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**THE DEVELOPMENTAL ROLES OF CENTRAL
BANKS IN THE WEST AFRICAN
MONETARY ZONE**

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THE DEVELOPMENTAL ROLES OF CENTRAL BANKS IN THE WEST AFRICAN MONETARY ZONE

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EXECUTIVE SUMMARY

This study seeks among other things, to outline the key developmental roles that West African Monetary Zone (WAMZ) member central banks may adopt to resolve the structural challenges that inhibit rapid economic growth and the attainment of monetary policy objectives in their respective economies.

The recent Global Financial Crisis has challenged the prevailing paradigm of monetary policy in both the developed and emerging economies. The crisis has brought to the fore the fact that dangerous financial imbalances could creep up under the condition of stable price level and output gap. The established pre-crisis consensus of focusing monetary policy on price stability has given way to the revival of Keynesianism to restore financial system stability and economic growth. The imperatives of monetary easing using unconventional measures by notable banks in the developed world were not in doubt during the crisis.

The resolution of the crisis through unconventional means in the developed world begged the question whether central banks in the emerging economies should continue focusing monetary policy solely on price stability in the face of numerous structural challenges that retard economic growth and impair the effectiveness of monetary policy transmission mechanism in their respective jurisdictions. All the West African Monetary Zone (WAMZ) economies are plagued by wide infrastructure deficit and supply-side bottlenecks that inhibit rapid and sustainable economic growth. In the midst of these challenges, do central banks have a developmental role to play?

The paper reviews the key arguments for the use of market-based monetary policy prior to the Global Financial Crisis. It then juxtaposes them with the post-crisis views that when the monetary policy transmission is weak or completely broken down, direct interventions by the central bank may be necessary for the attainment of monetary policy goals and output expansion. A point worth noting is that all the WAMZ central banks engaged in some kind of development finance at one point in time during the immediate post-independence era. However, the WAMZ central banks decided to move away from development finance as their economies suffered financial repressions in the late 1970s and 1980s on account of administrative controls and selective credit policies pursued by their central banks; the bureaucracy and red tapism associated with some credit schemes; incongruent general macroeconomic framework adopted at the time; and the economic slowdown emanating from commodity price slumps and high oil price shocks.

In recent times, especially during the post-global financial crisis era, the Central Bank of Nigeria (CBN) and the counterpart in Liberia (CBL) have launched stimulus initiatives targeting critical sectors such as agriculture, aviation and power, manufacturing, tourism and housing. These initiatives by the CBN and CBL have provided some experience sharing within the WAMZ and considering general and country-specific macroeconomic, structural and development finance challenges, the paper suggests key areas that WAMZ central banks should focus on in their respective countries.

Based on the findings from literature, the survey conducted as well as discussions held with policy makers in the Zone, the paper recommends the following as the extent to which central banks can go in implementing the suggested developmental roles:

- i) Central banks need to have detailed discussions with finance ministries to agree on which particular sectors to target and mode of funding the selected intervention programmes;*
- ii) In countries where the central bank's balance sheet is not healthy, funding for the development programmes could come by way of complete government support, partnership between the bank and the ministry, central bank guarantee to commercial banks with excess liquidity, and/or concessionary funds from development partners;*
- iii) All direct intervention programmes should have clear-cut objectives with targeted beneficiaries clearly identifiable prior to the implementation of the programme in order to avoid encroachment by politicians and "well-connected" business people;*
- iv) Monitoring and evaluation tools should be designed with clear deliverables or indicators in line with the programme objectives and agreed to by all stakeholders before the programme is rolled out;*
- v) Exit strategies should also be designed alongside the programme and in line with the programme objectives;*
- vi) All direct interventions by the central bank should be in sync with the government fiscal policy and budget; and*
- vii) Central banks should avoid direct interventions in sectors where government policies have created distortionary prices.*

Following this Executive Summary, the study is divided into five sections. Section one provides an introduction to the study, section two gives a review on understanding developmental roles of central banks, whilst section three gives an overview of the developmental roles adopted by central banks in the WAMZ. An analysis of the direct interventions conducted by the central banks and the key development finance challenges is undertaken in section four, whilst section five concludes the study and highlights the policy recommendations.

Keywords: Central Banks, Developmental Roles, West African Monetary Zone (WAMZ)

JEL Classifications : E5, O1, O5.

1.0 INTRODUCTION

Since 1980s, almost all of the WAMZ central banks have adopted market-based monetary policy with the primary objective of price stability as part of their financial sector liberalization programmes. Though the focus of WAMZ central banks on price and financial stability seems to have contained inflation and deepen the financial sector in some Member States, inclusive growth and development have not been achieved, resulting in high unemployment in the Zone. Most WAMZ economies are plagued by wide infrastructure deficit and supply-side bottlenecks that inhibit rapid and sustainable economic growth. Further, most member central banks' price and financial stability objectives are challenged by weak transmission mechanism and structurally disjointed nature of their economies.

The past decades have seen the mandate of most central banks in developing and emerging countries widened beyond macroeconomic stability. There is a growing shift from the central banking practice which focus on the primary objective of price stability using market-based instruments (that which was also promoted in developing countries by institutions such as the International Monetary Fund (IMF) and multilateral development banks) to central banking with a broader mandate. Central bank policies are now being redirected towards promoting economic development and structural transformation in addition to price stability. Financial sector development, the promotion of financial inclusion and efforts towards aligning the financial system with sustainable development are common characteristics of central banking policies in developing economies (Epstein, 2005).

One major factor which has brought this renewed focus on economic development and undermined the conventional approach to central banking which focused on price stability is the Global Financial Crisis (2007-2008). In response to the crisis, major central banks (The Fed, the Bank of England and the Bank of Japan) have designed unconventional methods (beyond their narrow framework) of extending credit or large liquidity support to depository institutions and, using emergency authority, to non-bank financial institutions to ensure financial stability. Similarly, central banks in developing countries, drawing lessons from the financial crisis and in view of the challenges associated with the implementation of market-based monetary policy, have sought to promote sustainable economic development in recent times.

In view of these challenges and the lessons from the financial crisis, some central banks in the WAMZ are pursuing developmental roles using non-conventional policy measures as a means to overcome the structural and financial challenges confronting their respective economies. However, expanding the mandate of central banks in developing countries particularly in the WAMZ, to include the role of promoting sustainable development, is inconclusive. This is due to the fact that the developmental objectives can conflict with price stability objective. These, therefore, raise several questions for investigation.

First, should central banks in the WAMZ continue to focus primarily on price stability using market-based instruments or should they widen their primary mandate towards

economic development using non-market based/non-conventional measures. Secondly, given the possible conflict between stability and development objectives, to what extent should central banks in the WAMZ make direct interventions to promote economic development and structural transformation?

In the light of the foregoing, the study seeks to: 1) review the past and the current developmental roles played by central banks (2) provide the directions for developmental roles WAMZ member central banks can adopt, to achieve the desired objectives.

2.0 UNDERSTANDING DEVELOPMENTAL ROLES OF CENTRAL BANKS

Central banks perform different functions in the economy which impact on economic growth and development. Though these functions have changed or evolved overtime, modern central banks are known for issuing currency notes and coins, acting as banker to the government, banker to commercial banks and lender of last resort. Central banks also conduct monetary policy, supervise and regulate the financial system and promote financial and payment system development. Though all central banks' functions (directly or indirectly) impact economic development; in the context of this paper, we define developmental roles of a central bank as the central bank sponsored institutional arrangements that provide support to critical sectors of the economy which conventional or traditional tools of monetary policy are unable to adequately address.

Despite the inadequacies and failures in the past, several arguments have been advanced to support direct interventions by central bank in recent times, largely driven by the failures of the pre-financial crises

2.1 What was the conventional approach to central banking prior to the Global Financial Crisis?

The conventional approach to central banking prior to the financial crisis (2007-2008) was characterized by a single primary goal of price stability using market-based or indirect instruments under an environment of central bank independence. The focus on price stability presupposes that the central bank should not be concerned with other goals such as, directly supporting critical sectors of the economy or allocating credit to sectors of special or social needs such as

conventional approach to central banking and the structural challenges militating against the effectiveness of market-based central banking or monetary policy in developing economies like the WAMZ Member Countries.

Major central banks (The Fed, the Bank of England and the Bank of Japan) in response to the financial crisis (2007-2008), designed novel methods (beyond their narrow framework) of extending credit or large liquidity support to both depository institutions and using emergency authority, to non-bank financial institutions. These proved very effective in handling the challenges associated with the crisis.

In developing economies, direct interventions by central banks have taken various forms and have been used to address liquidity constraints in the financial system, as well as structural or supply-side challenges which render conventional or market-based monetary policy ineffective in promoting growth and development.

industry, housing, agriculture or education. The focus on price stability also means that central banks should not attempt to manage the exchange rates through monetary policy and certainly not through controls on capital flows. The use of indirect tools of monetary policy means the central bank should not use credit allocation techniques such as subsidized interest rates, credit ceilings and capital controls to affect either quantity or the allocation of credit. The central bank

independence suggests that the central bank should not be subjected to pressure from the government to finance government deficit (Epstein,2005). These tenets of pre-crisis

conventional central banking approach were promoted in both developed and developing countries.

