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Common Currencies: Precedents and Prospects

by Frank A. Southard, Jr.*

A common currency emerges when two or more political units use the same currency as their sole or predominant legal tender. It may be issued by one political unit (an independent country or a political dependency) and made legal tender in one or several other units, or it may be issued by an institution common to all the participating units.

A common currency is to be distinguished from a monetary agreement by which a group of countries provides for some degree of interchange of their currencies.¹ However, the distinction between the two becomes narrow in some cases. The Latin Monetary Union, organized in 1865 by Belgium, France, Italy and Switzerland, provided for standard coins which all public offices were required to accept, even though they were separately minted by each country. The five-franc silver coin was for many years the standard coin in the four countries.² The Scandinavian Monetary Union, organized by Norway, Sweden and Denmark by treaties concluded in 1873 and 1875, similarly involved identical (but

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His numerous positions with the United States Government included those of U.S. Executive Director, International Monetary Fund and Special Assistant to the Secretary of the Treasury from 1949 to 1962. He has also served as a member of U.S. delegations to various international conferences. Dr. Southard is the author of several books and of articles in professional journals and encyclopedias, all in the field of international economics.

¹ See Nielsen, *Monetary Unions*, 10 *ENCYCLOPEDIA OF THE SOCIAL SCIENCES* 595-601 (1933) [hereinafter cited as Nielson] and BITAR, *LES UNION MONETAIRES* (1953) [hereinafter cited as BITAR].

² Nielson, *supra* note 1, includes a useful brief account; see also H. WILLIS, *A HISTORY OF THE LATIN MONETARY UNION* (1901) and BITAR, *supra* note 1.

separate) coins and notes, the former being lawful money in all three countries and the latter being accepted at par. For all practical purposes, these unions provided for common currencies, although the coins and notes were issued in each country. But other monetary agreements, such as the European Payments Union (in the early post-war years) or the current "Snake" arrangement of the European Economic Community, aim only at convertibility of the currencies of the participants.

The issuance of a currency (in the form of coins or notes) is an attribute of sovereignty. But the sovereign (*i.e.*, the state) can refrain from exercising the right of issue and can confer legal tender status on some other currency, or it can (as did Cuba before World War II and as do Liberia, Panama, and Swaziland today) issue its own coins or notes and at the same time give legal tender status to another currency. This was done by Cuba before World War II and is still done today by Liberia and Panama (all with respect to the U.S. dollar) and by Swaziland (with respect to the South African rand). The International Monetary Fund has admitted to full membership countries which do not issue their own currencies or in which the national currency is of negligible importance.³

There are historical examples of common currencies such as the use of a common monetary unit by all states joining the German Zollverein in 1838 and the use of the Maria Theresa thaler by the short-lived Vienna Union, 1857-1866, involving Austria and states in Germany. The thaler, in fact, circulated as a common currency in an unplanned way in some areas of East Africa and Arabia until recent times, as did Indian rupees (both coins and notes) and British gold sovereigns.⁴

Viewed historically, the term "common currency" embraces both coins and notes. In fact, prior to the twentieth century, coins were the prevailing medium of exchange in many areas of the world. Coins issued by various mints circulated widely as common currency for three centuries. The most notable of these was the silver Mexican peso or "dollar Mex" which was minted in huge quantities in Mexico in the last part of the seventeenth and all of the eighteenth centuries. At various times the U.S. Trade dollar (1873-1887), the Hong Kong dollar, the British dollar (1895-1935), and the "Piastre de Commerce" (issued by France in 1878), competed with the Mexican peso.⁵ Also, as mentioned above, in some areas the Maria Theresa thaler and the coins of the Latin Monetary Union had wide circulation.

These silver coins (as well as gold coins, especially British sovereigns) were accepted on the basis of their known reliability and their silver (or gold) content. Even small differences resulted in dis-

³ This aspect is fully examined in J. GOLD, *MEMBERSHIP AND NON-MEMBERSHIP IN THE INTERNATIONAL MONETARY FUND* ch. 4 (1974).

⁴ An account can be found in Eda, *Currency Arrangements and Banking Legislation in the Arabian Peninsula*, IMF STAFF PAPERS, July 1975, at 510-38.

⁵ SOBRINO, *LA MONEDA MEXICANA* ch. 11 (1972) contains a detailed account of this whole episode. See also KING, *MONEY IN BRITISH EAST ASIA* ch. 1 (1957).

counts, and forgeries were quickly discovered and rejected by traders. In many instances foreign coins were made legal tender; for example, in 1867 the British authorities adopted the Hong Kong dollar, the Spanish real and the Mexican peso as legal tender in the Straits Settlements. In 1903 those coins were replaced by the Straits Settlements dollar as the sole legal tender.

Those "trade dollars" were issued to serve as common currencies outside of the country of issue. They became the chief medium of exchange in large areas, especially the Far East, where they were the mainstay of the "China Trade." However, with the emergence of paper money, such coins were largely replaced by the various common currencies with which this article is chiefly concerned.

I. The Development of Common Currencies.

A common currency provides substantial advantages for the countries using it. The exchange rate within the currency area will be uniform and is likely to be stable over time. There will be few, if any, exchange restrictions, and there is likely to be general freedom from trade restrictions within the area. If the constituent countries are small, or are relatively weak economically, membership in a currency area will provide financial strength.

However, notwithstanding such advantages, and leaving aside a few historical cases, notably the Latin and Scandinavian Monetary Unions, there are very few instances of independent countries choosing to use a common currency. Most common currencies were an aspect of colonial finance, and, except for the CFA franc in West Africa and the East Caribbean dollar, have not survived the emerging independence of the constituent political units.

In the concluding section consideration will be given to the prerequisites of a common currency which complicate current efforts to establish a monetary union and its concomitant common currency. But it will be useful first to examine in some detail the modern history of common currencies.

