlemen:

INTRODUCTION

I am delighted to be able to present some empirical perspectives in a paper of some relevance, no doubt, to all of us present here today - involved as we are in academia or the practice of monetary management in the Caribbean. On earlier reflection, the broad topic of monetary convertibility, its relevance to monetary management and their mutual relationships to the structure and emergence of capital markets, struck me as being of growing significance to our own rapidly evolving Commonwealth Caribbean scene. Equally, however, there appears distinct applicability to perhaps the potentially most important and progressive region of Africa today, Southern Africa. Indeed, over the past six years, and especially the last four of these, I was particularly fortunate to witness first hand the unprecedented robust evolution of this sub-region of Africa, from the vantage point of one of the key actors in that part of the world, Botswana, during my tenure with the Bank of Botswana. It has forcefully struck me on many occasions how similar, yet often distinct, are the paradigms in the strategies of monetary and financial development evident in these two emerging regions of the developing world.

In structuring this necessarily overview presentation, I have divided the paper into five sections. **Section 1** briefly presents a macro-economic profile for the last decade or so of the twelve Commonwealth Caribbean countries being surveyed (**The Bahamas, Barbados, Belize, Guyana, Jamaica, Trinidad & Tobago** and the

individual **OECS** countries, **Anguilla, Antigua & Barbuda, Dominica, Grenada, Montserrat, St.Kitts/Nevis, St.Lucia** and **St. Vincent** and the **Grenadines**) and that for the Southern Africa region (**Botswana, Lesotho, Malawi, Mauritius, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe**). Key similarities and differences are highlighted. **Section II** surveys the capital market scene in Southern Africa and the Caribbean. **Section III** examines the issue of currency convertibility and how it relates it to the two regions under survey. **Section IV** examines currency convertibility and some implications for monetary management in both regions. A few closing questions for further consideration are set out in a brief **Section V.**

1. THE SURVEY COUNTRIES

Table 1 sets out a profile of the twenty-six countries being surveyed in this paper. Twelve of these are Southern African and fourteen CARICOM (except Anguilla & Montserrat), which are, however, full members of the OECS). As the Table reveals, Southern Africa is a region of well over one hundred million people, if Tanzania and Mauritius are included (both are strictly not in Southern Africa, but Tanzania is part of the **Southern Africa Development Community (SADC)** and Mauritius part of the **Common Market of East and Southern Africa (COMESA)** - successor to the Preferential Trade Area (PTA) and an important economic force in the region). Both countries are, therefore, included in the analysis of Southern Africa. Southern Africa is a mix of relatively strong economies (S.Africa, Botswana, Mauritius and

TABLE 1: SOUTHERN AFRICA AND THE CARIBBEAN AT A GLANCE
KEY MACRO - PARAMETERS (1985-94)
US$ (1994)

	Popul (mill)	GNP per cap	Total Ext. debt (mill)	External Reserves (mill Gross	Net	Surplus/ Budget Deficit GDP (%)	Total Debt/ GDP (%)	Av. GDP Growth rate (1985-1993)	inflation (mill)
A. SOUTHERN AFRICA									
Botswana	1.4	2800	735	4462	3889	B 8.5	18.3	8.3	12.7
Lesotho	2.0	700	618	373	335	L 3.1a/	45.7	6.7	14.6
Malawi	10.8	140	2033	36		Ma (17.7)	156.2	2.1	17.8
Mozambique	16.0	80	5612			Mo (29.6)	382.5	6.0	54.3
Mauritius	1.1	2980('93)	306('93)	750	750	Mu -		5.8d/	9.0
Namibia	1.5	2030	325	203	4	N (3.7)	11.3	3.2	10.0
South Africa	41.6	3010	1531('93)	2103	4721	Sa (6.7)	-	0.7	13.8
Swaziland	0.9	1190	244	297	214	Sw -	22.1	2.9	11.3
Tanzania	28.5	100		331	-1	T -		1.4d/	23.4
Zambia	9.2	350	7020	192('93)	-12	Za (11.9)	201.6	0.9	89.0
Zimbabwe	11.0	490	4426	492	43	Zm -	77.8	(0.6)	20.5
	124.0								
B. CARIBBEAN	(1993)	(1993)	(Mar'95)					(1985-93) Av. GNP	
Anguilla	-	-	c/	b/		An 1.9			
Antigua/Barbuda	.06	6390	c/	b/		A/B 1.0		2.4	4.8
						BH (1.4)		(0.2)	2.5
Bahamas	.27	11500	398	188	170	BR (2.1)		(0.4)	3.1
Barbados	.26	6240	473	210	128	BE (4.3)		5.7	3.5
Belize	.21	2440	179	27	28	D (2.2)		4.8	4.5
Dominica	.07	2689	c/	b/		G 1.3		4.1	4.1
Grenada	.09	2410	c/	b/		GY (6.1)		0.6	53.5
Guyana	.82	350	2055	246	-308	J 1.6		3.1	26.9
Jamaica	2.5	1390	3652('94)	b/	362	M 1.0		-	-
Montserrat	-		c/	b/		STK 0.5		5.2	5.8
St.Kitts/Nevis	.04	4470	c/	b/		SL 7.0		4.3	3.5
St.Lucia	.14	3040	c/	b/		SV 4.7		4.6	3.8
St.Vincent	.11	2130	c/	b/		TT 0.1		(2.7)	5.9
Trinidad & Tobago	1.30	3730	2061	767	630				
	5.87								

5a) GNP, not GDP
b) ECCB as a whole US$516 mill (Mar '95)
c) ECCB as a whole US$670 mill (Mar '95)
d) 1985-93

Source: World Trade: Southern Africa (1995);
IMF International Financial Statistics: Yearbook 1995

Namibia) and relatively weak ones (Mozambique, Tanzania, Zambia); most are heavily indebted and most still experience sizeable fiscal imbalances (**Table 1**). Yet, some of the strongest growth rates for countries in the world over the past decade have been recorded in Southern African countries (Botswana, Lesotho and even Mozambique, despite the ravishes of persistent wars here in the 1980s). Most of the region's countries have experienced modest inflationary rates in the past decade, Zambia and Mozambique being marked exceptions.

This broad Southern Africa picture contrasts noticeably with the CARICOM region, with a population of at least twenty times smaller, strikingly higher per capita GDP as a group, and with average external debt levels much smaller than Southern Africa. Caricom countries have also experienced in the past decade convergence as a group to modest levels of budgetary deficits and rates of inflation, on balance, historically quite lower than in Southern Africa.

Over and above these, there are several important **similarities** and **differences** between these two regions. These include the fact that:

(a) both regions are moving rapidly to important **market-based structures** in their economies, largely resulting from World Bank/IMF type adjustments and stabilisation type projects (5 of the 10 sample Southern Africa countries and 2 of the 14 Caribbean ones were this year involved in an IMF programme);

(b) both groups have moved aggressively to **integrate** their

economies, Southern African economies being part of a complex and often overlapping network of trade and currency integration effort. As **Table:2** below indicates, these groupings include: (a) **the Southern Africa Customs Union (SACU)** in force since 1910; **COMESA** previously the PTA; **SADC**, previously **SADCC (Southern Africa Development Coordinating Committee)** and the World Bank/IMF/ European Union/ADB sponsored **Cross Border Initiative (CBI). The Common Monetary Area**, since 1986 and previously the **Rand Monetary Area**, is more an Exchange Rate Union than a full Monetary Union, more a currency area. It is therefore different from the ECCA in the OECS group, which has a common currency and a regional monetary authority, the **ECCB**. This is not the case in the **CMA**, where each of the four present members (South Africa, Lesotho, Namibia and Swaziland) has its own currency co-existing with the rand and its own central bank exercising some domestic monetary control discretion;

(c) both groups of countries are increasingly embracing **private sector** activities as a basis for future economic growth, pursuing active programmes of **privatisation** etc. The private sector in Southern Africa is an extraordinarily powerful force;

(d) Southern Africa, as has the Caribbean, has in the past 5-10 years been consistently dismantling **restrictive investment practices**, and radically liberalizing and reforming its trade, financial and fiscal regimes, especially its tax structures (Mozambique, Zimbabwe, Malawi, Botswana and S.Africa being fully active in this area);

(e) with the dismantling of apartheid, the end of the liberation wars in Namibia and Mozambique, **stable democratic governments** are the order of the day in the region, as in the Caribbean.