2.2 Arguments for the pre-crisis conventional approach to Central Banking?

2.2.1 *Focus on a Single Primary Goal of Price Stability*

The focus on price stability though not an end in itself, it is argued that a low target rate of inflation could produce the monetary conditions that will produce the highest long-run growth of output and the lowest long-run unemployment for the economy. In addition, the target of price stability is meant to remove or minimize the potential destabilizing impact of monetary policy and create the conducive environment for the economy to respond to shocks, although fluctuations could originate from the supply side of the economy (Handa, 2000). The switch from multiple goals to a single goal of price stability emanated from the experiences of central banks during the 1970s and early 1980s, when the pursuit of expansionary monetary policies produced higher rates of inflation without higher growth over a long period of time. The switch to single goals was also influenced by theoretical revision in the scope of monetary economics particularly, the augmented Phillips curve argument by Milton Friedman and the rational expectations hypothesis and neutrality of money by Lucas, and subsequent contributions by Barro, Sargent and Wallace and Kydland and Prescott.

The policy implication of this view is that given that economic agents form expectation rationally, the central bank needs credibility in order to succeed in the conduct of monetary policy. In the 1980s, the impact of

these theoretical revisions persuaded central banks of the Western economies to abandon the multiplicity of goals in favour of a heavy and sometimes sole focus on controlling the rate of inflation or price stability (Handa, 2000). These views also led international financial institutions such as the International Monetary Fund (IMF) to encourage central banks in developing and emerging countries to pursue a single goal of price stability in the 1990s. Indeed, the focus of price stability was based on the belief that price stability will provide the necessary monetary conditions that will produce the highest long-term growth and the lowest long-run unemployment.

2.2.2 *Market-based or indirect monetary policy*

The argument for the use of market-based monetary policy stems from the ineffectiveness direct control methods particularly in an open economic environment with current account convertibility and increasing progress towards full external account convertibility (Mishkin, 1999). Based on the experiences of central banks, it was observed that direct control led to financial repression and disintermediation. In addition, economic agents find means to circumvent direct controls. Consequently, the argument for market-based monetary policy is to enhance the use of price signals in the economy to improve market efficiency. The indirect approach is also to encourage intermediation

through the formal financial sector and also permit the central bank to have greater flexibility in policy implementation to be able to respond to shocks and quickly respond to policy errors.

2.2.3 Central Bank Independence

The argument for central bank independence was highly influenced by the new classical thinking or the Real Business Cycle (RBC) theories particularly with respect to inflationary expectations, time inconsistency, reputation and credibility. Following Kydland-Prescott (1977) argument that discretionary policies lead to inflation bias, then there is the need to establish some institutional foundation that will constrain discretionary actions. The dynamic inconsistency theories of inflation initiated by Kydland-Prescott (1977) and developed by Barro and Gordon (1983a, 1983b) and Backus and Driffil (1985) explains that excessive inflation will be the outcome of a monetary regimes where long-term commitments are precluded.

The political economy argument for central bank independence is in recognition of the fact that incumbent politicians may often succumb to temptation and use discretionary policies in order to maximize their re-election creating a problem of reputation and credibility. Consequently, it is argued that the responsibility for anti-inflationary policy should be given to a non-political independent central bank. Two main distinctions are made in respect of central bank independence – goal independence and instrument independence. Goal independence implies that the central bank sets its own objectives (political independence), while instrument independence refers to independence with respect to the various tools of monetary policy (economic independence). For central banks with goal independence, the influence of political factors on the goals they pursue will be minimal whilst those with instrument independence cannot extricate themselves from political influence.

2.3 Arguments for developmental roles of Central Banks Post – Global Financial Crisis

A number of weaknesses have been observed about the pre-financial crises conventional approach to central banking. These weaknesses have been exposed by the crisis and the challenges regarding the effective implementation of market-based monetary policy in developing economies like the WAMZ Member countries. Based on the weaknesses of the pre-crisis approach to central banking, there is growing advocacy for central banks to augment the pre-crisis central banking approach with some direct interventions particularly in developing and emerging economies. Some of these weaknesses include:

2.3.1 Price stability does not necessarily guarantee growth and development

Although price stability is necessary for economic growth and development, it has been argued that limiting monetary policy and by extension central banking solely to price stability cannot guarantee balanced economic growth and development (G. Epstein 2007). Though central banks react both to output and price fluctuations, the approach is still considered narrow. With the experiences and lessons from the crisis, major central banks have now observed that price stability is not enough to ensure

financial stability, output growth and employment; price stability is a necessary but not sufficient condition. The mandates of some central banks, like Bank of England, have been enlarged to include financial stability. Others like the Bank of Japan also adopted unconventional approach (quantitative easing) to stimulate growth.

2.3.2 Weak Transmission Mechanism in developing economies

It has been argued that the under-development of the financial system in most developing countries constitutes a major constraint to the achievement of monetary policy goals (M. Ncube n.d). The lack of well-developed financial markets means that the interest rate channel of monetary policy transmission is less effective. It is therefore argued that when monetary policy transmission is weak or completely broken down, direct interventions by the central bank may be necessary for effective monetary policy. Thus, for the central bank to achieve its goals, there may be need to implement

some direct interventions in the real sector of the economy.

2.3.3 Structural Challenges may be more responsible for macroeconomic instability than monetary factors

It is the view of various proponents (C. Goodhart among others), that whilst pursuing price stability may be the focus of central banks, inflation may not always be a monetary phenomenon. Consequently, the central bank may need to consider interventions to address some of the structural factors responsible for inflation. Central banks need to engage in development financing because certain challenges may not be addressed expeditiously by the fiscal authorities. Considering the fact that decisions of the fiscal authorities regarding what challenge to address and at what time are more often than not clouded with politics, the treasury or the fiscal authorities may not be able to tackle identified challenges expeditiously.

2.4 Some cases of Post-Crisis Direct Interventions or Unconventional Approach to Central Banking

During the past decade, a number of central banks in advanced economies have adopted various approaches to impact their respective economies when standard or conventional approaches proved unsuccessful or ineffective. These include the Bank of Japan (BOJ), The Federal Reserve System of United States and the European Central Bank (ECB). Whilst the results from these interventions were mixed, lessons from them might be very useful to guide direct interventions or developmental roles in developing economies like the WAMZ member states.

2.4.1 Direct Interventions by the Bank of Japan (BOJ)

The BOJ since 1999 has made a number of interventions in response to some crises faced by the Japanese economy. The BOJ introduced Zero Interest Rate Policy (ZIRP) in response to Credit Crunch (1997-1998), Quantitative Easing (QE) to the Inflation Target (I.T.) bubble in 2001 and Quantitative Easing (QE) and Comprehensive Monetary Easing (CME) policy in response to the Global Financial Crisis (2007-2008). The programme was doubled after the earthquake

in 2011, pushing BOJ's balance sheet to about 30.0 percent of GDP. The evidence on the effectiveness of the QE in Japan is mixed. While there are suggestions that the QE have helped reduce yields (Ugai, 2007; Berkmen 2012), its impact on economic growth was very small (0.825 percent average growth rate between 1999 – 2010). However, the low growth impact of the QE was attributable to series of external shocks and natural disasters suffered by the country during the period. The negative shocks to the economy included land and stock prices bubble burst, IT bubble burst, global financial crisis, and earthquake and accompanying tsunami in north-eastern Japan in 2011 (Ueda, 2011).

2.4.2 Direct Intervention by the Federal Reserve System (The Fed) United States of America

Before the crisis, the Fed conducted monetary policy by buying and selling (outright or repo) only Treasury and agency securities with relatively small set of large broker-dealers. The discount window loans to depository institutions existed but were rarely used by depository institutions because of the stigma associated with it (Dietrich and Vladyslav, 2014). In response to the global financial crisis, the lending to financial institutions, providing liquidity directly to key credit markets, and buying longer-term securities. The three sets of policy tools used by the Fed were termed Credit Easing (CE). These policies were designed to allow the Federal Reserve to continue to push down interest rates and ease credit conditions in a range of markets, despite the fact that the federal funds rate was close to its zero lower bound. The Fed's intervention or credit easing, was similar to the QE of the BOJ in that it involves an expansion of the central bank's balance sheet. However, the credit

easing approach focuses on the mix of loans and securities that the Fed holds and on how this composition of assets affects credit conditions for households and businesses; whilst in the QE of the BOJ, in a pure QE regime, the focus of policy is the quantity of bank reserves, which are liabilities of the central bank. The composition of loans and securities on the asset side of the central bank's balance sheet is incidental. Credit easing involves increasing the money supply by the purchase not of government bonds but of private-sector assets, such as corporate bonds and residential mortgage-backed securities.