Unilaterally-adopted common currencies. Liberia and Panama are two current examples of the use of a foreign currency as virtually the sole legal tender in a sovereign state.

1. *Liberia.* As a matter of law, there is a Liberian dollar, equal to the U.S. dollar, but except for subsidiary coinage, only the U.S. dollar circulates. It had been legal tender along with the pound sterling, but in 1943, replaced sterling as legal tender.⁶ In 1974 Liberia established a National Bank, which has the right to issue coins, but not notes, and has the other powers of a central bank. The money supply and the fiscal position are

⁶ See Qureshi, Mizoe, and Collings, *The Liberian Economy*, IMF STAFF PAPERS, July 1964, at 285-326 and unpublished lecture by Charles L. Merwin, Deputy Director (Ret.) of the African Department of the IMF [hereinafter cited as Merwin].

necessarily closely linked to the balance of payments, and the resources of the Bank are limited to relatively small deposits by the Government and commercial banks.

2. *Panama*. Panama has used the U.S. dollar since independence, when the U.S. Secretary of War on June 20, 1904, acquiesced in a Panamanian Act to make it legal tender.⁷ In 1930 and 1931 the U.S. agreed to mint several denominations of Balboas for Panama. However, most of those silver Balboas are in coin collections, and dollar notes and coins provide most of Panama's circulating medium. As in the case of Liberia, the legal exchange rate is at par with the dollar, but has no significance.

Panama has a National Bank and a very active money market well-furnished with the branches and affiliates of a large number of foreign banks. But the National Bank, for the same reason as in the case of Liberia, has little capacity to carry out an independent monetary policy.

Colonial currency arrangements. The colonial powers, especially the United Kingdom and France, devised currency arrangements for their colonies which typically involved the establishment of some form of issue institution. These institutions, whatever their names, were providers of a local currency against the payment of sterling or francs. These latter were invested in securities of the ruling power. In the British areas the "cover" of the local currency typically was 100 to 110 percent and there was no local fiduciary issue, that is, the currency board did not extend credit. In the French areas the issue institutions usually were provided with operations accounts in the French Treasury, and fiduciary issues were common.⁸

These arrangements were a successful effort to replace the melange of coins and notes circulating in the colonies (e.g., Spanish dollars and Mexican dollars) with a single, reliable currency with a fixed (and generally unchanged) exchange rate in terms of the currency of the ruling power.⁹

As the colonies gained political strength and as local governments, traders and industries developed, currency boards came under pressure to take on some central banking functions, particularly to provide credit to local governments and businesses through fiduciary issues, and to invest at least some of the boards' assets in local securities.

1. *East African currency arrangements*. There were two currency areas in East Africa developed under British rule: the East African Currency Board and the Central African Currency Board.

⁷ Agreement on Legal Tender and Fractional Silver Coinage, June 10, 1904, United States-Panama, reprinted in 10 BIVANS, TREATIES AND OTHER INTERNATIONAL AGREEMENTS OF THE USA, 681-83 (1972).

⁸ As early as 1878 a "special current account" in the French Treasury was opened for the Banque de l'Algerie, which issued notes in Algeria and later in Tunisia.

⁹ For a convenient account of British colonial arrangements, see Shannon, *Evolution of the Colonial Sterling Exchange Standard*, IMF STAFF PAPERS, April 1951, at 334-54.

(a) *The East African Currency Board.* The East African Currency Board (EACB) was established in 1919 to provide a currency — the East African shilling — for Kenya Colony and Protectorate and the Uganda Protectorate with the additions of Tanganyika in 1920 and Zanzibar in 1936. The British authorities also used the EA shilling in British-occupied areas in East Africa during World War II.¹⁰

Like all British currency boards, the EACB was an automatic money changer, issuing EA shilling coins and notes against sterling at a fixed rate of EA sh. 20 to £1. All reserves were invested in public sterling securities, and profits and losses were placed in a reserve fund. There was no fiduciary issue and no control over the quantity of money in circulation, which was determined by the balance of payments.

The aim was to maintain a currency cover of 100 percent in sterling securities. But various coins (rupees and local issues) had to be retired at face value and disposed of at metallic value, and not until 1950 were the losses absorbed and a full 100 percent cover reached.

By 1955 the rising tide of local autonomy and prospective independence pushed the EACB into broader monetary functions. EACB began investing a part of the reserve fund in local securities, and in 1957 all three territorial governments placed long-term loans with the Board. In 1959 the Board began purchasing local treasury bills, thus providing, for the first time, some financing of fiscal deficits.

In 1960 the head office was transferred from London to Nairobi and local representation was added to the Board. At that time the EACB began providing seasonal crop financing, opened accounts for commercial banks, and introduced greater flexibility in interest rates. But the total of crop advances and the fiduciary issue were both subjected to fixed limits. By 1962 the limits were raised to 50 percent of total currency in circulation, although in practice they reached 36 percent. At that time 76 percent of EACB assets were invested in external securities.

These developments had carried the EACB a long way from its original role. But it still lacked authority to control credit, require minimum reserves, or accept deposits from the three governments and local banks.

With independence, the three countries in 1965 and 1966, with much technical help from the International Monetary Fund (IMF), established central banks and issued their own national currencies (still named shillings). In 1967 they entered into a treaty establishing the East African Community and Common Market which, *inter alia*, provided for the free exchange of the three currencies at par and for freedom of current transactions. Thus, for a few years, the East African common currency was replaced by a monetary union. Unhappily it, too, disin-

¹⁰ See Kratz, *The East African Currency Board*, IMF STAFF PAPERS, July 1966, at 229-55 and 2 THE INTERNATIONAL MONETARY FUND, SURVEYS OF AFRICAN ECONOMIES (1969).

tegrated as national political, economic and financial differences created stresses.