One key and important **distinction** between the two regions though, is the primary and dominant role of **South Africa**, over 20 times the size of the second largest economy in the region, Zimbabwe. South Africa is already playing a critical role in the post-apartheid development, financial and trade activities in the region. With an extremely diversified structure of production, South Africa is already well extended, both in trade and finance, throughout the rest of the region, despite the patent inefficiencies in its own economic management that the dismantling of apartheid has already made manifest. This phenomenon of a pronounced dominance, in economic terms, of one country by another is not evident in the Caribbean, but raises rather important issues for the prospect of say **Venezuela**, **Mexico** or perhaps **Brazil** in the Caribbean Basin assuming such a role, should the ACS emerge as a viable economic grouping.

(f) Yet another distinction is that one of the smallest countries (by population) in the region, Botswana, for over a decade now has had one of the highest absolute and relative levels of external reserves (almost US$5 billion currently) and stable economic management in the world.

II. CAPITAL MARKET STRUCTURE

There are a few generally accepted preconditions for effective

TABLE 2: REGIONAL INTEGRATION GROUPINGS IN SOUTHERN AFRICA

	NAME	TYPE	YEAR ESTABLISHED	MEMBER COUNTRIES
1.	Southern Africa Customs Union (SACU)	Customs Union	1910 Renegoiated in 1969. Currently being renegotiated	Botswana, Lesotho, Namibia, Swaziland, South Africa
2.	Common Monetary Area (CMA)	Exchange Rate Union	1986, previously from 1974 the Rand Monetary Agreement	Lesotho, Namibia, Swaziland, South Africa (Botswana left in 1974)
3.	Southern African Development Community (SADC)	Development Cooperation Forum	1992, previously SADCC (Southern Africa Development Coordination Conference), established in 1980	Angola, Botswana, Lesotho, Malawi, Mozambique, Namibia South Africa, Swaziland Tazania, Zambia, Zimbabwe
4.	Common Market of East and Southern Africa (COMESA)	Free Trade Area	1995; previously since 1960s. The Preferential Trade Area (PTA)	Angola, Burundi, Comores, Djibouti, Ethopia, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Somalia, Sudan, Swaziland, Tanzania Uganda, Zaire, Zambia, Zimbabwe
5.	Cross Border Initiative (CBI)	Not formal; forum for discussion of relaxation of cross-border investment constraints	1994/5, coordinated by World Bank, IMF, European Union and African Dev. Banks	Malawi, Namibia Zambia, Zimbabwe

Source: MAASDORP, G. and Whiteside, A, (1993)
World Bank (1995)

development of capital market structures in developing countries. These include: **a) an appropriate enabling and supportive macro environment; b) the presence of an efficient domestic banking system; c) a large and growing capacity for savings by residents; d) the existence of an appropriate legal and regulatory framework.**

In respect of the **environment**, it is evident that both the authorities in Southern Africa and the Caribbean have been taking this quite seriously in recent years. Many of the countries in both groups are in the midst of active **programmes of adjustment**, some domestically inspired and others Fund/Bank led. The process of active **economic convergence** is well under very, especially among countries, on both sides, involved in programmes of development, economic or monetary integration. **Fiscal deficits** are declining as a percentage of GDP; **inflation rates** are trending downwards; and **interest rates** in real terms are approximating international levels. **Exchange controls** are disappearing as a reality in both the Caribbean and Southern Africa, remaining in only few countries in both regions. Authorities in both countries are becoming increasingly sensitive to the negative impact of **taxation** for attracting foreign investment and taxes are being systematically lowered, especially in Southern Africa. This is particularly true with respect to financial assets, where the world is rapidly equalizing differentials in interest and dividend income, abolishing taxes on capital gains and moving to double taxation treaties. Such trends have not been lost on both the Caribbean and Southern Africa.

TABLE 3: SELECTED OPERATING PERFORMANCE MEASURES OF SOUTHERN AND OTHER AFRICAN AND CARIBBEAN BANKING SYSTEMS
(averages for profitable banks for respective financial years ending 1992, 1993 & 1994)

	PROFITABILITY				STRENGTH /SOUNDNESS		EFFICIENCY					
A. SOUTHERN AFRICA	Return on Equity (%) 1992	1994	Return on Assets (%) 1992	1994	Capital Adequacy (%) 1992	1994	Net Income/Staff (US$ 000) 1992	1994	Net Income/Branch (US$ 000) 1992	1994	Net profit to Operating expenses(%) 1992	1994
Botswana	17.9	14.6	1.7	2.4	18.2	15.9	8	-	370	-	30.3	48.1
Mauritius	16.2	24.1	1.1	1.4	-	17.0	10	-	20	-	-	96.3
Namibia	25.5	31.7	1.4	1.7	9.7	10.6	9	-	240	-	46.6	48.1
South Africa	17.5	11.3	1.2	0.7	9.1	10.8	6	-	186	-	29.1	30.9
Swaziland	12.2	14.3	0.7	1.0	9.0	8.6	5	-	128	-	12.7	15.5
Zambia	52.8	144.4	5.8	7.4	29.6	35.1	4	-	168	-	102.8	78.4
Zimbabwe	20.8	42.3	1.5	3.3	-	19.9	-	-	-	-	-	161.8
Kenya [a]	51.5	42.8	3.4	5.7	12.9	56.2	6	-	136	-	38.9	56.4

B. CARIBBEAN	Return on Equity (%) 1993	1994	Return on Assets(%) 1993	1994	Gross Earnings Margin(%) 1993	1994	Net Earnings (%) Margin 1993	1994	Operating Costs / T. Assets (%) 1993	1994
Bahamas	-	-	1.63	2.22	4.61	5.04	1.33	1.70	4.03	4.03
Trinidad & Tobago	15.5	13.4	1.20	1.0	-	-	-	-	-	9.5

[a]/ For comparison purposes only
[b]/Shareholders Funds to Risk - weighted Assets

Source: (i) Own calculations from data in KPMG Africa (1993 and 1995) "Banking Survey".
(ii) Central Bank Bulletins and Other Publications 1992 and 1994

In short, authorities in both Southern Africa and the Caribbean have grown conscious that a 'sine qua non' of good governance in today's increasingly competitive world is responsible fiscal and monetary management, cardinal tenets of a sound environmental framework for fostering capital market development.

Table:3 above presents some statistics on the **operational efficiency of banks** in the Caribbean and Southern Africa for the period 1992-1994. On balance, banks in Southern Africa appear more profitable than in the Caribbean larger volumes and relatively less competition being largely responsible. What is also evident for Southern African banks is the distinct overall improvement in profitability indicators for most countries between 1992 and 1994 and improved efficiency management in general. Although similar data are not available for the wider Caribbean, a mixed trend is generally evident for Trinidad and the Bahamas presently included, improvements appearing in some indicators and deterioration on others. It is likely that there are many factors responsible for the broad similarities that are evident, but the generally more propitious operating environment in both regions and increasing competition, both from local and external banks entering the domestic system (especially in Southern Africa following the dismantling of apartheid), have in the aggregate played a significant part. There is also, no doubt, that the massive strides taken by central banks in their regulatory oversight for the banking system in both regions have laid the basis for sound capital market development.