Fed undertook a number of extraordinary actions to ensure that financial institutions had adequate access to short-term credit. The actions included

- a) Liquidity provision by the Fed reduced systemic risk by assuring market participants that, should short-term investors begin to lose confidence, financial institutions would be able to meet the resulting demands for cash without resorting to potentially destabilizing sales of assets.
- b) In addition, the Federal Reserve developed a second set of policy tools, which involved the provision of liquidity directly to borrowers and investors in key credit markets. There were facilities to purchase highly rated commercial paper at a term of three months and to provide backup liquidity for money market mutual funds. Further, the Fed and the Treasury jointly introduced a facility that lent against AAA-rated asset-backed securities collateralized by student loans, auto loans, credit card

loans, and loans guaranteed by the Small Business Administration.

- c) The Federal Reserve's third set of policy tools included purchase of longer-term securities for the Fed's portfolio. Plans were put in place to purchase up to \$100 billion in government-sponsored enterprise (GSE) debt and up to \$500 billion in GSE mortgage-backed securities.

2.4.3 Direct Interventions by the Central Bank of Kenya (CBK)

The Central Bank of Kenya (CBK) rolled out a comprehensive direct intervention programmes towards promoting financial deepening, ensuring quality of institutions and financial inclusion. The CBK was at the fore front to transform the financial system, leading to the growth and expansion of non-bank financial intermediaries, such as savings and credit organizations, insurance companies and mutual funds. The Bank has also taken proactive role of ensuring the development of the capital market by providing alternative liquid investment vehicles. Taking advantage of technological advancement, especially ICT, and financial innovation, the CBK has helped in the introduction of a variety of products with unlimited-room for more innovative financial products. To relax the binding constraints to economic growth, especially in water, energy and road sectors, the Bank has introduced infrastructure bond to finance long-term infrastructure projects.

Kenya has had some early successes in terms of extending financial services to previously unreached populations. The CBK has provided space for innovative solutions by leveraging on technology for cost effective

financial services to increase the level of financial inclusion through the use of mobile telephones. Total mobile phone transactions per day averaged US\$ 54.4 million (Ksh4.6 billion) by January 2013, with the average size of transactions per customer increasing from US\$45.5 or Ksh3,067.0 in March 2007 to US\$78.6 or Ksh6,660.4 in January 2013. The number of deposit accounts increased from 1.9 million in 2002 to over 18.6 million in February 2013, while number of micro accounts rose by over 900 percent from about 1.55 million accounts in 2002 to about 17.62 million accounts in February 2013. Micro-accounts balances are fully covered by Deposit Protection Fund. In addition, the CBK licensed Deposit Taking Microfinance Institutions (DTMIs) and promoted agent banking. The Bank further introduced credit reference bureaus and promoted commercial bank branch expansion, financial education, currency centres and consumer protection by encouraging transparent disclosure, fair treatment and prompt dispute resolution.

2.4.4 The Central Bank of Egypt (CBE)

The Central Bank of Egypt (CBE) sets in agreement and coordination with the government, the objectives of the monetary policy through the Coordinating Council that was formed by Presidential Decree No. 17 for 2005. This law introduced other several critical improvements, including stronger prudential regulations and enforcement powers, higher minimum capital requirements, and principles for loan settlements and workouts. Significant improvements also occurred in the institutional framework and financial infrastructure during the financial reform programme. The CBE began its efforts to modernize the payment system with changes in policies, regulations and oversight and

improvements in existing arrangements that reduced processing times for payments.

- The first phase of the financial sector reform (2004 – 2008) focused on financial and managerial restructuring of state-owned banks, privatization and acquisitions, upgrading the control and supervision sector, and addressing the problem of non-performing loans.
- The second phase of the reform (2009 – 2012) touched on financial and managerial restructuring of specialized state owned banks, upgrading the

efficiency of the state-owned banks in financial intermediation and risk management, applying Basel II standards to enhance the risk management practices of state-owned banks, promoting the development and growth of banking services and access to finance especially for SMEs as well as reviewing and applying the international governance rules of banks. In addition, a database was established for SMEs in all the state governorates, and was launched on the Egyptian Banking Institute's site (EBI) in February 2012.

3.0 DEVELOPMENTAL ROLES OF CENTRAL BANKS: THE WAMZ EXPERIENCE

This section chronicles the experiences of the WAMZ member central banks in development financing. It provides a brief overview of the establishment and initial mandates of the WAMZ member central banks. This section recognises that development financing or engaging in developmental roles is not a new issue in the Zone. All member central banks at one time or another have undertaken development financing of certain critical sectors of their

respective economies. Given this fact, the obvious question is “why have central banks moved away from development financing undertaken during the immediate post-independence era?” This section attempts to answer this question by first giving the reasons why central banks’ retreated from development financing during the early years of establishment, before providing a catalogue of their recent experiences.

3.1 Overview of Central Banking in the WAMZ

3.1.1 Establishment and Initial Mandates of Central Banks in the WAMZ

Most central banks in the WAMZ, having evolved from the West African Currency Board (WACB), began with orthodox central banking functions – issuing and managing the internal and external value of currency and promoting sound financial environment. Emphasis on direct involvement in development was limited or secondary. The early central banks were assigned strict or orthodox central bank functions to protect them from undue political interference despite the huge development challenges faced by countries in the zone. For instance,

the Ordinance 34 of 1957 which established the Bank of Ghana prescribed orthodox central banking function for it, with strict rules that provided it adequate insulation from unrestrained political influence in the form of excessive budget deficit financing. Similarly, the CBN Act of 1958 also defined traditional central bank functions for the CBN and spelt out mandates that included issuing of legal tender currency, maintaining external reserves to safeguard the international value of the currency, promoting monetary stability and a sound financial system and acting as banker and financial adviser to the Federal Government.

Table 1: WAMZ Central Banks and Their Establishment

Central Bank	Date of establishment	Monetary Authority Before Central Bank	Establishing Act
Bank of Ghana (BOG)	March 5,1957	West African Currency Board (WACB)	Bank of Ghana Ordinance 34 of 1957
Central Bank of Nigeria (CBN)	July 1,1959	West African Currency Board (WACB)	The CBN Act of 1958
Bank of Sierra Leone (BSL)	August 4,1964	West African Currency Board (WACB)	The BSL Act of 1963
Central Bank of The Gambia (CBG)	May 1,1971	West African Currency Board (WACB) and The Gambian Currency Board(GCB)	CBG Act, 1970
Central Bank of Guinea (BCRG)	February 29, 1960	The French West Africa's Central Bank	BCRG Statue, Decree no 010
Central Bank of Liberia (CBL)	October 18,1999	National Bank of Liberia	The CBL Act of 1999

Source: Member Central Banks

The establishing act of BSL mandated it to promote monetary stability, sound financial structure, maintain internal and external value of the Leone, and promote credit and exchange rate conditions conducive for balance growth. The Central Bank of The Gambia was charged with the responsibilities to regulate the issue, supply, availability and international exchange of money, to promote monetary stability and to promote sound financial structure and credit and exchange conditions conducive to the orderly and balanced economic development of the country.

3.1.2 Financing of Government Development Projects

Despite the foregoing efforts to safe guard central bank operations of the WAMZ member central banks, they experienced several challenges emanating from political interference (to finance government deficit), civil wars and military takeovers, and global economic shocks. Some of the WAMZ central banks, in view of the prevailing

challenges, shifted to supporting their governments' development agenda, while others were constrained in executing their mandate. In Ghana, for instance, the operations of the central bank under Ordinance 34 were considered inconsistent with economic and political philosophy of the then political authority, the Nkrumah government. The focus of the government was to aggressively transform the economy through a Seven Year Development plan (1959-64) which the central bank was expected to play a major role in terms of financing. The government philosophy was that a central bank in a developing economy should not restrict itself to traditional functions of central banking but also be made to finance development projects of government. Consequently, political agitation about the lack of harmony between the central banking act and the political philosophy of the government led to the repeal of Ordinance 34 and enactment of a new central bank law, the Bank of Ghana Act, 1963 (Act 182) (Bank of Ghana, 2007).

Similarly, the CBG also aligned its policies with The Gambian's government agenda in 1978 when a five-year National Development Plan was launched. The CBG was charged with the responsibilities of mobilizing domestic resources to support the plan and manage the public debt. The plan emphasized the importance of monetary policy in popularizing banking habit, in facilitating the granting of loans at reduced administrative costs and default risks and moderating the use of labour-intensive technology. Under the CBG Act of 1971 and the five-year development plan, the Central Bank of the Gambia was charged to use both quantitative controls and selective credit allocations to encourage the provision of long-term funds for fixed capital investment.