(b) *The Central African Currency Board.* The Central African Currency Board (CACB) has a history similar to that of the EACB, and can be treated briefly before turning to the more interesting West African Currency Board.

The CACB was organized to issue the Rhodesia and Nyasaland pound.¹¹ In 1956 the CACB was replaced by the Bank of Rhodesia and Nyasaland, which until 1965 continued to issue the R.N. pound. The Bank also carried on the CACB's practice of investing a portion of its assets in the securities of the three governments. In 1965 the three areas separated, with Nyasaland becoming Malawi, Southern Rhodesia becoming Rhodesia and Northern Rhodesia becoming Zambia. Each issued its own currency in exchange for the R.N. pound, which ceased to be legal tender in June 1965.

2. *West African Currency Arrangements.* West Africa provides two important areas of common currencies: the West African Currency Board in the British colonial area and the CFA franc area. The latter survived the independence movement and is still operating at the present time.¹²

(a) *West African Currency Board.* The West African Currency Board (WACB) had a long history.¹³ It was organized to provide convenient coins and notes for four colonies, Sierra Leone, The Gambia, the Gold Coast, and Nigeria. Previously, British coins had been legal tender and traders going into the interior had been burdened with heavy loads of coins. There were also other coins in circulation, especially the two- and five-franc coins of the Latin Monetary Union.

Following the report of a United Kingdom Committee in 1912, the WACB, the first of the currency boards, began operations in 1915 and set the pattern which was faithfully followed in all other British colonial currency boards. That is, the WACB's activities were confined to the issue and redemption against sterling of local coins and notes (the West African pound) at a specified rate of exchange. A full-cover reserve was to be maintained in the United Kingdom in gold and liquid securities. The head office was in London, and there was an office in each of the four territories. Initially each office issued and redeemed only its own notes (identical in appearance but with a distinguishing mark). Later a

¹¹ 4 THE INTERNATIONAL MONETARY FUND, SURVEY OF AFRICAN ECONOMIES 256-57, 417-18 (1971) and Shannon, *The Modern Colonial Sterling Exchange Standard*, IMF STAFF PAPERS, April 1952, at 318-62 [hereinafter cited as Shannon].

¹² Passing reference may be made to another common currency, the franc issued by the Central Bank of the Belgian Congo and circulating also in the Trust Territory of Ruanda-Urundi. In 1960 two separate currencies were issued, and in 1964, following the independence of Rwanda and Burundi, that remaining common currency was exchanged for separate Rwanda and Burundi francs.

¹³ J. LOYNES, A HISTORY OF THE WEST AFRICAN CURRENCY BOARD, (rev. ed. 1974) and [1955-1973] ANN. REP. WEST AFRICAN CURRENCY BOARD.

uniform issue was introduced. Throughout much of the life of the WACB coins were a larger element in the total circulation than notes; but by 1957, when the total circulation was £107 million, notes amounted to £71 million.

The WACB never added to its functions and not until 1963 did it introduce a fiduciary element into its issues. In that year, on the eve of the demise of the Board, The Gambia asked the Board to take a proportion of a development loan. The Board did so and later in the year also made small advances to the treasury. It distributed dividends to the four governments, which, in the period from 1920 to 1969, amounted to £32 million.

With the independence of Ghana (formerly the Gold Coast) in 1957, the disintegration of the WACB began. The Bank of Ghana was established and redeemed the WA pound notes in exchange for the Ghana pound. Nigeria followed in 1959, and Sierra Leone and The Gambia in 1964. The sterling reserve in London was distributed to each of the four new central banks in proportion to its share in the total issue of WA pounds. The reserve had been invested in both U.K. and Commonwealth public securities. In 1956, for example, 17 percent of the reserve was in cash in London and 73 percent in various treasury obligations with maturities of less than five years. In 1968 the notes of the WACB ceased to be legal tender, and in 1973 the Board was terminated.

(b) *French Colonial Currency Arrangements in Africa*. France introduced two currencies into its principal colonial areas.¹⁴ One is the CFA franc (formerly meaning the Colonies Françaises d'Afrique franc, now the franc of the Communauté Financière Africaine; the other is the CFP franc (*i.e.*, the franc of the Colonies Françaises du Pacifique) to which brief reference will be made later. The CFA franc shares with the East Caribbean Currency Authority¹⁵ the distinction of being the only colonial currency to survive the independence of the members, and the latter can be included only because independent Grenada has decided to remain in the ECCA along with the remaining group of British Caribbean dependencies. The CFA franc, in contrast, continues to be the

¹⁴ Before turning to colonial and post-colonial currency arrangements in the French areas and in the Caribbean, reference should be made to the South African rand monetary area, embracing South Africa, Botswana, Lesotho, and Swaziland. Brief accounts may be found in Dini, Quinn, and Wohlgemuth, *The Economy of Botswana*, IMF STAFF PAPERS, March 1970, at 127-69; and 5 THE INTERNATIONAL MONETARY FUND, SURVEYS OF AFRICAN ECONOMIES ch. 2 (1973). In all four countries the South African currency was legal tender in long-standing arrangements. Until recently none of the smaller countries had either central banks or local currencies. However, Botswana in 1975 and in 1976 began the issue of its own currency, the sula, which is the sole legal tender. In 1974 Swaziland established the Monetary Authority of Swaziland to issue a currency, the lilangeni, which has equal legal-tender status with the rand. As of 1977 Lesotho has not issued a local currency.

¹⁵ See *infra* notes 19-20.

common currency of two joint central banks, one comprising as members seven independent countries and the other, five.¹⁶

France operated its sub-Saharan empire by means of two huge administrative units: Afrique Orientale Française (AOF) embracing present day Dahomey, Ivory Coast, Mauritania, Niger, Senegal and Upper Volta; and the Fédération d'Afrique Équatoriale (including present day Central African Republic, Chad, Congo and Gabon). It is not necessary to recount in detail the complicated monetary history of the two areas. As a brief example, the AOF was established in 1895, and a commercial bank, the Banque de l'Afrique Occidentale, was given the right of currency issue. In 1955 the right of issue was transferred to a public institution, the Institut d'Émission de l'Afrique Occidentale Française et du Togo, which was the direct forerunner of the joint central bank serving those countries. The CFA franc circulated as the currency common to the two colonial areas, with an exchange rate set from time to time in terms of the French franc.

