SHOULD THE WEST AFRICAN COUNTRIES FORM A CURRENCY UNION?

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Abstract

This paper examines whether or not the Economic Community of West African States (ECOWAS), comprising fifteen countries, constitutes an Optimum Currency Area (OCA). The paper uses secondary data obtained from the International Financial Statistics Bulletin, covering the period 1986 to 2003. The Vector Autoregressive (VAR) modelling technique was used to investigate the optimality of the community as a currency area.

The study found that shocks to the output growth rate and inflation rates aligned symmetrically. Except for Nigeria and Sierra Leone, shocks to the real exchange rates also aligned symmetrically across countries. However, the degree of openness variable showed asymmetrical disturbance across countries.

This paper thus concludes that a low trade link exists among member countries of ECOWAS, traced principally to the fact that these countries' exports were competitive rather than complementary. The asymmetric disturbance of real exchange rate shocks and the low degree of openness across the countries implied that the sub-region could not effectively form a successful Optimum Currency Area (OCA). Nevertheless, the sub-region exhibits some potential for forming an optimum currency area in the future.

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