3.1.3 Ensuring Economic Stability – Monetary and Exchange Controls

Almost all the central banks in the WAMZ have been involved in the enhancement of economic stability, particularly in monetary and exchange controls. The Bank of Ghana introduced monetary and exchange controls to contain the macroeconomic instability as result of rising inflation and dwindling reserves. The CBN also in its early years, was faced with challenges of the civil war and the weaknesses in the structure of the economy, particularly the dependence on primary commodities for exports. The civil war (the Biafra War) also led to the diversion of a considerable proportion of the country's resources to financing the war. Owing to the civil war in the later part of this period, the monetary authorities did not consider it expedient to devalue the Nigerian pound in sympathy with the British pound but rather imposed severe restrictions on imports via strict administrative controls on foreign exchange (Nnanna, 2001). As the structure of

the Nigerian economy changed following the discovery of oil in the early 1970, the increased revenue accruing to government from oil, the balance of payments and external reserves of the country improved drastically. However, the need to finance post-war developments led to a considerable growth in public expenditure, thus intensifying inflationary pressures. Under the circumstances, the central bank adopted a new monetary policy framework. This development marked the beginning of monetary targeting in Nigeria, which involved the use of market (indirect) and non-market (direct) instruments. Consequently, the major focus of central banking was predicated on controlling the monetary aggregates, a policy stance which was largely based on the belief that inflation is essentially a monetary phenomenon.

The central bank of the Gambia, soon after its establishment, was challenged by the effects of the collapse of the Bretton Woods System and Smithsonian alignment of currencies. In March 1973, exactly two years after its establishment, the Bank had to manage the challenges associated with the instability in the international markets, particularly, the need to protect the value of the domestic currency. The effects of the global oil crisis, the widespread global inflation and the Sahelian drought also posed challenges to the Bank's operations, though these were slightly moderated by boom in the prices of primary commodities exported by The Gambia. The Bank played a critical role in managing the crisis.

3.1.4 Development Finance

As noted above, development finance has been one of the key functions of central banks in the WAMZ. The development roles

initiated, promoted and supported by WAMZ central banks over the years cover several areas. These include direct interventions in key sectors of the economy, pioneering and promoting the establishment of strategic industries. For example, the Bank of Ghana in the 1970s, set up the Development Finance Department, established a Development Fund as well as Export Development and Investment Fund (EDIF), among other initiatives. In the same vein, the CBN established a developmental finance department, export-import bank (EXIM), and Agricultural Credit Guarantee Fund. Other central banks in the zone have one developmental function or the other in addition to the core mandate of financial stability.

3.1.5 WAMZ Central Banks' Departure from Development Finance in the 1990s.

WAMZ economies suffered financial repressions in the late 1970s and 1980s due to administrative controls and selective credit policies pursued by their central banks. Some central banks notably Bank of Ghana created carefully selected subsidiaries in strategic areas of the economy, especially agriculture, export, manufacturing, housing and tourism. Although BOG had a Business Intelligence Unit that advised on the establishment of the subsidiaries, the management of these subsidiaries left much to be desired. The bank could not provide the needed monitoring and supervision of these subsidiaries.

Secondly, the bureaucracy and red tapism associated with some credit schemes did not permit the targeted beneficiaries to access the funds. Thus, some of the funds meant for some sectors like agriculture were accessed

by untargeted beneficiaries and applied in different sectors like import trade sector.

Thirdly, the general macroeconomic framework used at the time did not favour these selective interventions. The removal of the invisible hand from most markets by the introduction of subsidised/controlled prices meant that no selected sector for intervention by the central bank was able to make adequate returns to cover its operations. Thus, most of the intervention programmes became a drain on the balance sheet of central banks.

Finally, the economic slowdown emanating from low commodity price shocks and high oil price shocks at the time had reduced the buoyancy of most economies in the WAMZ. These economy-wide challenges also impacted adversely on the interventions programmes as most central banks' balance sheet became weak.

In lieu of the above challenges, some WAMZ governments (Ghana, Nigeria and The Gambia) rolled out the recovery and structural reforms programmes starting in early 1980s to bring to a halt, the deterioration in the economic performance and to lay the foundation for sustained economic growth. Central banks played critical role in the structural and financial sector reforms. The programmes laid the foundation for the development of the financial market, liberalization of interest and exchange rates and the adoption of market-based monetary policy instruments by the central banks. The reforms led to positive real output growth, decline in inflation and improvement in external competitiveness of the economy.

3.2 Current Developmental Roles of Central Banks in the WAMZ

3.2.1 *The Central Bank of the Gambia*

The developmental functions of the Central Bank of the Gambia are premised on the Bank's primary responsibility for ensuring price, exchange rate and financial stability. The CBG Act 1995, mandates the Bank to, in addition to the pursuit of these core objectives, encourage and promote sustainable economic development and efficient utilisation of resources of The Gambia through the effective and efficient operation of the financial system' (Article 54. 1d). The Bank has spearheaded the development of an extensive microfinance system in the country made up of Village Savings and Credit Associations that has contributed significantly to enhancement of financial inclusion in the country. Other recent developmental interventions by the CBG include the establishment of a Collateral Registry and Credit Reference Bureau. These institutions were established to promote efficiency, transparency and information disclosure in the credit market to encourage lenders to grant loans to small and medium scale enterprises. The Bank also set up a National Switch Company in line with modernisation of the payments system in collaboration with the WAMZ Payments System Development Project.

A one-off quasi-fiscal intervention was undertaken in early 2015, under which the CBG settled the external liabilities of some key public enterprises at risk of defaulting on payments due to its major multilateral creditors that could have jeopardised the country's entire development portfolio with those institutions. Although the fiscal authorities issued bonds to the Bank in respect of the transaction, the intervention

had resulted in a significant drawdown on the nation's foreign exchange reserves.

3.2.2 *Bank of Ghana*

The current legal framework for the Bank of Ghana implicitly recognizes developmental functions as an integral part of the mandate of the Bank. Section 3(1) of the BOG Act of 2002 (Act 612) states that the primary objective of the Bank of Ghana shall be maintenance of stability in the general level of prices. Nevertheless, Section 3(2) of Act 612 states that without prejudice to subsection 3(1), the Bank of Ghana shall support the general economic growth and effective operation of the banking and credit system.

In due recognition of the second provision therefore, the Bank of Ghana has made significant efforts in promoting economic growth. However, its recent interventions have largely been restricted to development of the financial sector, which in turn is expected to stimulate growth and development. Some of the key interventions undertaken by the Bank during the last decade include the:

- I. *Establishment of a Collateral Registry:*
The Bank of Ghana, in 2010 established a Collateral Registry as a credit information system to help perfect security interest through its registration services, promote transparency in the credit delivery system by providing avenues for searches to be conducted on its database, promote fair credit practices through discharges and renewal and facilitate the enforcement of security right through realization.

- II. *Licensing of Credit Bureau:* The Bank of Ghana has licensed private Credit Bureaus, which serve as credit reporting system, provides credit data submission, protect and manage data, as well as effective dissemination of credit information. The overall objective is to reduce information asymmetry in credit market, improve access to credit by small and medium scale businesses, reduce probability of default on credit, and promote financial stability and efficient resource allocation.

3.2.3 Central Bank of Guinea (BCRG)

The primary objective of the monetary policy of the BCRG is to achieve and maintain price stability and a stable financial system. A secondary function is to support the general economic policy of the government in conformity with the market economy principle of promoting an efficient resource allocation without prejudice to the achievement of the price stability objective. One of the developmental functions of the BCRG is to enhance financial inclusion by promoting and regulating micro finance institutions, insurance and financial market bodies.

The statute of the BCRG stipulates that the bank cannot grant direct or indirect credit either to Government or to any other public body or entity of the state, except the short-term financing necessary for the day to day treasury management. All financing of government must at any time not exceed 5.0 percent of average of the previous year's tax revenue and must be guaranteed by negotiable state securities. The latter may acquire state securities, provided those acquisitions take place solely on the secondary market.

However the BCRG intervened in the economy recently by offering guarantee facility for financial institutions granting credit to financial institutions lending to public infrastructure projects, including roads and electricity.

3.2.4 Central Bank of Liberia (CBL)

The CBL ensures the establishment of a vibrant financial sector characterized by relative stability in the value of the Liberian dollar with sustained single-digit inflation. The Bank continues to work towards financial deepening in order to ensure sustained flow of credit and the provision of other financial services to the private sector so as to stimulate economic activities. The CBL launched stimulus initiatives targeting critical sectors such as agriculture, industry and services. Some of the recent direct interventions include:

SME Credit Stimulus Initiative: The Central Bank of Liberia (CBL) initiated the Economic Stimulus Initiatives (ESI) SMEs credit stimulus in 2010, in order to make financing more accessible to Liberian-owned SMEs at lower rates and longer tenors. An initial placement of US\$5 million was provided under the scheme. Loans extended to the private sector under the program were offered at an interest rate of 6 percentage points lower than the average commercial bank lending rate of 14 percent. It targets employment creation in sectors such as manufacturing, agriculture and fisheries among others. Since the commencement of the program, in December 2010, ten sectors in three counties have benefitted from the scheme. The scheme has also created 2, 812 jobs.

Mortgage Credit Stimulus Initiative: The Mortgage credit stimulus initiative was designed to provide loans for low income earners for mortgage financing. The initiative was launched on November 13, 2012 by CBL, with a long-term placement of US\$10 million with the Liberian Bank of Development and Investment (LBDI) to engage in mortgage lending at an interest rate not exceeding 8 percent including commissions and fees. The scheme has benefitted 17 females and 46 males from two Counties.