TABLE:4 SAVINGS PROPENSITIES
(%)

	1985	1993	1994	1985	1993	1994
	Gross Domestic Savings/ GDP			Gross National Savings/ GDP		
A. Southern Africa						
Angola	28.3	70.0	32.3	20.8	3.1	-4.4
Botswana	32.9	24.9	24.8	21.8	...	...
Lesotho	-48.1	-14.2	-9.0	21.1	21.7	24.7
Malawi	12.9	0.4	-0.9	9.1	-0.2	-2.9
Mozambique	3.8	7.2	4.7	-0.2	4.0	1.2
Namibia	21.9	8.5	16.9	0.7	11.9	19.5
S.Africa	29.2	19.1	19.7	24.5	16.1	17.7
Swazi-	15.3	0.3	4.5	15.3	0.3	...
land	4.7	9.0				
Zambia	14.1	9.2	-7.5	0.6	1.5	-15.4
Zimbabwe	21.0	16.8	...	17.2	11.7	...
Southern Africa Average						
B. Caribbean						
Bahamas	35.7	9.8	11.2	44.5	14.9	15.6
Barbados	23.1	19.1	26.1	24.9	20.9	26.3
Belize	25.8	26.3	20.3	12.8	19.9	17.7
Guyana	10.6	25.6	34.6	20.5	46.9	56.1
Jamaica	15.1	19.3	30.8	19.6	17.8	31.0
T&T	22.9	24.5	23.2	28.3	33.7	31.9
Antigua & Barbuda	10.2	28.6	29.6	5.6	42.7	33.8
Dominica	5.1	7.7	14.2	-14.1	-1.4	9.1
Grenada	1.0	14.2	12.9	-30.5	1.4	4.7
St.Kitts	7.8	29.2	26.7	- 2.2	27.5	24.4
St. Lucia	12.7	11.6	13.6	3.8	10.5	17.1
St. Vincent	22.5	10.4	16.2	13.2	-2.7	10.7

Source[(1)] **World Bank**, Oct. 1995

TABLE 5: CENTRAL BANKING ROLE IN DEVELOPMENT OF CAPITAL MARKET REGULATORS AND STOCK EXCHANGES IN SELECTED SOUTHERN AND OTHER AFRICAN MARKETS

	APEX REGULATORY INSTITUTIONS				STOCK EXCHANGES		
	Year Institution Established	Name	Central Bank Direct Role in *Establishment?*	Current Direct Central Bank Involvement	Year Established	Direct Central Bank Role in Establishment?	Current Direct Central Bank
BOTSWANA	-		No	Not applicable	1989	No	Represented on Interim Council
EGYPT	1979	General Authority of Capital Markets	-	Sits on Board	1883	No	No
GHANA	1993	Securities and Exchange Commission	-	-	1990	Yes	Managing Director previously with Central Bank
KENYA	1989	Capital Markets Development Authority	Yes	Sits on Board	1954	No	No
MAURITIUS	1989	Stock Exchange Commission	Yes	Sits on Board	1989	No	No
MOROCCO	..	..	..	..	1929;1948; 1967	..	..
NAMIBIA	-	-	No	-	1992	Yes	Staff Provided
NIGERIA	1979	Securities and Exchange Commission	Yes	Staff seconded; sits on board	1961	No	Sits on Council; Original Issuers of Securities
S. AFRICA	1990	Financial Services Board	Indirectly	Sits on Board	1887	No	No
SWAZILAND	1990	-	Yes	Sits on Board; Staff Seconded	1990	Yes	Staff Provided
ZIMBABWE	-	-	-	Routine Capital Markets relationship	1946	No	No

.. not available
- none existing

Source: *Survey undertaken in 1993*

In respect of **savings mobilization** there are no clear trends for Southern Africa, though **Table:4** shows a general upward trend as between the 1980's and 1990's of average levels of savings for Angola, Lesotho, Mozambique. South Africa, however, as it pursues its post-apartheid adjustment agenda, is likely to manifest a different profile in time, resulting from the need to draw on its national savings and relying increasingly on foreign savings to fund the vast demands for 'catching up' investments, especially in the social sectors. Botswana, in turn, a key regional saver, has been hit by a softening diamond market, and, for the first time in 1994 since the early 1980s, experienced a fiscal deficit. Fortunately, it has procured a high stock of mainly public sector savings on which to draw for some time. Changes in the regime of exchange controls in many of the countries are expected to reduce national savings stocks in the short term but hopefully to enhance these in the longer term.

Serious attention has been afforded **regulatory structures** for capital markets in both regions in recent years. A key player in this regard has been the **Central Bank**, which in the case of Southern Africa, has played a significant role, as **Table:5** below shows for Mauritius, S. Africa and Swaziland, in particular, as well as for a number of other African countries. Even for the other countries, however, initiatives aimed at developing the stock exchanges or securities regulatory structures have been largely provided by the Central Bank. Once these structures, which have tended to be fairly independent, are in place, typically the

TABLE 6: CHARACTERISTICS OF REGULATORY STRUCTURES OF CAPITAL MARKETS: SELECTED SOUTHERN AND OTHER AFRICAN COUNTRIES WITH STOCK MARKETS

	NAME OF SPECIALIST APEX REGULATORY INSTITUTION	YEAR ESTABLISHED	NAME OF PREDECESSOR ENTITY	CURRENT SELF REGULATORY ORGANISATION ?	GOVERNMENT SUPERVISION OVERSIGHT	
					PREVIOUSLY	CURRENTLY
BOTSWANA	-	-	-	No	Min of Finance	Min of Finance
EGYPT	General Authority of Capital Markets	1979	Min. of Economy	Yes	Min of Economy	Min of Economy
GHANA	Securities & Exchange Commission	1993	-	..	Min. of Finance/ Central Bank	Min of Finance/ Central Bank
KENYA	Capital Markets Development Authority	1989	Capital Issues Committee	No	Min of Finance	Min of Finance
MAURITIUS	Stock Exchange Commission	1989	None	No	-	Min of Finance
NAMIBIA	-	-	-	No	-	Ministry of Finance (Dept of Finance Int. Supervision)
NIGERIA	Securities and Exchange Commission	1979	Capital Issue Committee	No	Central Bank	Min. of Finance/Central Bank
S. AFRICA	Financial Services Board	1990	Registrar of Financial Institutions	Yes	Min. of Finance	Min. of Finance
SWAZILAND	-	-	-	Yes	-	Central Bank
TUNISIA	-	-	-	Yes	Min. of Finance	Min. of Finance
ZIMBABWE	-	-	-	No	Min. of Fin./Res.Bank	Min. of Fin./Res. Bank

Source : Central Banks of Most Countries; other General Sources

central banks maintain some contact in the form of a Board seat or joint working arrangements with these institutions **(Table:6 below)**.

In the Caribbean, central banks have also played a catalytic role in the evolution of the regulatory structures for capital markets, especially in the 1970s and 1980s. **Central Banking Acts for most countries now confer oversight responsibility for non-banks and some role in new securities boards or agencies set up by these central banks. CLose relationships with the Councils of the Stock Exchanges are also not unusual.**

In relative terms, the Southern Africa area appears to have made more progress in capital market development than the Caribbean, with South Africa, Zimbabwe and Mauritius being particularly well developed in these areas. In both regions the models of regulatory structures for capital markets appear to be moving in the direction of the North American, in terms of a separation between oversight responsibility for the financial system, as between the central bank for the monetary systems and a securities exchange type system for the capital markets (banking failures).