With the emerging independence of the components of the two areas in 1959, the French authorities moved swiftly to reorganize the monetary regime, establishing two multi-national central banks to take the place of the existing issue institutions. One is the Banque Centrale des États de l'Afrique Équatoriale et du Cameroun (BCEAEC), including Central African Republic, Chad, Congo, Gabon and Cameroon, which in 1973 was reorganized as the Banque des États de l'Afrique Centrale (BEAC). The other is the Banque Centrale des États de l'Afrique de l'Ouest (BCEAO), including Dahomey, Ivory Coast, Mauritania, Mali, Niger, Senegal and Upper Volta. In 1973 it also was reorganized, omitting Mali and including Togo.

Since the political units had all become independent, treaties and accords were signed in 1960 and 1962, and revised in 1973, establishing a monetary union in each area and setting out in detail the rights and obligations of the signatories, and the financial regime which was being agreed upon. In the case of the West African Monetary Union (establishing the BCEAO) the treaty of 1973 includes 25 articles. It has attached to it an "Accord de Coopération," which contains 15 articles, and a "Convention de Compte d'Opérations," which contains 11 articles. There is also attached a seventy-article statute for the Central Bank.

Both central banks issue the CFA franc, which currently has an exchange rate of CFA Fc. 50 to FFc. 1, long unchanged. While the CFA notes are identical in form, they have letter designations indicating the central bank of issue and the country in which issued, and in each country the Central Bank branch issues only the notes with its letter designation.

¹⁶ *The CFA Franc System*, IMF STAFF PAPERS, November 1963, at 345-96; 1 & 3 SURVEYS OF AFRICAN ECONOMIES (1968, 1970); *Financial Arrangements of Countries using the CFA Franc*, IMF STAFF PAPERS, July 1969, at 289-387; and Merwin, *supra* note 6.

The French authorities have been successful in developing into full-fledged central banks the preexisting institutions which, like those in British colonial areas, had limited their activities almost entirely to non-fiduciary currency issue. Moreover, two other elements have undoubtedly helped to make them acceptable to most of the newly-independent countries: first, the establishing of Operations Accounts in the French Treasury and second, the gradual "Africanization" of the two banks, culminating recently with the transfer of the head offices from Paris to Dakar and Yaounde and with the election of African Governors. France has only two directors out of fourteen in the BCEAO, and three out of twelve in the BEAC.

Taking the BCEAO as the example, it has several important powers in addition to issuing the CFA franc: (1) It may extend credit to the constituent governments up to 20 percent (previously 15 percent) of their revenue in the preceding year; (2) it may rediscount paper for the commercial banks; (3) it administers a policy of flexible interest rates.

From the French point of view, at least, an essential element in the monetary regime administered by the two central banks is the centralization of the foreign exchange reserves in an Operations Account maintained by the French Treasury for each central bank. In return, each bank has an unlimited right to draw against its Account. As the banks acquire French francs and other foreign exchange against the issue of CFA francs, they deposit it in their Operations Account. However, now up to 35 percent may be deposited outside the franc area. When payments deficits occur in either area, the central bank can draw against its Account to acquire French francs (and, using them, buy dollars or other currencies in the Paris foreign exchange market) and can, as indicated above, run a debit balance in its Account if necessary. The constituent members may be expected to take steps to correct the deficits and may be asked to use their drawing rights in the IMF, the proceeds being deposited in the Operations Account. A change in the exchange rate, however, has not been included among such corrective measures.¹⁷ It would require the approval of all member countries and France.

The CFA franc is, then, the common currency for two groups of African countries, totalling eleven countries, each linked in a monetary union and having a common central bank. The circulation of CFA francs is legally limited to the area in which they have been issued, since each central bank has a separate Operations Account in Paris. Up to now the system has functioned smoothly, and assures the constituent countries of freedom of monetary transfers within the French franc zone at a fixed exchange rate with the French franc. Exchange rates with all other currencies move with that of the French franc; hence a constituent country

¹⁷ Article 14 of the Treaty provides that the denomination and the definition of the monetary unit (the CFA franc) can be changed by decision of the Council of Ministers, which consists of the Minister of Finance of each country.

can change its exchange rate only by leaving the monetary union and the CFA franc system. In any monetary union involving a common currency the constituent members must achieve a tolerable degree of harmonization and coordination of economic and financial policy. Wide and persistent disparities in inflation rates and in movements in balances of payments, for example, would give rise to severe strains in the common currency system. This will be referred to again in the final section.

3. *Common currency in the Caribbean.* At the end of World War II the Caribbean, aside from long-independent Cuba, Dominican Republic and Haiti, was an area in which the British, French and Dutch had many colonies. The French and Dutch issued local francs and guilders in their areas. The British (except in the British Virgin Islands where, for obvious reasons of physical propinquity, the U.S. dollar circulates) have for many years operated a common currency which has survived the defections of participants which became independent and which continues today to serve a number of small dependent islands and one independent one (Granada).¹⁸

The British Caribbean Currency Board (BCCB) was established in 1946 to replace earlier diverse currency arrangements and provide a uniform currency for Trinidad and Tobago, Barbados, British Guiana, and the Leeward and Windward Islands. The currency was the British West Indies dollar (the "Beewee dollar"), with an original value of 4s. 2d. in London. The currency agreement¹⁹ provided, *inter alia*, for the establishing of a Currency Fund in London which was to be administered by the Crown Agents to meet any needed redemption of the currency and was to be invested in sterling securities of or guaranteed by the Government of any part of the British Empire or in such other securities as the Agents selected. If the value of the Fund exceeded 110 percent of the face value of currency in circulation, the excess would be transferred to a Currency Surplus account, from which periodically a distribution could be made to the participating Governments on the basis of a schedule set forth in the Agreement or of a later revised schedule. The BCCB, with headquarters in Trinidad, was operated by a Board of Commissioners consisting of five members, one from each participating Government or group of Governments.