Agricultural Credit Stimulus Initiative: The Agricultural Credit Stimulus Initiative was designed to help empower farmers by improving access to finance. This initiative was launched in November 2012 with the initial placements of US\$5 million and L\$181.25 million at a commercial bank with a minimum interest rate of 2.5% per annum. Since the establishment of the initiative, five key products/sub-sectors have benefitted, including Rubber (US\$0.750 million and L\$18.125 million), Cocoa (US\$1,125 million and L\$25.378million), Coffee, (US\$1,125,000.00 and L\$25.375 million), Oil Palm (US\$1. 0 million and L\$21.75 million), and Animal Husbandry (US\$1.0 million andL\$90,625,000). The initiative is estimated to have created 1, 931 jobs. Other initiatives under the agricultural sector stimulus included that of:

Cash Crops under which a total of US\$4 million and L\$90.625 million was made available by the CBL to a local bank for onward lending to farmers involved in the production of rubber, coffee, cocoa and oil palm;

Livestock and poultry initiative scheme making available about US\$1 million and L\$90.625millionthrough local banks for on-lending to livestock and poultry, fisheries and other farmers engaged in livestock and poultry farming.

Credit Stimulus Initiative: The Liberian Business Association (LIBA) credit stimulus initiative was designed to make financing more accessible to the private sector-particularly Liberian-owned businesses. The amount of US\$5 million placement was made available as stimulus support for LIBA members for a period of five years, with an interest rate not exceeding 7 percent. The aim is to support Liberian entrepreneurship and the creation of the Liberian middle class to ensure long-term growth and stability of the country. The stimulus initiative has benefitted seven counties.

Loan Extension Assistance Facility (LEAF): The CBL launched the LEAF in January 2012, providing L\$200 million to support low cost loans to microfinance institutions, credit unions and Village Savings and Loan Association (VSLAs) throughout the 15 counties for on lending to their members, at an interest rate of 3 percent per annum over a three-year period. Following the establishment of the scheme, the membership of LEAF increased by 27 percent to 4,000. In addition, 9 Microfinance Institutions, 109 Credit unions, and 246 Village Savings and Loan Associations benefitted from the scheme. The CBL has also embarked on the campaign of decentralizing commercial banks in all of the 15 counties. The Bank is providing both financial and technical support to the Rural and Community Financial Institutions (RCFIs) with the approval of the Board of Governors.

Table 2: Summary of CBL’s Intervention in Real and Financial Sectors of the Liberian Economy

Intervention	Objective	Date of Commencement	Fund (USD)
SME Credit Stimulus Initiative	Empowering Liberian-owned SMEs	December 2010	5.0 mil
Mortgage Credit Stimulus Initiative	Providing loans for low income earners for mortgage financing	November 2012	10.0 mil
Agricultural Credit Stimulus Initiative	To empower farmers by improving access to finance	November 2012	7.5 mil
Cash Crops Stimulus Initiative	Empowering farmers involved in production of cash crops	November 2012	5.25 mil
Livestock and Poultry Initiative	Empowering farmers involved in livestock and poultry farming	November 2012	2.25 mil
LIBA Credit Stimulus Initiative	Empowering the private sector (Liberian-owned businesses)	January 2012	5.0 mil
Loan Extension Assistance Facility (LEAF)	Supporting low cost loans to microfinance institutions, credit unions and village savings and Loan Associations (VSLAs)	January 2012	2.76 mil
Total			37.76 mil

Source: CBL and WAMI

3.2.5 Central Bank of Nigeria (CBN)

The CBN has made significant interventions in the real sector of the economy in the last decades. The Bank had intervened in some sectors of the economy in accordance with Section 31 of the CBN Act of 2007. Each of the interventions has its peculiar objectives and guidelines for effective administration. These include:

N300 billion Power and Airline Intervention Fund (PAIF): This intervention was designed to unlock the credit market and fast-track the development of electric power projects and the aviation sector. It is also to serve as a credit enhancement instrument to improve the financial position of the Deposit Money

Banks (DMBs). It is to improve power supply, generate employment and enhance the living standards of the citizens. In addition, it is to provide leverage for additional private sector investments in the power and aviation sectors. The source of funding for this intervention has been debenture stock issued by the Bank of Industry (BOI). The funds and loans are to have a maximum tenor of 15 years as determined by the Project’s cash flow profile not exceeding July 31, 2015. A working capital facility shall be of one-year duration with provision for roll-over but not more than 5 years. Repayments under this facility have been amortised. Impact evaluation is yet to be done but there are indications that this intervention has succeeded in sustaining the

airlines in the industry. One of the achievements of the PAIF is the development of long-term financing products for infrastructure projects. As at end March 2014, ₦ 233.161 billion was disbursed to 46 projects. It also increases electricity generation, and also sustained the operations of the airlines which could have gone moribund.

N200 billion Commercial Agriculture Credit Scheme (CACS): The objectives of CACS are to: i) enhance national food security by increasing food supply and affecting lower agricultural produce; ii) provide credit support to targeted agricultural commodities along the entire value chain; and iii) fast track development of the agricultural sector by providing credit facilities to commercial agricultural enterprises at a single-digit interest rate. Financing source has been refinancing and restructuring, including three years cash flow allowance and/ or working capital facility of one year with provision for roll over. The Scheme commenced on May 14, 2014 and was initially expected to end at September 30, 2016. However, the end-date was extended to September 30, 2025. Regarding exit strategy, the loans shall have a maximum tenure based on the gestation period of the enterprise. The Scheme also allows for moratorium in loan repayment schedule, taking into consideration the gestation period of the enterprise. In addition, each State Government could borrow up to ₦1.0 billion for on-lending to farmers' cooperative societies and other areas of agricultural development. A full impact assessment on the scheme had not yet been carried out by the authorities. It was however estimated that since its establishment, the scheme has created over 160,000 jobs, increased agricultural production, especially

rice, and over 300 projects in the agricultural value chain had received funding at a below market interest rate of 9 per cent.

Agricultural Credit Guarantee Scheme Fund (ACGSF): The fund was set up through the joint initiative of the Federal Government and the Central Bank of Nigeria. The Federal Government holds 60 per cent and the Central Bank of Nigeria, 40 per cent of the shares. The aim of the scheme is to encourage banks to support the agricultural sector, by providing guarantee for loans for crop and livestock production, processing and marketing. Under the scheme, any default suffered by banks in the course of lending to the agricultural sector is settled to the tune of 75 percent of the defaulted amount after netting out securities pledged. As at March 2014, a total of 876,608 loans valued ₦74.08 billion have been guaranteed, of which ₦50.88 billion have been fully repaid by 660,108 farmers (CBN, 2014). Also, a cumulative total of 14,471 default claims valued ₦530.5 million have been settled for participating banks

N200 billion Small and Medium Enterprises Credit Guarantee Scheme (SMECGS): The project was designed to: i) fast track the development of the manufacturing SME sector by providing guarantee for credit from banks to SMEs and manufacturers; ii) set the pace for industrialisation of the Nigerian economy; iii) increase access to credit by promoters of SMEs and manufactures; and iv) increase output, generate employment, diversify the revenue base, increase foreign exchange earnings, and provide inputs for the industrial sector on a sustainable basis. This scheme is wholly financed by the CBN and loans advanced under the scheme have tenor of seven years and/or working capital facility of one year with provision for roll over. The

scheme allows for moratorium in the loan repayment schedule. It has encouraged banks to lend the sum of N3.084 billion directly from their balance sheet to 65 projects.

Interest Drawback Programme (IDP): The aim of the programme is to provide interest rebates to farmers that borrowed under the Agricultural Credit Guarantee Scheme to reduce the cost of borrowing and burden of high interest rate. The fund was established with contributions from the Federal Government (60 per cent) and Central Bank of Nigeria (40). As at march, 2014, the resources of the IDB stood at ₦1.86 billion. Since its establishment, the IDP Fund has provided interest rate rebates of ₦ 2.234 billion to a total of 273,609 farmers who repaid on schedule.

N200 billion Intervention Funds for Refinancing and Restructuring bank loans to SMEs (SMERRF): The objectives of this scheme were to: i) fast track the development of manufacturing sector by improving access to credit to manufacturers; ii) improve the financial position of Deposit Money Banks (DMBs); and iii) increase output, generate employment, diversify the revenue base, increase foreign exchange earnings, and provide inputs for the industrial sector on a sustainable basis. The source of finance for the scheme is a debenture stock issued by the Bank of Industry (BOI). The loans shall have a maximum tenor of 15 years and/ or working capital facility of one year with provision for roll over. The Fund allows for moratorium in the loan repayment schedule. The SMERRF has financed 574 projects valued above N300 billion, and resuscitates over 270 moribund projects. Also, projects funded under the scheme have increased their annual turnover by 25 per cent. It also contributes to job

creation with over 20 per cent increase in the number of employees.