Finally, an overview of the structure of capital market of both the regions presents an interesting picture. Tables:7(a) AND (b) present an overview of the key capital market institutions for those African and Caribbean countries with active Stock Exchanges - Botswana, Mauritius, Namibia, S.Africa, Swaziland and Zimbabwe in the former; and Barbados, Jamaica and Trinidad in the latter. In terms of the securities segments of these capital markets, Southern

TABLE 7 (a): EVOLUTION OF CAPITAL MARKETS
(SECURITIES)
SELECTED COUNTRIES WITH STOCK MARKETS
SOUTHERN AFRICA AND CARIBBEAN

	Year established	(i) Market Capitalisation (US$ mill)			(ii) No. of Domestic Listings			(iii) Market Turn Over Ratio a/	(iv) (P/E Ratio	(v) Taxation(%) Interest(*)	Dividend	Capital Gains	Investment Free Access by foreigners to listings	(vi) Regulation Repatriation Restrictions?	
		1985	1990	1994	1985	1990	1994							Capital	Income
A.SOUTHERN AFRICA															
Botswana	1989	-	261('91)	377	-	9('91)	11	8.2%	9.4	15	15	0	Yes	No	No
Mauritius	1989	-	268	1514	-	13	35	7.0%	18.4	0	0	0	Not fully	No	No
Namibia	1992	-	326('92)	9574	-	4('92)	14	0.3%	15.4	0	10	0	N.I	N.I	N.I
S. Africa	1987	55439	137540	225718 c/	462	732	640	8.5%	21.3	0	15	0	Yes	No	No
Swaziland	1990	-	17	338	-	1	4	0.6%	10.6	10	15	0	N.I	N.I	N.I
Zimbabwe	1946	360	2395	1828	55	57	64	11.5% b/	10.1	15	15	10	Not fully	No	No
AVERAGE (with	S. Africa)	27900	35055('90)	39892	259	201('90)	128	6.0%	14.2						
(ex	S. Africa)	360	670	2726	55	24	26	5.5%	12.8						
B.CARIBBEAN															
Barbados	1990?	-	261('91)	377	-	(1991)	11	1.4%	10.1('93)	15	15	0	No	No	No
Jamaica	1969	266	911	1735	38	44	50	8.3%	8.4	15	15	0	Not fully	No	No
Trinidad & Tobago	1981	463	696	663	36	30	27	~~9.0%~~	~~13.7('90)~~	~~25~~	~~25~~	~~20~~	~~Not fully~~		
AVERAGE		365	803('90)	931	37	37('90)	29	6.2%	8.4('94)						
TOTAL EMERGING	MARKETS	171263	611660	192897	28916	12541	17115	Best(323%)	22.9						
TOTAL WORLD d/		4667766	9424144	15185607	26669	28944	36176	-	23.2						

a) Average total market capitalization divided by total value traded.
b) Most active of selected group - 56th rank in world of 80 stock markets in 1994.
c) 11th largest in World in 1994
d) Morgan Stanley World Capital Index

N.I. - No Information

Source: I.F.C. Markets Factbook, 1995.

TABLE 7 (b) EVOLUTION OF CAPITAL MARKETS
(NON-SECURITIES)

SELECTED COUNTRIES WITH STOCKMARKETS
SOUTHERN AFRICAN AND CARIBBEAN
(before and after establishment of Stock Markets)

A. SOUTHERN AFRICA	Total Assets: (US$ million)			Av. P. A. Growth Rate	
Botswana	1980		1991		1980-91
Insurance Cos.	4		63		31.5
Pension Funds	45		145		11.1
Housing Finances	5		11		7.1
S. Africa	1970	1980	1991	1970-80	1980-91
Insurance Cos.	4096	20411	58696	17.4	10.0
Pension Funds	2581	25756	57151	25.9	4.9
Housing Finance Cos.	3332	13872	24616 ('92)	25.9	5.1 ('80-'92)
Swaziland	1980		1992		1980-92
Insurance Cos.	0.7		418		74.9
Pension Funds	4.0		52		25.2
Housing Finance Cos.	22.0		140		17.6
Zimbabwe	1975	1983	1987	1975-83	1983-87
Insurance Cos.	584	1017	1534	7.2	10.8
Pension Funds	526('77)	750('80)	3077	12.4	21.9
Houseing Finance Cos.	946	...	562 ('92)	16.9 ('75-'87)	

Total Assets: Mill. Local Currency

B. CARIBBEAN							
BARBADOS		1985	1990	Mid 1995			1990-95
Trust Companies		168	383	435			2.7
Development Banks		399	109	90			-4.0
National Insurance		363	513	664			5.3
(Commercial Banks)		1410	2180	2803			5.2
TRINIDAD & TOBAGO		1975	1985	1995		1975-85	1985-95
Managed Pension Funds		-	-	5751('94)			
Trust & Mortgage Cos.		68	1856	2945		39.2	4.7
Development Banks		160	271	282		5.4	0.4
Finance Companies & Merchant Banks		80	854	1279			
Thrift Institution		42	73	66		26.7	4.1
Life Insurance Companies		362	2034	2001('93)		5.7	43.9
(Commercial Banks)		1556	10165	16151		20.6	5.2
JAMAICA	1975	1980	1990	1994	1975-80	1980-90	1990-94
Trust Companies	98	-	109	...	-	-	-
Merchant Banks	144	-	4527	14837	-	-	34.6
Building Societies	-	311	2972	...	-	25.3	-
Credit Unions	-	180	812	2608	-	16.3	33.9
(Commercial Banks)	1011	2100	17328	96129	(15.7)	23.5	53.5

Source: Various Bank Publications; Company Annual Reports: Own Calculations.

African markets have tended to grow in relative terms much faster than those in the Caribbean, even leaving out the 'distortive' effects of South Africa's extraordinary market, the eleventh largest in the world. Over the past ten years market capitalization per capita in both regions have trebled, though apparently at a faster per capita rate in Southern Africa. Listings have grown faster in the African stock markets than in the Caribbean ones. By contrast, on balance, there appeared to be more activity in Caribbean markets in 1994. Lower P.E. ratios also suggest greater growth prospects in these markets than in Africa's. The generally more positive progress in African markets may be attributed to many reasons, but mainly one hinged on greater maturity, lower and less repressive levels of taxation and an increasingly less restrictive operating environment.

Growth in the non-securities segments of African markets has equally tended to be stronger than in the Caribbean, whose non-banks appear more mature. What is also of interest is that in both regional economies the arrival of stock markets has coincided with some slower growth in non-securities segments of the capital markets. This is probably attributable mainly to the novelty of most of the stock exchanges in either group of countries, relative to the more established insurance companies, pension funds, development banks, etc. It is equally possible, however, that poor environmental factors such as inflation, exchange controls etc. may have had a debilitating effect on savings mobilization by these bank-type institutions and less so on the nascent stock exchanges.

An analysis of savers by types in each of these institutions - domestic as well as foreign would have been revealing, but this is not possible presently.

Finally, capital markets in Southern Africa and the Caribbean appear both to be at a rudimentary stage of integration, with cross-listings being actively considered but not traded in any significant way.

In summary, the real question for the progression of capital markets in both regions is to what extent this has been influenced by environmental factors, especially movements towards increased convertibility. It is likely that this has been strongly possible due to a distinctly positive change in the macro-environment through which countries have evolved in both regions. Some of these factors are indicated in a general way in the following sections, which successively analyses convertibility of currencies and aspects of monetary management in the two regions over the past decade or so.

III CONVERTIBILITY

Currency Convertibility; Since the path-breaking essay on the topic of currency convertibility by **Gotfried Haberler (1954)**, there have been various definitions and interpretations of the term currency convertibility and of the broader term convertibility itself. Prior to the 1930s, currency convertibility represented the right to convert a currency freely into gold at a fixed rate of exchange. The broad consensus now, however, is that currency convertibility is about the capacity for readily exchanging one's

domestic currency at market rates for an external, usually 'harder', reserve currency within or outside one's domicile. Full convertibility, therefore, relates to the absence of restrictions on foreign exchange transactions. In many respects currency convertibility is typically accompanied by another form of convertibility, namely current account or **trade convertibility** or even partial or full **capital convertibility** i.e. the total absence of, or only limited restrictions on a nation's current capital account as it were. It is accepted, however, that the presence of currency convertibility does not automatically imply current account or capital account convertibility, though it is desirable to have these first. The existence of no or limited trade and investment restrictions typically guarantees free convertibility of a given currency.