In the following years the BCCB took over the preexisting circulation of government notes in British Guiana, Barbados, and Trinidad and Tobago, and by agreement in 1951 acquired the sole right of issue. In 1955 the notes issued by Jamaica and the BCCB acquired reciprocal legal tender status in Jamaica and the BCCB area.

¹⁸ [1953-1965] ANN. REP. OF THE BRITISH CARIBBEAN CURRENCY BOARD; [1965] ANN. REP. OF THE EAST CARIBBEAN CURRENCY AUTHORITY; and Shannon, *supra* note 11.

¹⁹ Reproduced in Shannon, *supra* note 11, at 352-62.

The BCCB was authorized to invest up to BWI \$12 million in securities of the participating Governments, and, at the end of 1960, \$9.8 million was so invested, out of total investments by the Currency Fund of \$100 million. This small fiduciary issue represented the beginning of broader functions than the issue of currency which had characterized British colonial currency boards.

In 1962, Trinidad and Tobago and British Guiana decided to issue their own currencies. A conference was held in Trinidad in January 1964, to plan the dissolution of the BCCB with the Governments of Barbados, St. Vincent, St. Lucia, Dominica, Antigua, St. Kitts-Nevis-Anguilla and Monserrat deciding to issue a new currency and to establish the East Caribbean Currency Authority (ECCA), with headquarters in Barbados. This was done by means of the East Caribbean Monetary Agreement of January 18, 1965. The currency was the East Caribbean dollar, with a parity of 4s. 6d. Provision was made for a reserve of external assets to be not less than sixty percent of the value of the notes and coins in circulation plus other liabilities. There was also provision for a General Reserve Fund to which profits would be transferred and from which periodic distributions could be made to participating Governments.

The ECCA was given greater powers than the BCCB had: it could (1) act as agent of the participating Governments; (2) accept deposits from governments and banks; (3) buy, hold, sell and discount inland bills and notes payable in EC dollars arising from agricultural and commercial transactions and having maturities in 90 days; (4) buy, sell, hold and discount 93 day treasury bills not exceeding 10 percent of the estimated current revenues of the participating Government in the current year; (5) buy and sell securities of not over 17 years maturity and with a total not exceeding EC \$3 million or 15 percent of currency circulation and demand liabilities; (6) buy and sell shares and debentures of any corporation set up under the authority of a participating Government to finance development; and (7) grant advances of up to 90 days to any bank against promissory notes.

It will thus be seen that the ECCA was given virtually all of the powers of a central bank.²⁰ It was evidently recognized that only with such powers could the ECCA meet the needs of the participating countries; merely providing a common currency would not suffice.

The ECCA came into existence on March 26, 1965, following the enactment of enabling legislation by each participating Government. Its governing body consisted of four directors and a managing director. New EC dollar notes were issued in October, in exchange for BCCB notes, and by March 31, 1966, \$24.5 million had been exchanged. Only EC dollar notes

²⁰ On December 17, 1977, the U.S. Internal Revenue Service decided that the ECCA is a foreign central bank of issue and, accordingly, that its income from U.S. securities or bank deposits in the United States are tax exempt. Rev. Rul. 77-482.

were legal tender, but notes of Jamaica, Trinidad, and Guyana were by agreement accepted at par at the discretion of commercial banks. The ECCA acquired from the BCCB securities of the participating Governments totalling \$2 million, and thus, from its inception, had a small fiduciary issue.

With the devaluation of sterling in 1967 the ECCA faced its first major decision, and concluded that the EC dollar should follow sterling, which would maintain the sterling value of the assets in the currency reserve and would help tourism (although it would increase the cost of imports). In 1972 and 1973, with sterling floating, the ECCA maintained the sterling peg unchanged. However, in 1976 the Authority decided to define the parity of the EC dollar in terms of the U.S. dollar, and fixed the rate at U.S. \$1 to EC \$2.70, the then-prevailing rate.

In the following years the ECCA moved slowly in using its broad powers. In 1968 it accepted the accession of Grenada, made its first local short-term investment (in Barbados), and accepted commercial bank deposits. But at the end of 1969 local assets amounted to only EC \$6.2 million, and sterling assets were 91 percent of total assets. By 1971, local assets had doubled, and were 17 percent of total assets. At the same time, deposits of commercial banks with the ECCA greatly increased.

With the decision of Barbados to issue its own currency and to withdraw from the ECCA in 1974, the Authority moved its headquarters to St. Kitts and continued to operate as a central bank providing a common currency for the group of islands still political dependencies of the United Kingdom. When Grenada became independent, it decided to continue as a participant in the ECCA.

The ECCA has thus survived the vicissitudes of reduction in membership and of fluctuations in the exchange rates of sterling and the U.S. dollar. It has felt its way cautiously toward broader functions, making local loans and advances and becoming a major depository institution for both governments and commercial banks. The Authority has continued to hold most of its assets in foreign currencies, the cover in 1976 being 95 percent of currency circulation and other demand liabilities. For the remaining participants, it is difficult to see any sensible alternative to a common central bank and common currency.