N200 billion Micro, Small and Medium Enterprises Development Fund (MSMEDF): This Fund was established to channel low interest funds to the MSME sub-sector through PFIs to i) enhance access by MSMEs to financial services; ii) increase productivity and output of microenterprises; iii) increase employment and create wealth; and iv) engender inclusive growth. This intervention scheme is financed by CBN. The facility has a maximum tenor of one year for microenterprises and up to five years for SMEs with option of moratorium. PFIs shall access the fund as many times as possible upon full repayment. Impact evaluation strategies include i) on-site verification and monitoring of projects under the Fund by the CBN and PFIs during the loan period; ii) off-site ICT based reporting system to provide up-to-date information on the Fund's activities; iii) Reports of the monitoring exercise shall be shared with concerned PFIs; iv) CBN shall leverage Apex Associations' capacities and information in monitoring and evaluation; and v) the CBN shall periodically evaluate the activities of the PFIs to ensure achievements of the Fund's objectives.

N300 billion Real Sector Support Facility (RSSF): This intervention scheme was designed to: i) improve access to Nigerian SMEs to fast track the development of the manufacturing, agricultural value chain, and services subsectors of the economy; and ii) increase output, generate employment, diversify the revenue base, increase foreign exchange earnings, and provide inputs for the industrial sector on a sustainable basis. The CBN is the sole financier of this scheme. The loans have a maximum tenor of 15 years, depending on the complexity of the project

and shall terminate December 31, 2030. Each project tenor is determined in relation to its cash flow and life of the underlying collateral. The scheme also allows a working capital facility of one year with provision for roll over of a maximum of three years. Further, a moratorium of one year in the loan repayment schedule is granted under the scheme.

Entrepreneurship Development: Since 2008, the CBN had engaged in entrepreneurial

development through the establishment of CBN Entrepreneurship Development Centres (EDCs) across the country. The EDCs were set up to develop entrepreneurial skills among Nigerian youths; generate employment and provide a platform for the growth of indigenous entrepreneurship and industrialization of the country. Following the establishment of the EDCs, over 5,000 entrepreneurs had been trained, and a total of 1,812 jobs created.

Table 3: Summary of CBN's Intervention in Real and Financial Sectors of the Nigerian Economy

Intervention	Objective	Date of Commencement	Fund (US\$)
Power and Airline Intervention Fund (PAIF)	To unlock the credit market and fast-track the development of electric power projects and aviation sector	September 2010	1.98 billion
Commercial Agriculture Credit Scheme	To enhance national food security and credit support to targeted agricultural commodities	May 2014	1.33 billion
Agricultural Credit Guarantee Scheme Fund (ACGSF)	To support the agricultural sector	August 1978	0.49 billion
Interest Drawback Programme (IDP)	To provide interest rebates to farmers that borrowed under the ACGS	February 2010	0.01 billion
Small and Medium Enterprises Credit Guarantee Scheme (SMECGS)	To empower SMEs and manufacturers	March 2010	1.36 billion
Refinancing and Restructuring bank loans to SMEs (SMERRF)	To fast track the development of manufacturing sector by improving access to credit to manufacturers	March 2010	1.32 billion
Micro, Small and Medium Enterprises Development Fund (MSMEDF)	To enhance access by MSMEs to Financial services	August 2013	1.27 billion
Real Sector Support Facility (RSSF)	To improve access to Nigerian SMEs to fast track development	December 2014	1.77 billion
Entrepreneurship Development	To develop entrepreneurship spirit and skills among Nigerian youth, etc.	N/A	N/A
Total			9.54 billion

Source: CBN

3.2.6 *Bank of Sierra Leone (BSL)*

Developmental functions of the BSL were mainly restricted to financial sector development unlike other Member States. The perspective could be understood within the context that the country just came out of civil strife. The key developmental activity was the establishment of community banks. Following the end of the rebel war, the BSL took the initiative to establish six pilot Community Banks (CBs) namely Marampa-Masimera Community Bank (MMCB), Yoni Community Bank (YCB), Mattru Community Bank (MCB), Segbwema Community Bank (SCB), Zimmi Community Bank (ZCB), and Kabala Community Bank (KCB). The main objective for the implementation of this project was to replace the defunct rural banks and provide financial services for rural communities, as almost all commercial bank branches were destroyed during the war, leaving no form of financial

intermediation to support productive activities. Other objectives for the setting up of the CBs included, making financial services accessible to a large segment of the potentially productive Sierra Leonean population which otherwise have little or no access to financial services; promote synergy and mainstreaming of the informal sub sector into the national financial system; extending banking services to the rural poor, facilitating credit flow to promote trade, agriculture, rural infrastructure and development, promote policies, practices and innovations conducive to rural development and strengthen rural credit delivery system through institutional development. The CBs were established through a 40-year debenture loan of Le4,962,083,454.00, provided by BSL on concessional terms with an interest rate of 0.75% per annum and a grace period of five years on interest payment and ten years on principal repayment.

4.0 ANALYSES OF THE DIRECT INTERVENTIONS BY THE CENTRAL BANKS IN THE WAMZ

This section contains findings from discussions, interviews and information elicited from the structured questionnaire administered during the on-site visit to

member countries. It focuses on why Central Banks in the Zone should or should not engage in development financing and the underlying issues emanating therefrom.

4.1 Should Central Banks in the WAMZ Engage in Developmental Financing?

Although most central banks in the WAMZ have engaged in development financing in the past and some still continued to do that, several questions have been raised about the appropriateness and relevance of such development financing in emerging countries like those in the WAMZ. The debate centres on whether central banks should continue to confine themselves to the traditional functions of price stability or complement these with unconventional measures to address specific developmental challenges in their economies. The views expressed for and against unconventional monetary policies/development finance by policymakers in the survey are summarised below.

4.1.1 *Arguments against Development Financing/ Unconventional Monetary Policies*

Key among the arguments put forward by the respondents are as follows:

- Development financing is the sole responsibility of the government. In almost every jurisdiction, the government is the only entity entrusted with taxation and spending powers on behalf and for the benefit of its citizens. Thus, responsibility for developmental challenges that confront the economy should rest on the fiscal authorities. This

will ensure clear separation of powers in economic management.

- Central banks are finding it difficult even to achieve their primary objective of price stability. Hence, it will be imprudent to saddle central banks with development financing roles that may compromise or conflict with their primary objective.
- Central banks do not have inelastic balance sheets to engage in development financing. Thus, they should not be tempted to use high powered money to finance developmental projects which in the long run may impact adversely the banks' capital base. In the WAMZ, most central banks need recapitalization and until that is done, they will not be able to carry out development financing.
- Central banks are agents of the government or the treasury and central banks' profit and seigniorage revenue are transferred to the treasury. Hence, central banks should not take on board risky assets that could jeopardise future transfers to government but should concentrate on their core functions and transfer any profit made to the treasury for fiscal authorities to fund developmental projects. Thus, direct interventions in the economy by central

banks will impair accountability and obscures responsibility for what are exactly fiscal transfers.

- In a fiscally dominant environment where the central bank is always called upon to finance the fiscal deficit, it will be an added burden to ask the central bank to engage in development financing.
- Central banks bear the risks associated with direct interventions in the economy. As agents of the government, they have to transfer any contingent liability arising out of their direct intervention programmes to the government/ treasury. Since liabilities will eventually be laid at the door step of the Treasury, it is proper that the Treasury be responsible for the development financing and not the central bank.

4.1.2 Arguments for Development Financing/ Unconventional Monetary Policies

The proponents of developmental roles for central banks in the WAMZ argue as follows:

- Central banks need to engage in development financing because certain challenges may not be addressed expeditiously by the fiscal authorities. Considering the fact that decisions of the fiscal authorities regarding what challenge to address and at what time are more often than not clouded with politics, the treasury or the fiscal authorities may not be able to tackle identified challenges expeditiously. This

where central banks should come in to ensure that challenges are tackled based on their economic benefits rather than political advantage to those in power.

- The monetary policy transmission mechanism is weak or completely broken down. Consequently conventional monetary policy may be ineffective in achieving the objective of price and financial system stability. Thus, the need for central banks to engage in some interventions in the economy to facilitate the supply of finance to key sectors to address structural bottlenecks and impediments to holistic and inclusive growth.
- The financial market in most of the Member States is not deep, thereby making access to funds by some relevant sectors of the economy limited. Central banks should therefore explore the possibility of making funds available to viable projects in these sectors, to complement monetary policy
- Development financing activities of the central bank that are properly formulated and implemented could effectively tackle challenges that are likely to have systemic adverse effects on the economy and subsequently impair the attainment of central banks' primary objective of price stability.
- Central banks need not unilaterally decide on development financing schemes but should coordinate their policies with stakeholders including the banks and government.

4.2 Issues Emanating from Recent Developmental Financing in the WAMZ

All the member central banks have implemented some intervention policies at some point in their existence. The objectives of these development finance programmes were to address one challenge or the other. In examining these direct interventions in the economy, one has to assess first the extent to which these measures were within the mandate of or in line with the objectives of the central banks and second, the objectives of the measures undertaken.

It is noteworthy that, aside price stability objective, supporting economic growth or ensuring sustainable economic growth is one of the key objectives of the member central banks of the WAMZ. Thus, undertaking some degree of developmental intervention in the economy is in line with the statutes establishing almost all the central banks in the WAMZ. Of the WAMZ central banks, CBN is the only central bank with dedicated department responsible for development financing.