Current account convertibility: This represents the particular absence of restrictions on current transactions of goods and services. It is typically the first stage towards wider convertibility and in terms of membership of the **International Monetary Fund (IMF),** represents a move, once formally acceded to, **Article VIII** status in the Fund by member nations. However, accession to Article VIII status does not necessarily imply full current account convertibility, but rather an intent to move in this direction, over a usually defined time frame. Thus, it is possible that some countries which have not formally accepted Article VIII status could, as is still currently the case in Botswana and until recently Mauritius, have a more liberal regime

of exchange controls on the current account than even countries already in Article VIII status e.g. South Africa. South Africa still has a number of restrictions on payments for trade of goods and services, even though it has attained Article VIII status since September 15, 1973. According to the **IMF**, as at September 1995, some 105 countries had accepted Article VIII status, but including only 4 of the 10 Southern Africa countries examined in this paper. As would be noticed from **Table:8** overleaf, however, of these four countries already at Article VIII (Mauritius, South Africa, Swaziland, and Zimbabwe, with Botswana formally already declaring its intention to move shortly to this status), all but Swaziland still have some restrictions on their current account. All the other of these Southern African countries still require some form of surrender/repatriation of export proceeds by domestic entrepreneurs.

In the case of the Caribbean countries there is, however a dramatic difference. Every single one has already acceded to **IMF** Article VIII status and at the end of 1994 only minor restrictions on current account remained in Barbados and Jamaica. Several of these countries in fact acceded shortly after becoming **IMF** members.

In principle, current account convertibility is desirable to the extent that it enhances a country's supply side capacity, creates a more competitive environment and promotes product and investment decisions relative to a nation's comparative and competitive advantage. Yet, there are some costs and risks, including short run adverse domestic employment possibilities,

TABLE 8: STATUS OF PAYMENTS CONVERTIBILITY - SELECTED SOUTHERN AFRICA AND CARIBBEAN COUNTRIES (AS AT EARLY 1995)

	Article XIV*	Article VIII Status** (Date accepted)	Some Restrictions on Current account	Some Capital Controls in place
1. **Southern Africa**				
Botswana	x		x	x
Lesotho	x		x	x
Malawi	x		x	x
Mauritius		x(9/93)	x	x
Mozambique	x			
Namibia	x		x	x
South Africa		x(9/73)	x	x
Swaziland		x(11/89)		x
Tanzania			x	x
Zambia	x		x	x
Zimbabwe		x(2/95)	x	x
2. Caribbean				
Bahamas		x(5/73)		x
Barbados		x(11/93)	x	x
Belize		x(6/83)		x
Guyana		x(2/66)		x
Jamaica		x(2/63)	x	x
Trinidad & Tobago		x(12/93)		
<u>OECS</u>				
Anguilla		-		
Antigua/Barbuda		x(11/83)	x	x
Dominica		x(12/79)		x
Grenada		x(1/94)		x
Montserrat		-		
St.Kitts/Nevis		x(3/84)		x
St.Lucia		x(5/80)		x
St.Vincent/Grenadines		x(8/81)		x

- Not Fund members   x= yes
* Status upon joining Fund
** Formal commitment to removal of restrictions on current account

Source: Exchange Arrangements and Exchange Restrictions - Annual Report 1995: IMF

current account imbalances and possible considerable increases in consumption. On balance, though, this form of convertibility is widely accepted as a necessary prerequisite for wider liberalization and reform effort in emerging economies (**Greene and Isard, 1991**).

Capital account convertibility: This represents no or limited restrictions on the flow of capital or investment funds and, is typically a more difficult status to attain, even for more advanced countries. Indeed, it is well known that many Western European countries did not attain final capital account convertibility until the late 1980s (e.g. **France and Italy) (Mathieson and Rojas - Suarez 1993)**. As **Table**:8 also indicates, no Southern Africa country has presently removed all restrictions on investment flows. In the case of the Caribbean, virtually a similar situation obtains. Even in Jamaica, Trinidad and Guyana where the exchange rates are 'freely' floating, there appears some limitations still on capital flows. In terms of the degree of liberalization, it would appear that Botswana is the most advanced for the Southern African countries, with remittances up to the equivalent of US$18 million being automatically permitted on capital transactions. Other regional countries are rapidly also dismantling these capital controls to underpin their wider move towards fuller currency convertibility.

It is widely accepted that capital account convertibility could, on balance, induce net foreign resource inflows and ultimately promote macroeconomic progress, though the risk of short

run capital flight and greater exchange rate variability, especially in regimes of flexible exchange rates, are often cited as real possible constraints (**Table:9**). In practice, however, capital flight takes place, even with the presence of stringent exchange controls (**Clarke, 1993**).

Internal convertibility: Currency convertibility itself, however, does not have to be only external, in the sense that domestic funds would be converted into foreign currency for export abroad or vice versa. There could also be 'internal convertibility', involving the availability of **foreign currency denominated accounts (FCA's)**, domiciled in a given economy, side by side its own currency. As is already the case in several Southern African countries (Botswana, Malawi, Mozambique, Zambia and Zimbabwe) as well as Caribbean countries (Guyana, Jamaica, Trinidad & Tobago and to a lesser extent, Barbados), it is then possible for both residents and non-residents to maintain both local currency and foreign currency denominated accounts, in their domestic banks. The growing tendency in this area by a number of developing countries arises essentially out of a desire on their part to more progressively integrate their local with global economies, relax exchange restrictions gradually, while offering alternative investment opportunities for residents in particular, without the "permanent loss" of the use of these funds from the domestic economy.

However, what is equally evident before and after the 1994/95 Mexico external sector crisis is that more and more emerging

TABLE 9: CURRENT EXCHANGE RATE REGIMES SOUTHERN AND CARIBBEAN COUNTRIES (AS AT EARLY 1995)

A. FIXED PEGS		US$	£	Basket of other currences
1. Southern Office	(Currency)			
Botswana	(Pula)			
Lesotho	(Maloti)			x (Rand)
Namibia	(N.Dollar)			x (Rand)
Swaziland	(Emalengeni)			x (Rand)
2. Caribbean				
Anguilla	(EC$)	x		
Antigua/Barbuda	(EC$)	x		
Bahamas	(B$)	x		
Barbados	(B$)	x		
Belize	(B$)	x		
Dominica	(EC$)	x		
Grenada	(EC$)	x		
Montserrat	(EC$)	x		
St.Kitts/Nevis	(EC$)	x		
St. Lucia	(EC$)	x		
St.Vincent/Grenada	(EC$)	x		

B. LIMITED FLEXIBILITY

C. MORE FLEXIBILITY

1. S. Africa	Set Indicators	More Managed Floats	Independently Floating	Multiple Rates	Rates Determined By
Angola (New Kwanza)		x		Yes	Central Banm
Malawi (M. Kwacha)		x		No	Bureaux & Banks Auctions
Mauritius (M. Rupee)		x	x	No	Inter-bank Market Trades
Mozambique (Metical)				No	" "
South Africa (Rand)			x	No	Exchange Market with some Central Bank Intervention
Tanzania (T. Shilling)			x	Yes	Inter-bank Market
Zambia (Z.Kwacha)			x	Yes	Commercial bank Auctions
Zimbabwe (Z. Dollar)			x	No	Inter-bank markets
2. Caribbean					
Guyana (G$)				Yes (?)	Market forces in the Cambio market
Jamaica (J$)				No	Inter-bank market trades
Trinidad & Tobago (TT$)				No	Inter-bank Market trades

Source: Exchange arrangements and Exchange restrictions - Annual Report 1995: IMF

nations in particular are finding it necessary to insulate themselves from massive foreign capital shocks by putting into place appropriate controls on some capital flows. These include transaction taxes (**Chile and Colombia**); or quantitative limits (**Indonesia, Malaysia, Phillipines, Mexico**). As will be seen in **Section IV**, a number of issues of a policy and operational nature could emerge from such scenarios.

The progressive idea, therefore, appears to be for countries to move towards currency convertibility, which as a general rule would itself need to be underpinned, if they are to be sustainable and effective, by adequate volumes of external reserves, especially in a fixed exchange rate regime. Further, it is emerging common cause that attempts at serious current or capital account, as well as, full currency convertibility before the existence of an appropriate exchange rate, sound macroeconomic policies and a market-based environment are in place, are likely to be less than effective in scope and practice (Mathieson and Rojas-Suarez 1993).