4. *French colonial currency in the Pacific.* Brief reference should also be made to the CFP franc, the common currency established by the French authorities to serve French possessions in the Pacific.²¹ The Colonies Françaises du Pacifique franc (CFP franc) was first issued in 1945 as legal tender principally in New Caledonia and French Polynesia. The Institut d'Émission d'Outre Mer (IEOM), with headquarters in Paris, is the issu-

²¹ The most accessible source of information is the ANN. REP. OF THE INSTITUT D'ÉMISSION D'OUTRE MER, Paris.

ing authority.²² The CFP franc has since 1957 been pegged to the French franc at CFP Fc. 1 = FFc. 0.55, and hence parallels the previously described policy of the two central banks issuing the CFA franc in West Africa.

The IEOM carries on extensive central banking activities in addition to currency issue. It makes short-term rediscounts for credit institutions in the area in order to finance exports and provide liquidity to the rediscounting banks. The rediscounts in the period 1974-1976 increased from CFP fcs. 830 million to CFP fcs. 1.3 billion. It makes advances to the treasuries of New Caledonia and Polynesia, which at the end of 1976 amounted to CFP fcs. 1.2 billion. It also makes medium-term rediscounts for a wide range of agricultural, mining, industrial, construction and tourism purposes, which at the end of 1976 amounted to CFP fcs. 4.6 billion.

As in the case of the two West African multi-national central banks, the French authorities provide Operations Accounts in Paris for the participating Governments. At the end of 1976 the external assets of the IEOM amounted to 82 percent of the circulation of CFP francs. If either of the two principal participants incur payments deficits they are financed by the Operations Account, but efforts are then made to correct the imbalance.

The Supervising Council of the IEOM is comprised of six French officials (representing the Treasury, Bank of France, and Minister of Overseas Territories), and three persons with experience in the affairs of the overseas territories. It is thus evident that there has been no development comparable to the "Africanization" of the two multi-national central banks in West Africa. The IEOM is a colonial bank of issue, but with substantial central banking powers which are being extensively used.

5. *The East Indian area.* The monetary history of this area might well merit a separate record, with its numerous and changing sovereignties and its skill in improvising coins and notes (usually the former) with which trade could be carried on. But this article, concerned with common currencies, will deal with two colonial currency experiences: the British in the Malaysian-Singapore area and the French in Indochina.²³

(a) *Malaysia and Singapore.*²⁴ During much of the 19th Century, the Straits Settlements (Penang, Malacca, and Singapore) were a mixing ground for a melange of foreign coins. In 1867 legal tender status was

²² The Institut also issues the CFP franc in Wallis and Futuna and the New Hebrides franc in the New Hebrides, and provides French francs in St. Pierre, Miquelon, and Mayotte (the last being one of the Comoro Islands).

²³ Mention can be made also of the Indian rupee, which as a coin was widely used in Asia, the Arabian Gulf area, and the East Coast of Africa. Notes of the Reserve Bank of India were issued for circulation in Burma prior to 1947.

²⁴ F. KING, *MONEY IN BRITISH EAST ASIA* (1957) and ANN. REP. OF THE COMMISSIONERS OF CURRENCY, MALAYSIA AND BORNEO.

granted to the "Dollar Mex," the Hong Kong dollar, and the silver coins of Spain, Peru and Bolivia; in 1874 the U.S. Trade dollar and the Japanese silver yen were added. As indicated earlier, all of these were, in effect, common currencies. In 1889 the Dollar Mex was made the standard coin. Not until 1903 was a Straits Settlements dollar minted to replace those coins and become the sole legal tender in the entire Malay Currency Area.

Earlier, in 1898, the Board of Commissioners of the Currency was established in the Straits Settlements to issue legal tender notes with a sterling reserve of 100 percent. This dual system of silver dollars and notes continued until 1938, with several reductions in silver content. In that year full legal tender was granted only to the notes of the Commissioners, covering the Straits Settlements, the Malay States, North Borneo, and a portion of the Dutch islands. In 1940 new notes were issued, with the rubric "Malayan dollars," instead of Straits Settlement dollars, although the term "Straits dollar" continued in common usage. After World War II, the Board of Commissioners was reconstituted to include the Malayan Union, Singapore, Labuan, North Borneo, Brunei and Sarawak. The par value of the new notes was \$1 to 2s. 4d.

In 1952, based on an agreement in 1950 between the Governments of the Federation of Malaya, Singapore, Sarawak, North Borneo and Brunei, the Commissioners of Currency, Malaya and Borneo, was constituted with the sole right to issue notes and coins. The aim, which was achieved, was to maintain a reserve in sterling and sterling securities equal to 110 percent of the circulation of notes and coins. As in the case of other British currency boards, profits were distributed to the participating governments.

When the Federation of Malaya became independent in 1960, the 1950 agreement was revised to give Malaya a greater representation on the Board and powers theretofore exercised by the Secretary of State for Colonies were vested in the new Board.

Automatic conversion of dollar notes into sterling at 2s. 4d. continued. The new agreement allowed the Board to invest up to \$300 million in the securities of the participating governments, and also (by unanimous vote) to invest in non-sterling securities other than of the participating governments. But those powers were not utilized, and the Commissioners continued to operate as a currency-issuing authority maintaining a reserve of 110 percent in sterling securities. There was no fiduciary issue.

As in the case of all other British currency boards, except in the Caribbean, this one did not long survive independence. In 1967 the newly-established Central Bank of Malaysia,²⁵ the Board of Commis-

²⁵ The establishing of this Bank may have been hastened by the recommendation of the World Bank in 1955 that a central bank be established in Malaya. See *THE ECONOMIC DEVELOPMENT OF MALAYA*, 227-33, 640-53 (1955).

sioners of Currency, Singapore and the Brunei Currency Board took over the issue privilege and the notes of the old board were redeemed in sterling at 2s. 4d. Subsequently, the split-off of Singapore eliminated the last vestige of a common currency in that prosperous area.