Direct interventions in the real sector of the economy have been undertaken by the CBN and CBL, while other central banks have focused mostly on developing the financial system of their respective economies. The objectives of most of the interventions in the Member States were to address specific challenge in the real sector or the financial sector development. Other central banks' interventions were directed at addressing general issues mostly in the financial sector regarding payments system, financial deepening and financial inclusion, among others. Thus, programmes targeting the real sector of the economy appeared to have more focused objectives.

4.2.1 Programme Design and Implementation

In most jurisdictions where development financing has been undertaken, the programme design and implementation has been the preserve of the central bank. For instance, in Ghana, the direct interventions in the real sector were designed as subsidiaries of the Bank of Ghana which provided management oversight, while intervention funds for agriculture and industry were initially directly managed by departments of the bank before their conversion into commercial banks. Also, in most member countries where the intervention was to develop and deepen the financial markets, the central bank was the programme designer and implementer. However, in the case of recent interventions in Liberia and Nigeria, the central banks were the designers of the various programmes but the deposit money banks were the implementers.

Furthermore, most of the intervention programmes were designed without any explicit assessment of expected impact on monetary policy and financial stability. Hence, there are no exit strategies imbedded in the intervention programmes. Some programmes do have terminal periods, but these are not linked to the attainment of programme objectives.

4.2.2 Programme Funding

Most of the funds for direct interventions in the economy by central banks of the WAMZ were sourced from the balance sheets of the banks. The fact that the balance sheet of most central banks in the WAMZ are not buoyant has limited the number and size of

interventions that central banks can do. That some central banks are in dire need of recapitalisation implies there is very little that they can do in terms of development financing using their own resources. However, the CBN has shown that funds for direct interventions in the economy can be raised from bond issue and placed at the disposal of deposit money banks for management and disbursement in line with its objectives.

4.2.3 Monitoring and Evaluation

It has been difficult assessing the impact of development financing carried out WAMZ

4.3 Development Finance Challenges in the WAMZ

This section discusses general and country-specific macroeconomic, structural and development finance challenges to form the basis of policy recommendations and conclusion of this paper. As noted in section four, there have been arguments for and against development finance or unconventional monetary policies in developing countries. All WAMZ member central banks perform developmental roles in their respective economies in the pursuit of their monetary objectives at a point in time of their existence. As in many developing countries, WAMZ central banks primary mandate is the pursuit of price and financial stability. Their statutory mandates, however, do not preclude the promotion of economic growth and development to the extent that this objective is consistent with the stability objectives. The study revealed that two WAMZ central banks, the CBN and CBL, have gone a step further and have introduced explicit intervention schemes in selected sectors of the economy that are considered crucial to growth, employment and poverty reduction. Central banks intending to

member central banks. This is because, most of the central bank intervention programmes have been in place for a relatively short period of time and the relevant institutions were yet to carry out impact assessments for the programmes. Some general short-term achievements can however be discerned. Thus, the achievements cannot be measured in terms of medium and long-term objectives of the programmes. It also made it difficult to assess their impact on overall monetary policy as well as the effectiveness the relevant exit strategies.

complement their traditional functions with developmental ones must ensure that the schemes are consistent with their stability objective as both approaches have advantages and disadvantages.

The health of capital base of the Central Bank could represent a major challenge in the Bank's ability to directly finance developmental projects. This is because the loans extended under the development schemes represent risky contingent liabilities on the balance sheets of the central bank. For instance, the institutions benefiting from the programmes could be confronted with challenges specifically, weak corporate governance structure, paucity of trained and qualified staff, lack of institutional capacity, undercapitalization, political interference and insider borrowing/abuse. These challenges may increase the likelihood of distress and insolvency. Some other key challenges could be summarized as follows:

- Inadequate Institutional Framework: Given that development

financing involves concessionary provision of funds below conventional bank financing, the issues of moral hazard on the part of borrowers and adverse selection from the side of the lenders continue to constitute significant challenge to efficient financing of key projects. The WAMZ economies lack infrastructure for collecting, storing and retrieving information about participants in the financial system, as reflected in the non-existence of credit bureaus that maintain information. A starting point for a credit information system is the availability of systems for identifying participants in the market. The absence of such an identification system has been a major factor in the low level of credit market development.

- **Legal and Regulatory Framework:** The absence of supportive laws and regulations severely inhibits the effectiveness of long-term development finance, especially, from non-governmental and foreign sources. The most serious barriers to long-term financing come from issues related to the adequacy of laws and enforcement mechanisms in respect of formation of companies, required disclosure to relevant parties, and protection of the interest of stakeholders.

- **Ineffective Equity Financing Schemes:** In view of the high interest rate on bank financing, equity financing could serve as a veritable alternative but this is also constrained by a number of challenges. These include: low per capita income which constrains savings, absence of government-funded venture capital funds except Ghana Venture Capital Fund and Fidelity Fund; difficulty in evaluating SMEs' investment; long gestation period of investment; and difficulty in liquidation of investments.

- **Absence of Expertise and Capacity for Long-Term Financial Products:** Most development projects are lacking in required managerial capacity that could attract the interest of financier. In addition, financial products for developmental projects are special structured products and completely different in nature from conventional bank financing. Thus most of the financing institutions lack the required skill and expertise in the design and implementation of these products.

- **The critical supply bottlenecks confronting the WAMZ economies vary from one sector to the other but those that cut across all sectors include inadequate and epileptic power supply, poor road infrastructure, lack of access to long term finance, lack of access to markets particularly for perishable agricultural goods, lack of capacity in key technical areas, high interest rate, highly volatility in exchange rate, land tenure issue, and inadequate local raw materials for industries.**

- **The low level of utilisation of developmental funds has been a challenge due to the high level of risk in the banking system as reflected in high non-performing loans ratio and excess liquidity in the system. The commercial banks have excess funds with limited investment opportunities, hence, the banks are not keen to participate in the central bank's development financing schemes to lend to targeted sectors.**

- **Poor targeting of beneficiaries:** Interventions in the agricultural sector are not benefiting the most vulnerable farmers in that more politically connected farmers may take the greater chunk of the funds allotted for the programme.

- Slow Disbursement rates: The process is very slow due to due diligence that the commercial banks attached to the background checks on the applicants, manipulation and political pressures from applicants, as well as application of the funds for the wrong purpose.

- Lack of Synchronisation of intervention programmes: Infrastructural challenges, especially water and energy are widespread in the WAMZ and uncoordinated interventions in one sector accompanied by lack of intervention or non-performance of some critical areas becomes a drag on the sectors receiving intervention.

5.0 CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The study examines the developmental functions of the central banks in the WAMZ. The underpinning is the increasing recognition being given to the need for central banks to play active roles in the promotion of economic development and structural transformation of their economies by moving out of the narrow mandate of macroeconomic stability.

The study discovers that all the WAMZ central banks have developmental functions as part of their mandate and indeed deeply involved in developmental activities in the early days of their establishment. The focus shifted to price stability in the nineties up to around 2008. The emphasis on price stability, however, was undermined by the global financial crisis as it now becomes clearer that central banks need to safeguard financial stability, support growth, address unemployment and poverty frontally.

The study reveals that there has been increasing recognition by most central banks to embrace developmental functions as a means of addressing the huge challenges confronting the real side of their economies, which equally constrain the achievement of price stability objective. The major issue, however, is the heterogeneity in the phase of implementation due largely to balance sheet constraints.

The paper identifies the prevailing challenges of each of the WAMZ economies and proffers country-specific recommendations in addition to general ones that set the limits within which the central bank can operate. The need to set the institutional framework for developmental financing is a key recommendation that cut across almost all the countries.

5.2 Country-Specific Recommendations

With the above noted challenges taken into account, the following country specific recommendations may be considered for short, medium to long term implementation:

5.2.1 *The Gambia*

- i. *The need for interventions in the Agricultural Sector:* A key sector of the Gambian economy that has the potential to contribute significantly to growth, development and monetary policy objective is the Agricultural sector. However, the sector remained subsistent and rain-fed. *The central bank could*

complement government and development partner's efforts by promoting sustainable financing schemes for small holder farmers. The feasibility of the establishment of Agricultural Credit Guarantee Scheme to facilitate banking system lending to the agricultural sector may be considered.

- ii. *Interventions to Promote SMEs:* The feasibility of establishing a venture capital fund to promote the growth of the private sector in the country needs to be crucially considered by the central bank.