IV. DOMESTIC LIQUIDITY MANAGEMENT

As the process of convertibility advances in the developing economies of Southern Africa and the Caribbean, several problems are likely to face authorities in their stabilization and adjustment efforts. The recent examples of Mexico and to a lesser extent Argentina and Chile, despite their respective particular circumstances and responses, do not do much to calm the nerves of the several smaller economies that constitute the two survey regions in the main (**IMF 1995(c)**). Three distinct problems of

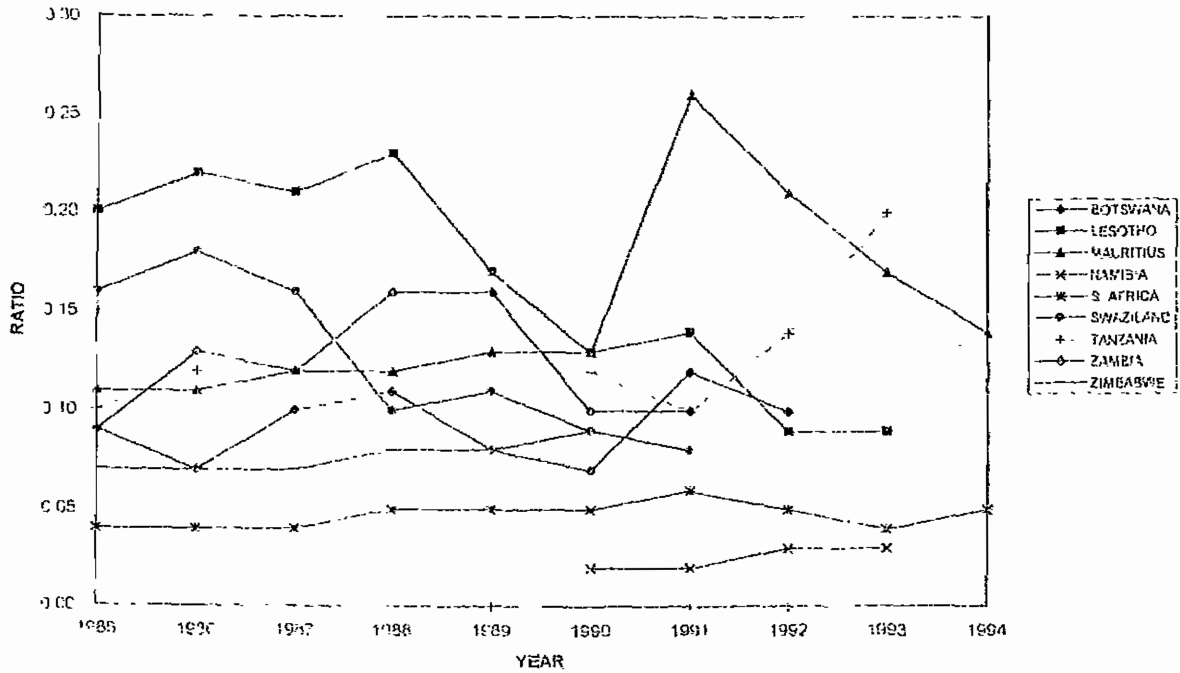
monetary management in the face of freer convertibility in economics are likely to arise: (a) more difficulty in monetary management; (b) the need for better external reserve management; and (c) likely resulting issues from the deepening of monetary cooperation/integration.

Liquidity Management. The key question appears to be the management of likely excess liquidity emerging from unexpected inflows and of tight liquidity situations emerging from massive unexpected outflows, either situation being induced by 'speculative attacks' on vulnerable economies or otherwise. The answer is, of course, efforts by the authorities to insulate or minimize the domestic money supply from the monetary effects of such flows, especially at a time when the traditional protection from exchange controls is fast disappearing.

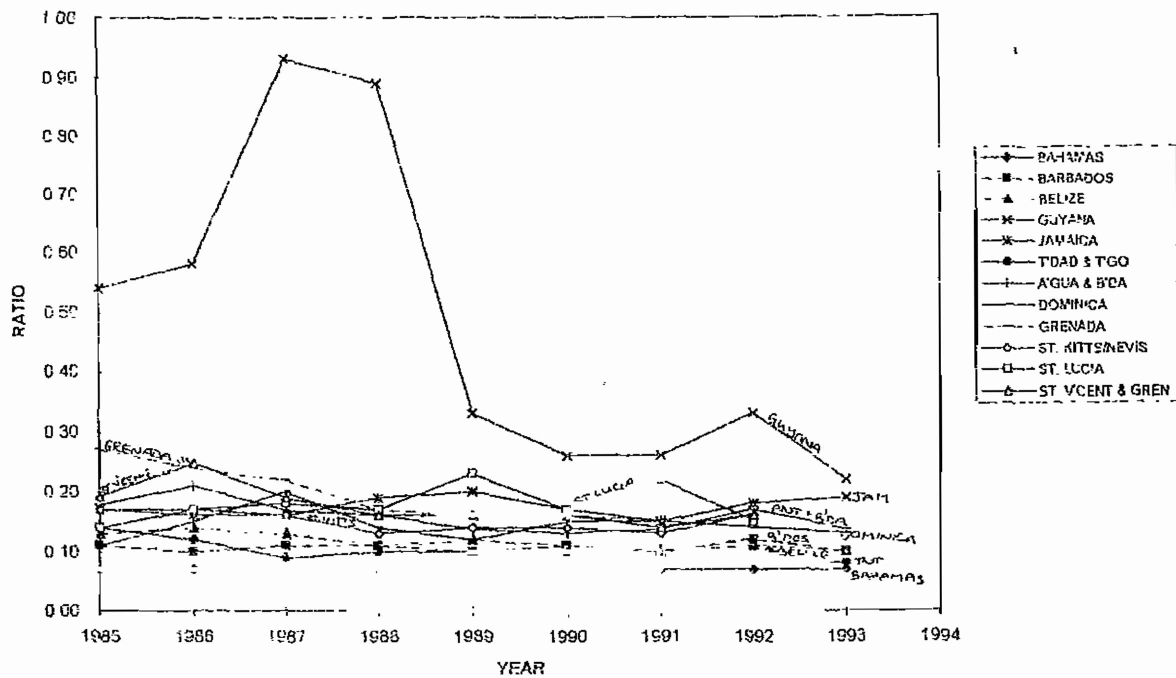
The graphs in **Chart I** overleaf suggest differences in liquidity characteristics between the Southern African and Caribbean regions, as approximated by the broad reserve money to GDP ratios and of the ratio of reserve money to broad money (**Table:10**). Caribbean countries tend to have larger RM/GDP ratios than Southern Africa, probably suggesting more active efforts to sterilise their banking systems in the face of a more liberal regime of exchange controls than Southern Africa. However, on the other hand GDP is on average much larger in Southern Africa than in the Caribbean, which could partially account for lower ratios in the former. On the contrary, the RM/M_3 measures indicate higher ratios for Southern Africa on average, suggesting greater

Chart I

RATIO OF RESERVE MONEY TO GDP FOR SELECTED SOUTHERN AFRICAN COUNTRIES



RATIO OF RESERVE MONEY TO GDP FOR SELECTED CARIBBEAN COUNTRIES



Source: International Financial Statistics :IMF Yearbook: 1995

(excess) liquidity problems for this region than for the Caribbean, This is certainly true of Botswana, Malawi and traditionally Zambia and Zimbabwe - countries well known for their difficulties with management of domestic liquidity.

Two responses to liquidity management from Southern Africa in recent years are instructive in this regard; one from Botswana and the other from Zimbabwe, though several other regional countries and most in the Caribbean have similarly grappled with these problems, often in not different ways.