(b) *Indochina*.²⁶ The early French colonial experience in Indochina paralleled that of the British in Malaya. When Admiral Bonnard occupied Cochin China in 1862 there was much the same mixture of coins and the same local preference for silver. In 1878 the French minted a *Piastre de Commerce* with the rubric "*Cochinchine Française*," and in 1884 substituted the words "*Indochine Française*," thus creating a common coin for all territories and protectorates in the area in order to replace the U.S. Trade dollar and other foreign silver coins.

Ten years earlier the *Banque de l'Indochine* had been given the privilege of issuing notes (a privilege which, it may be recalled, was granted later in New Caledonia). But for long years the French authorities (advised by several reports of a Currency Commission) struggled with the problems caused by the fluctuations and secular decline in the price of silver. Gradually the notes of the *Banque de l'Indochine* became important, and in 1920 the French Treasury established an Operations Account for the Bank, as it had done in Algeria and West Africa. The Bank thus became, in effect, the currency-issuing agency of the French authorities. In contrast to the British practice in Malaya, the issue was largely fiduciary (the metallic reserve throughout the Twenties was in the neighborhood of 30 percent), with the Operations Account taking the place of an overseas currency reserve. Periodically, the French authorities set the exchange rate between the piastre and the franc.

With the advent of independence, the French-sponsored piastre was replaced by the separate currencies of the two Vietnams, Laos and Cambodia, and this long episode of a common currency also came to an end.

II. General Considerations and Prospective Developments.

From the preceding sections it can be seen that a common currency has certain characteristics, most or even all of which must be present if it is to survive (or be established) under modern conditions.

A. The currency and coins must be uniform and must be fully legal tender in the whole currency area. This does not preclude the inclusion of designations on the notes (not the coins) to indicate the participating state (or other political unit) in which it is issued. Such a designation is used in the CFA franc area and is planned for the Gulf Dinar (described later), and makes possible intra-area settlement or other credit and policy determinations.

²⁶ A. TOUZET, *LE RÉGIME MONÉTAIRE INDOCHINOIS* (1939), and J. MAZZARD, *HISTOIRE MONÉTAIRE ET NUMISMATIQUE, 1670-1952* (1953).

B. There must be a common foreign exchange rate vis-à-vis outside currencies. This is obviously inescapable, and means that whatever monetary and economic differences may develop among the participants cannot be adjusted by means of exchange rate changes. If there are economically very strong and very weak participants, the resulting intra-area imbalances could be severe. In the case of the two CFA franc areas, the first impact of such an imbalance is absorbed by the Operations Account in Paris. But ultimately, if it persists, there must be policy adjustments and actions by both the strong and the weak units.

C. There must be a substantial pooling of foreign exchange reserves, including the foreign exchange proceeds of foreign credits (such as drawings on the International Monetary Fund). In all cases described above this pooling is by means of a foreign asset reserve or cover maintained in one or more major foreign currencies. The pooling for the Gulf Dinar is planned differently, as will be seen.²⁷

D. The common monetary authority must have most or all of the powers and characteristics of a central bank, including adequate representation of the participants on the governing board.²⁸ The few surviving common currencies which were established in colonial areas had to evolve from currency-issuing authorities into central banks.

E. A corollary of B is that there must be a reasonable amount of coordination and uniformity of policy and regulation in fiscal, financial, trade and other economic matters among the participants, if over time the common currency is to be maintained. For example, it would not be feasible for one participant to run a heavy fiscal deficit or to expand credit to a much greater extent than were the other participants.

In consideration of those essential elements of a common currency area, it is not surprising that there are few such areas in the world today. As the earlier section has described, the common currencies in the British areas of Africa did not long survive the onset of independence. The rand monetary area is disintegrating, notwithstanding the relative economic dependence of the three smaller participants. The CFA franc zone is continuing partly because of the progressive "Africanization" of the two central banks, but chiefly because of the credit facilities provided by the Operations Accounts in Paris. The Caribbean Monetary Authority and CFP Area are surviving because the participants (with one small exception) are politically dependent, and in the British Caribbean area two units (Jamaica and British Honduras) never participated, and two participants withdrew on becoming independent. A separate currency is so widely accepted as an element of political independence that coun-

²⁷ In the special cases of unilateral use of a major currency by a country (Liberia and Panama), the country, except as it can obtain foreign credits, must maintain its own foreign exchange reserves.

²⁸ An exception to this last is the Institut d'Émission d'Outre Mer, where control is fully maintained in Paris.

tries are generally unwilling to make the adjustments and accommodations which membership in a wider currency area would entail, even though its advantages might be great (not the least of which is the wide trade and payments area largely free of restrictions).

It must be concluded that the prospects are not bright for the formation of new common currencies.²⁹ There are, however, two possibilities which should be mentioned.

(1) *The Gulf Dinar*. Four states in the Gulf Area — Kuwait, the United Arab Emirates, Bahrain and Qatar — have completed, over the past two years, the technical preparations for a common currency to be called the Gulf Dinar. The full details have not been published, but the main characteristics can be described.³⁰ If the plan is carried out, this would be the first instance in modern times of a group of independent countries agreeing to establish and operate a new common currency in exchange for their existing separate currencies. The main elements of the plan are as follows:

(a) A new currency and coinage, the Gulf Dinar, would be issued, with designations to indicate the country in which the notes were issued.

(b) A Monetary Authority would be established which would be controlled by the governors of the four central banks.³¹ These banks would issue the Gulf Dinar as agents of the Authority.

(c) An official exchange rate or parity would be adopted, and the four existing currencies would be exchanged for Gulf Dinars on the basis of ratios between their exchange rates and the Gulf Dinar rate.

(d) There would be no actual pooling of reserves. However, a full foreign exchange cover would ordinarily be maintained, with each central bank setting aside an amount of foreign exchange equal to its issue of Gulf Dinars. Periodically there would be a settlement among the four banks, with deficit central banks transferring foreign exchange to creditor central banks. The Authority would keep the reserve records but would not be the actual holder or owner of the reserve. By unanimous vote of the Governors, a fiduciary issue up to 30 percent of total issue could be authorized, to provide fiscal financing.