5.2.2 Ghana

- i. *Enhancement of Credit Infrastructure:* As identified in the challenge, absence of soft infrastructure such as means for storing and retrieving data on borrowers is a critical challenge, constraining developmental financing by the Bank of Ghana. A starting point for a credit information system is the availability of systems for identifying participants in the market. The Bank of Ghana should develop a robust Credit Bureau system that could track credit history of borrowers. To improve the robustness of the system, the Bank could also take cue from Nigeria by implementing Bank Verification Number (BVN) which can uniquely identify a customer and thereby prevent cases of serial defaults.
- ii. *Partnership with Independent Power Producers:* Ghana energy deficit is currently estimated at 500 megawatts. The country has recorded some progress in tackling the deficit particularly with the recent delivery of power generating ship that could generate 235 megawatt, while about two more other ships are still expected under a 10 year contract with Independent Turkish power producer. This is just one element of the solution because the prevailing problem results from long era of neglect including insufficient rain to operate the hydro facilities, obsolete equipment, inefficiency and long term failure to add capacity to the grid. The BOG could complement government efforts by helping to source offshore facilities at concessionary terms for the various power projects. In addition, the Bank could design financing schemes targeted at independent power producers at concessionary terms.
- iii. *Provision of Equity Fund:* High lending rate was adjudged one of the binding constraints to improved economic activities. The single largest contributor to this precarious situation is astronomical high cost of fund. It is generally believed that per capita income is low in Ghana as a result of which mobilization of savings by commercial banks for long term financing is difficult. Consequently, the banks normally purchase funds from multilateral institutions which normally have idle funds. As expected, the cost of such funds is the Treasury bill rate plus certain premium. To mitigate this challenge, the Bankers Association in collaboration with the BOG has instituted an Equity Fund Scheme which could enable business owners have access to equity capital thereby eliminating the need for bank lending. The Scheme is yet to take off because the shareholders of the banks are yet to fully lend their support. The Bank of Ghana should complement the efforts of the Bankers Association in convincing shareholders of the commercial banks to support this initiative.
- iv. *Skills Building and Enhancement Centres:* Developmental challenges in Ghana are multi-dimensional in nature but most of the times wrongly attributed to lack of capital. Inadequate skill and competence particularly in business and financial management have considerably encumbered a sizeable number of the people from taking advantage of vast opportunities available in the country. Most operators of small and medium

scale enterprises (SMEs) lack the requisite skill to prepare good business proposal that could be acceptable to financing institutions in as much as they are equally lacking in basic business management techniques such as records keeping. The Bank of Ghana could as part of its developmental roles set up Entrepreneur Developmental Centres (EDCs) in the various regions of the country to enhance skill acquisition.

- v. *Liquidity Support to Critical Sectors of the Economy*: The Bank of Ghana has largely relied on short-term interest rate to signal the direction of monetary policy under its inflation targeting regime. The use of short-term interest rate is good to the extent that it helps to anchor expectation and leaves little or no scope for regulatory arbitrage. Interest rate, however, is a blunt instrument and could not be used to address challenges restricted to a particular sector. The implication of this shortcoming on the Ghanaian economy is the fact that an expansionary monetary policy stance achieved by reduction in interest rate may not necessarily lead to flow of credit to critical sectors like manufacturing, which could propel inclusive growth. Thus, the BOG may exploit the use of unconventional monetary policy like liquidity support to these critical sectors.

5.2.3 *Guinea*

Guinea continues to grapple with the outbreak of EVD. Several companies have become distressed with the collapse of agriculture, tourism and mining sectors. This has led to increases in the non-performing loans ratio of the commercial banks. Consequently, the banks are not willing to

lend to the private sector. Under these circumstances, the BCRG should consider developing some stimulus packages for the agriculture, tourism and mining sectors of the economy. These stimulus packages should be directed at priority sectors that have the greatest potential of resuscitating the economy.

5.2.4 *Liberia*

- i) *Revival of the Stimulus Packages*: The outbreak of EVD in Liberia has eroded the gains made by the various stimulus packages rolled out by the CBL. The EVD has resulted in default on loans accessed under these packages. With the country declared Ebola-free (notwithstanding the recent new cases), the CBL could repackage these stimulus packages in order to quickly revive the key sectors of the economy. A more concerted effort in development financing that promotes economic development and structural reform is needed. This approach would require policies aimed at developing the financial sector, promoting financial inclusion, and aligning the financial system with sustainable development.
- ii) *Fiscal and Monetary Policy Coordination*: Effective coordination would mean an ongoing interaction between fiscal and monetary authorities to decide jointly on aspects relating to policy design and implementation. It can also take the form of rules and procedures which reduces unnecessary bureaucracies between authorities or a need for frequent interaction to ensure efficiency of programs and actions.

5.2.5 *Nigeria*

The CBN has rolled out appreciable number of intervention programmes to impact the real sector of the Nigerian economy. However, there is the need for the Bank to review the ongoing programmes and provide solutions to some of the challenges militating against effective implementation of these intervention programmes. More specifically, the CBN has to:

- i) Review most of the existing intervention programmes to see whether the objectives are or closer to being achieved and make clear the intended beneficiaries.
- ii) Minimize the encroachment of intervention funds by politicians and “highly-connected” people. This the Bank can do by developing a strong data base on the key sectors of the economy with regard to demographic, financial and economic statistics. The bank can also carried out some population census in the targeted sectors before interventions are rolled out.
- iii) Put in place programmes to improve the financial literacy of intended beneficiaries. This can be done by intensifying the capacity building of potential beneficiaries regarding bookkeeping, contract negotiation, etc., and choosing a medium of communication for knowledge sharing among the beneficiaries.
- iv) Ensure internal coordination among its own departments to avoid conflicting policy directives to the deposit money banks who are the

implementers of their intervention programmes.

- v) Take a holistic view of the challenges confronting the economy, identify key areas to intervene in and prioritise/synchronise the various interventions to avoid a situation where some interventions become ineffective due to non-intervention in other related sectors.

5.2.6 *Sierra Leone*

The implementation of interventions in critical sectors of the economy by the Bank of Sierra Leone is definitely constrained by the size of the balance sheet of the Bank. Nevertheless, the Bank could still play some critical role by considering the following recommendations

- i. *Development of the Financial Sector:* Bank of Sierra Leone should continue to play the critical role of improving access to finance through rural financial intermediation, encouraging the growth of financial institutions, promote financial literacy and consumer protection, and reducing vulnerability of nonperforming loans. In addition, the Bank should continue to support the development of an efficient payments system, including mobile telephone-based banking, ATMs, money transfers, linkage banking and the downscaling of some commercial banks’ activities into microfinance, thus introducing new concepts/products and more competition.

- ii. *Resuscitate the Development Banks:* The Bank should strengthen efforts to resuscitate the National Development Bank and the National Cooperative Bank, in a bid to facilitate the provision of small and medium to long term funds to particular sectors including agriculture, agro industries and manufacturing and small scale enterprises (SMEs) that are unable to secure commercial bank loans.
- iii. *Stimulus Packages to Revive Agriculture and Tourism:* The two shocks, EVD and collapse of iron ore mines, have hit the Sierra Leonean economy severely. The non-performing loans ratio has increased rendering commercial banks unwilling to lend to the

private sector. In the post-EVD era, the BSL should consider developing some stimulus packages for the agriculture and tourism sectors of the economy. The debts of companies whose businesses collapsed as a result of the shocks that hit the economy should be addressed in the post-EVD reconstruction programme. In this regard, the BSL should consider the creation of a special purpose vehicle in cooperation with the international multilateral financial institutions to take up the bad debts from the books of the commercial lenders. Special long-term funds could be considered for these companies to use to revive their businesses.

5.3 General Recommendations

The foregoing country-specific recommendations should be looked at vis-à-vis the following general recommendations to determine the extent to which the central banks can go in the pursuit of their developmental roles. These recommendations centre on funding, programme design and implementation, programme objectives, monitoring and evaluation as well as exit strategy:

- i) In designing direct intervention programmes, central banks need to have detailed discussions with finance ministries to agree on particular sectors to target and mode of funding the selected intervention programmes. These should be done without compromising the central bank's operational independence.
- ii) In countries where the central bank's balance sheet is not healthy, funding for the development programmes could come by way of complete government support, partnership between the bank and the ministry, central bank guarantee to commercial banks with excess liquidity, and/or concessionary funds from development partners. It is important to note that central banks undertaking development financing need not necessarily and always resort to their balance sheet.
- iii) All direct intervention programmes should have clear-cut objectives with targeted beneficiaries clearly identifiable prior to the implementation of the programme. This to help avoid

encroachment by politicians and “well-connected” business people.

- iv) Monitoring and evaluation tools should be designed with clear deliverables/ indicators in line with the programme objectives and agreed to by all stakeholders before the programme is rolled out.
- v) Exit strategies should also be designed alongside the programme and in line with the programme objectives. These should contain the commencement and terminal points in time, expected impact on monetary policy objectives during the life cycle of the project and the mode of exit at the terminal point. It is important to reiterate that development financing programmes are not supposed to be permanent features of central bank

functions. They are only to be adopted as and when necessary to tackle challenges that are likely to have systemic adverse effects on the economy and subsequently impair the attainment of central banks’ price and financial stability objective.

- vi) All direct interventions by the central bank should be in sync with the government fiscal policy and budget such that central bank quasi-fiscal policies would replace central bank financing of fiscal deficit.
- vii) Central banks should avoid direct interventions in sectors where government policies have created distortionary prices unless the government has agreed to remove such policies.

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