Faced, since the early 1980s, by massive build up of excess liquidity arising from the mobilization of diamond receipts within the framework of solid exchange controls and weak domestic absorptive capacity, Botswana first responded by acting as a "depositor of last resort" to the banking system accepting wholesale deposits from the public, as banks were beginning to turn these away. A nominal interest rate was paid on these deposits. With time, it became evident that this system had its limitations and a desire to further liberalize the financial system gave rise among other things, to creation of a Bank of Botswana Certificate as part of an open-market type operation 'Dutch' auctions were held on average once monthly and bids tendered by banks and non-banks as well as the large diamond company. A key development, however, was that this system, while not only creating a new short term financial investment, was now the basis for determination of interest rates, which over time were targeted to become positive in real terms, relative to a local inflation rate driven in large

TABLE 10: RATIO OF RESERVE MONEY TO MONEY PLUS QUASI-MONEY (BROAD MONEY) (1980-1994)
(%)

	1980	1985	1990	1994
A. Southern Africa				
Botswana	30.4	32.6	29.3	44.7
Lesotho	14.2	33.9	37.3	18.3
Malawi	22.3	40.7	42.2	42.7
Mauritius	30.5	21.6	18.1	19.9
Namibia	-	-	5.2	9.0
S.Africa	16.5	12.2	11.7	-
Tanzania	36.4	44.7	24.8	22.3
Zambia	-	-	30.4	-
Zimbabwe	19.1	22.6	25.0	30.7
Average	24.2	29.8	24.9	26.7
B. Caribbean				
Antigua/Barbuda	28.0	26.9	19.4	17.8
Bahamas	16.8	16.7	14.0	12.7
Belize	24.4	30.6	24.2	22.4
Grenada	32.4	42.6	22.3	20.2
Guyana	38.2	55.8	42.5	36.6
Jamaica	27.8	33.7	43.1	37.4
St.Kitts/Nevis	5.9	17.5	17.8	22.3
St.Lucia	21.1	21.8	20.9	19.0
St.Vincent & Grens.	24.9	27.8	22.9	24.7
Trinidad	29.5	27.8	20.8	24.4
Average	24.9	27.4	24.8	23.8

Source: IMF: International Financial Statistics (Yearbook)

measure by imported inflation from South Africa. While this system was largely successful in periodically mopping up excess liquidity, it is clear that the movement in massive balances on government accounts with the Central Bank did not coincide with the movements in net external reserves because of financial programming, tax and other timing differences, partly reducing the effectiveness of the sterilization efforts (Similar trends were apparently evident in Jamaica in the late 1980s (Marston, 1994). Further, as liberalization and convertibility proceeded apace in Botswana, while there were increasing opportunities for unbottling local savings, more active management of interest rates through the market based system became necessary to stay in line with South African and other international market rates. As it turned out this kept rates relatively high in Botswana. This in turn raised growing concerns about the cost of sterilizing the monetary effects of the inflows, a problem also being increasingly experienced in the Caribbean through open market type operations. This necessarily became an issue with a weakening fiscal position and growing bankruptcies of local companies, which bankruptcies were of course blamed on the tight monetary policy stance. As liberalization proceeded in the exchange regime, this tight monetary environment became more pronounced with the benefits of convertibility ironically seeming to cause increasingly more pressure, because of the authorities' demand restraining interest rate stance.

One central point, therefore, is that continued convertibility

is not an end to itself, and must be accompanied by, other complementary macro-economic instruments to be fully effective. In Botswana's case, as is so often the case in Jamaica, Trinidad, Barbados and in the early 1980s in Guyana, the fiscal side was not accommodative enough of the monetary policy efforts.

Foreign Currency Accounts: One of the tools introduced to deal with the problem of domestic liquidity in Zimbabwe was that of 'foreign currency accounts' (FCAs). Unlike the case of Botswana though, when this was introduced in early 1995, the Zimbabweans from inception in-- treated such foreign currency accounts as part of their money supply, thus permitting active internal convertibility. They eventually placed reserve requirements on FCAS and attempted to manage them in this way. Botswana dealt with this problem, as did Zimbabwe initially also, by restricting the quantum and eligibility criteria for access to these accounts. Zimbabwe, however, clearly viewed this new system of FCA's more as a mechanism for attracting new inflows, unlike Botswana which viewed them as a basis eventually for assisting the sterilization process. Because the bases were different, the build-up in foreign currency accounts was much more rapid in Zimbabwe than Botswana and systemic problems in Zimbabwe were more severe, including the well-known 'round-tripping' problem. This arose initially from an effective dual exchange rate for holders of foreign currency and official transactions by the state, which in the early stages required some or all foreign receipts from 'bona fide' transactions to be sold to the Central Bank.

The central point is that the process of liberalization dictated the move to the creation of foreign currency accounts, a tangible facet of internal of currency convertibility, which because of the underlying implementation objectives, economic context and operational circumstances had different degrees of effectiveness in these two countries,(Botswana and Zimbabwe). This underscores the need for approaches to problems of this nature to be tailor-made and adopted to local circumstances in their application. Needless to say, in the case of Zimbabwe a significant degree of inflows resulting from the FCA's was via equity into its relatively cheap equity markets, giving rise to a marked build up in market capitalization and activity in the stock market in 1993 and 1994. So far in Botswana, by contrast, there is no evidence that the presence of FCAs has in fact affected capital markets in any unique way. The jury is still out on the responses to this feature as a tool of monetary management in the Caribbean.

Reserve Management: As earlier noted, freer and more convertible currencies are expected over time, in theory, to improve the external balance situation and especially in regimes of fixed exchange rates to require adequate stocks of external reserves, given the inability of exchange rate policy to assist in any required adjustment effort. This is not to infer, however, that countries with flexible exchange regimes should not hold reserves. Indeed, in some respects there is an even greater requirement to defend the external value of floating currencies and the need to intervene in markets, as the authorities in South

Africa and to a lesser extent Zimbabwe have already seen to their cost. One certainty, however, is that if the expressed benefits from currency liberalization and convertibility are to accrue to countries in Southern Africa and the Caribbean now undertaking such adjustments, building up their capacity to manage their growing stocks of reserves will become increasingly necessary. Indeed, as **John and Forde** (1995) adequately point out in their work on reserve management in Trinidad & Tobago, where foreign reserves ranged as high as US$3.3 million in 1981, any active management of such reserves becomes an exercise of some complexity. The experience of Botswana over the past ten years has been no less daunting. This is particularly necessary if such funds are invested within a region itself, in which there is significant internal trade activity, as is the case with most Southern African countries and South Africa. Special risks and problems very quickly emerge.

The real issue here for capital market development is that, with capital flows external to the Southern African and Caribbean regions drying up, the necessity for intra-regional savings to be appropriately transformed, maturity-wise and otherwise to assure the maximum social return to a region, becomes increasingly significant, especially as the region of a group integrates. How then could the flows from one strong member be appropriately invested within the region, facilitating system-wide development? What are the benefits of pooling reserves, if these are investible only outside the region of which countries form a grouping?

The fundamental problem facing the investment of these

reserves within the region are the major risks with which investments might be confronted, especially currency risks. For Botswana say,which has already tranched its reserves into longer-term and shorter-term liquidity components, with differing performance standards, guidelines, and benchmarks, there might be other types of risks such as duration/interest rates risks about which they would need to be preoccupied. However, for the near and medium term, it is likely that most reserve portfolios for countries in the region would have shorter durations, staying as liquid as possible, to meet transaction needs and flows. For Botswana, however, and for other strongly emerging economies in the future, the challenge is and will be, **how to preserve the capital value and effective purchasing power of the nation's precious reserve assets, having regard to existing or future trading patterns and their payment liabilities.**

More specifically, in Southern Africa, the preponderance of imports and, therefore payment liabilities, for most regional economies emanates from and are due to South Africa. Conventional currency risk management would, therefore, dictate correspondingly large weights of reserve asset holdings in rand, to insulate adverse changes in the future value of such assets i.e. large components of rand. But the realities of an emerging South Africa are already such that at best, the long-run prognosis for economic and political success for South Africa is mixed. An investment portfolio with heavy rand rates is therefore always a source of major concern, in spite of the higher yield potential induced by

South African capital market instruments in particular, to foreign holders of portfolios, currency weighted by trade patterns. Alternatively, should the rand components be arbitrarily underweighted in such portfolios, the portfolios could be exposed to the risk of major losses in value, especially if the rand appreciates vis-a-vis SDR currencies. While this is already a trade specific problem now mainly for Botswana and other regional countries it may already also be a problem for other countries in terms of their larger foreign debt service liabilities, in which repayment streams may be required in stronger foreign currencies over long durations.