(e) The Authority would be the coordinating body, arranging for supplies of notes and coins, reviewing financial and economic developments, and either deciding on or recommending to a Council of Finance Ministers changes in the official rate for the Gulf Dinar.

²⁹ Even if the Special Drawing Right of the IMF develops into the principal reserve asset of the world (which is unhappily only a remote possibility) it would not be a common currency as the term is defined and used in this article.

³⁰ Observations are based on the author's service as technical advisor to the four-country working group, 1975-1977.

³¹ Only one institution is called a central bank, but all four are in fact central banks and banks of issue.

(f) The four governments would enact appropriate legislation making the Gulf Dinar legal tender, providing for the transfer of all existing contracts, prices, wages, etc., into Gulf Dinars, and recognizing the existence and powers of the Authority. Also, over time, the four governments would adopt uniform legislation and regulations in areas such as banking, fiscal affairs, wages and tariffs. In other words, the declared intention would be to begin with a common currency and gradually evolve into a common economic area and market.

Whether the plan will ultimately be put into operation by the four countries cannot at this time be forecast. If it is, it would be a unique venture which would greatly strengthen the four countries as an economic and financial area, having in mind that three of the four are substantial producers of petroleum.

(2) *The European Economic Community.* European Monetary Union is an objective of the European Economic Community (EEC) but up to the present time no progress has been made. If it is made, it would contrast with the Gulf Dinar approach. In the latter case a common currency would be a first step to monetary and economic union; in the EEC economic union is evolving first.³²

There have been earnest efforts to push forward the EMU. At the Conference of Heads of State in December 1969, it was agreed that a plan should be drawn up during 1970 "with a view to the creation of economic and monetary union." On March 6, 1970, Pierre Werner, of Luxembourg, was designated to head a committee of appropriate ministers formed to prepare a plan. The resulting report³³ was issued in mid-1970.

The "plan by stages" proposed in the report aimed at a monetary union within the Community which would involve an "irreversible convertibility of currencies, the elimination of margins of fluctuations in exchange rates, the irrevocable fixing of parity rates and the complete liberation of movements of capital." There could be either a sole Community currency or the maintenance of national monetary symbols, but the Report favored the former. Decisions on monetary policy (liquidity, rates of interest, intervention in foreign exchange markets, etc.) would be centralized, and there would be fiscal harmonization. In the first stage there would be coordination of national policy in all matters. Later, responsibility would be transferred to Community authorities. A "European Fund for Monetary Cooperation" would be created under the control of the governors of the central banks as an organ for man-

³² Aside from the Belgo-Luxembourg Economic Union, there is no case of a common currency within the EEC area. In that case, both currencies are legal tender in Luxembourg.

³³ REPORT TO THE COUNCIL AND THE COMMISSION ON THE REALIZATION BY STAGES OF ECONOMIC AND MONETARY UNION IN THE COMMUNITY (1970) (the "Werner Report").

agement of reserves. In the final stage there would be a pooling of reserves and a Community system of central banks.

The Council of Ministers endorsed the conclusions of the Werner Report in June 1970, and agreed that the final objective, including the adoption of a sole currency, should be reached in the course of the ensuing decade.

There was attached to the Werner Report a Report of a Committee of Central Banks of the EEC, outlining the various possibilities. The Governors considered it premature to adopt a single Community currency, or even to link all Community currencies by parities and fixed rates. As a beginning they favored a differentiation between intra-Community margins of fluctuation and extra-Community margins, thus foreshadowing, in 1970, the development of the European "Snake" in 1973. The Governors agreed that in the final stage, if European Monetary Union (EMU) was to be realized, margins of fluctuation among EEC currencies would have to be eliminated, foreign exchange reserves would have to be pooled and managed in common, and a Community Authority (analogous to the Federal Reserve Board of the U.S.) would have to be established.

All of this thinking was in 1970. But the decade is nearing an end, and, except for a limping "Snake" arrangement centered on the Deutsche mark, there has been no progress toward EMU and a Community Currency. Toward the end of 1977 there was a flicker of life in the EMU. Mr. Roy Jenkins, President of the Commission of the European Community, in a speech in Florence on October 27, sought to give EMU a push. He set forth seven arguments in favor of EMU, and asserted that the concept of gradualism or backing into monetary union would not produce results. However, it does not appear that Mr. Jenkins' effort will produce early action. The only result has been the presentation by Mr. François-Xavier Ortoli (EEC Finance Commissioner) of a paper submitted to the EEC summit meeting in December 1977, proposing a five-year plan with economic targets for each country, closer coordination of exchange rates, an increased EEC budget to help poor countries, free movement of capital, etc. As *The Economist* concluded,³⁴ these proposals do not amount to Mr. Jenkins' "great leap."³⁵

It must be concluded that a common currency for the EEC is so far down the road as to be invisible. It is also not clear that the Gulf Dinar will be brought into existence. Hence, with little prospect for new

³⁴ November 26, 1977, at 60.

³⁵ A group of European economists in 1975, and again in 1977 following Mr. Jenkins' speech, proposed as an alternative first phase the introduction of a parallel currency, the *Europa*, to be freely interchangeable with national currencies, based on a weighted basket of currencies and given a purchasing power guarantee. When the circulation of *Europas* reached some predetermined proportion (say, 60 percent) of each country's currency circulation, monetary authority would shift to the Community. See *THE ECONOMIST*, December 3, 1977, at 71-72.

movement, common currencies are limited to the few which have been described earlier in this article. There are, and will continue to be, informal currency areas, such as the European "Snake," the countries pegging to the U.S. dollar, and countries continuing to peg to sterling. But these do not at all amount to common currencies.