The appropriate balance of portfolios is, therefore, an issue that cannot be treated lightly, as is the extent to which attempts to require asset cover for known liabilities within the very region itself are practical and workable, given the thinness and relatively liquid states of regional bond and equity markets. The fact that most of the regional economies in both Southern Africa and the Caribbean do not have fully convertible currencies, in addition, does not simplify, but rather compound the problem. Nor does the fact that exchange rate adjustment policies throughout the Southern Africa region are largely influenced by the rand, help matters in any way.

Monetary and Financial Integration: One of the issues of real relevance to both the Southern Africa and Caribbean regions has been in the past and will continue to be that of monetary integration, against the background of wider integration efforts as

discussed earlier in the paper. The extent to which the current trend towards wider convertibility influences the efforts by regional and national authorities in this direction, will continue to dominate the agendas of the respective regions for some while.

As already noted, the Common Monetary Area in Southern Africa, consisting of South Africa, Lesotho, Swaziland and Namibia, is in effect not a full monetary union, as it has no common central monetary authority, nor a common currency, each country having its own central bank. One issue that continues to be raised is the extent to which, given the new and more greatly relevant role of South Africa in the region: (a) membership of the CMA should now be broadened to other countries in the region; and (b) to what extent should the rand ultimately be the common currency of the region.

On the first point, the recent accession by South Africa to the Southern Africa Development Community and the creation of COMESA, of which S. Africa is not a member (but some of the SADC countries (Angola, Lesotho, Malawi, Mozambique, Namibia, Swaziland, Tanzania, Zambia and Zimbabwe) and all of the previous Preferential Trade Area (PTA) countries, (**Table:2**), has certainly forced this question. One factor influencing the discussion, however, has been the fact that the Southern Africa Customs Union, of which Botswana is also a member together with the four members of the CMA, has not worked properly and is the source of continuing concern by all the smaller members and by South Africa itself, though for differing reasons. The **BNLS** (Botswana, Namibia, Lesotho, Swaziland) countries take the view that the distributions

they receive from the Customs Union are not sufficient to compensate them for the opportunity and direct losses of investment location, trade diversion and loss of fiscal autonomy to which they are subjected as a result of the Union. Within SACU, therefore, there is hardly room for further consideration of deeper monetary cooperation while the trade arrangement continues to be a fundamental issue.

Relatedly, there is a feeling that probably goes beyond the confines of SACU, that should there be a movement **to deepen monetary integration** in the region, the rand's role as the central currency or even the anchor should not be automatic. Many are of the view that the jury is still out on South Africa and that an already relatively weak economic situation could further worsen, providing scenarios of divergence rather than convergence, in economic terms among possible member nations. In this connection, there is a strong view in several countries, that the **Botswana pula** should in fact play such a role, backed by about US$5 billion of foreign reserves presently.

In essence then, the degree of monetary integration that obtains in the OECS countries in the Caribbean is certainly not there in the CMA and while deeper monetary cooperation is on the agenda of most Southern African countries these days, at best, the adjustment process that is fully underway in most of the countries is creating a more propitious environment for deeper cooperation and integration. One of the likely realities to force the pace of such integration in Southern Africa member, is the fairly strong

stock exchanges that already exist in Zimbabwe and S. Africa. While there has been virtually no progress so far in integrating these markets, there are lots of discussions on cross-listing etc. Moreover, the recent Cross-Border Initiative (CBI) involving Malawi, Namibia, Zambia and Zimbabwe and sponsored by the World Bank, International Monetary Fund, European Union and the African Development Bank is a step that could facilitate closer monetary cooperation between these two countries.

Further, several of the region's currencies, the rand, the pula and to a lesser extent the Zimbabwe Dollar and the Mauritius rupee are already fully convertible among themselves. The question is how soon will all currencies within the region be fully convertible among themselves - the general direction of the thrust in the Caribbean - and how would this process influence the pace of deepening capital market integration. The creation of foreign currency accounts in our economy is meant to be a step in the right direction for further capital market integration. In this regard, the sense is that harmonization efforts in the area of stock markets and their regulatory structures in the Caribbean are more advanced, as appears also to be the level of functional cooperation by central banks in this region. What is clear, however, is that in both cases the persistent drive towards fuller and freer convertibility of regional currencies will have a positive effect in both regions, both on speeding up the pace towards some sort of a monetary union, while serving as a catalyst to integrating capital markets at a regional level. The build up of national

capital market structures will, as earlier noted, be also fundamentally reinforcing to this process.

Finally, there is the issue that Botswana is becoming increasingly new to the idea of partially transforming itself into a **centre for financial services**, analogous to the efforts being pursued, albeit luke warmly by Trinidad & Tobago. With its extraordinarily large stock of foreign reserves, the relative convertibility of its currency, best capacity in the region to dramatically remove if not abolish personal and corporate taxes (which account for less than 10% of total government revenues), a very stable political and economic environment for many years now and the virtual abolition of exchange controls, Botswana finds itself in a unique position to move in this direction. In a certain sense at a time when diamond revenues are being threatened because of softening international market prices and beef as a secondary source of national revenues is being threatened (following the signing of GATT), it is imperative that Botswana defines for itself quickly a new engine of growth for its economy. One such is without a doubt financial services. Like Trinidad, aspiring towards this role of a centre for financial services presents its own problems for Botswana. These include the mature financial infrastructure already existing in South Africa, a strong offshore and domestic banking structure in Mauritius and very educated and skilled human resources in Zimbabwe and white South Africa, all of which factors represent real challenges to Botswana. This is no different from the challenges that Jamaica, Bahamas,

Barbados and, to a lesser extent, the OECS group respectively present for Trinidad in this regard. There is little doubt that as these financial services centres emerge, greater integration of capital markets are necessarily facilitated through complex intermediation and other activities. Even so, South Africa ia already spreading its testacles throughout the financial system of Southern Africa, through banks and insurance company expansions.

In sum, while environmental circumstances no doubt precipitate greater tendencies to convertibility in both Southern Africa and the Caribbean region in recent years, one of the clear by-products in the wider area of monetary management has been the tendency towards greater cooperation and integrative approaches, themselves presenting emerging opportunities for enhancing capital market collaboration and harmonization.

SOME LINGERING CONCLUDING CONCERNS

Mr. Chairman, having said all of the above, there appears to be a growing desirability for further progress to full currency convertibility in our economies. This, despite the increasing complexity for monetary management especially in highly open economies such as ours, that is increasingly evident in the Caribbean. Despite the potential for further deepening and integrating our capital markets, I have to admit to the presence of a few key lingering questions in my mind, which I feel compelled to share with you.

These are:

i) Is there any real guarantee that the at best, if not

mixed, successes evident in larger economies in Latin American, South East Asia and even Southern Africa, in the liberalization of their external and financial sectors are likely to replicate themselves in our micro, more open, less integrated economies? Or is it more a matter of better and more appropriate sequencing and time, before we will reap similar fruits?

ii) how prepared are our **people** - technically, competitively, professionally and commercially for the upheavals that liberalization and reforms of this kind dictate? - In other words how significant are the complexity and complexion of the social dimension in all of this? How equitable will the distribution of new assets expected to be created by capital market expansion be? Will new social ills arise? and

iii) are our **institutions,** especially the regulatory ones, prepared for the onslaught that further convertibility and other forms of financial sector reform are likely to impose on them? In particular is a proliferation of regulatory structures, analogous to those evident in our powerful neighbours to the North West and North East, a viable guarantee for ensuring the evolution of robust and sustainable capital market structures? Or should we be looking to consolidated regimes with significant independence and sound capacities for ensuring good governance at all levels of economic and political life?

Mr. Chairman, the jury is still out on most, if not all of these questions. I trust the conference will assist in the resolution of some, if not all of these concerns, as we in the Caribbean are compelled to grapple with the daunting task of monetary management in liberalizing environments.

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