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**The Economics of Currency
Redenomination: An Appraisal of CBN
Redenomination Proposal**

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ABSTRACT

On 14th August 2007, the Central Bank of Nigeria (CBN) through its governor made public its proposal to restructure and redenominate the naira by dropping two zeros or moving two decimal points to the left from the currency and issuing more coin denominations with a view to ensuring macroeconomic stability and efficient payment system. The announcement, which took many by surprise, generated a lot of debate among Nigerians and non-Nigerians within and outside the country. While some are of the view that the CBN deserves commendation for the bold step, others are condemning the entire proposal, yet another group try to synthesise the various views from political economy perspectives. Although, the scheme has since been suspended, stakeholders and observers continue to express their views and opinions about the desirability and timeliness of the policy. Accordingly, this paper appraises the suspended naira redenomination scheme in the light of its objectives. The paper is descriptive with presentation based on literature survey and desk analysis. The paper confirms that currency redenomination is based on some happenings within a country and its outcome depends on various fiscal and monetary policies aimed at stabilising the economy. It further posits that redenomination of the naira is not completely a bad policy despite the problems associated with it. It however, suggests that the new strategy should be thoroughly studied and understood, and should go beyond its psychological and portability effects; it should be associated with broader macroeconomic and fiscal objectives.

BACKGROUND OF THE STUDY

Since 1960, governments of developing and transition economies have redenominated their currencies on approximately seventy occasions (Mosley, 2005). Redenomination generally involves the process whereby a country's currency is recalibrated through reduction in the number of zeros in the currency with a view to achieving a set of given economic and fiscal objectives.

While decisions on denomination and design of currencies may seem more technical than political, a government's control and administration of its currency and transactions within its boundaries is one of the hallmarks of the modern nation-state. Even though such monetary control began in the mid-nineteenth century, today, the main struggle is still to maintain this control, particularly in the face of civil conflict or economic collapse (Woodruff, 1990 in Mosley, 2005).

Accordingly, researches contend that currency redenomination may come as part of a broad package of economic and political reforms, as was the case in Afghanistan in October 2002, following years of decline in the currency's value, a new afghani was introduced, with three zeros removed; or a means by which credibility of the currency would be restored, as was the case in Turkey, leading to reduction in the nominal value of its Lira by six zeros (Mosley, 2005); or a measure by which government attempt to reassert monetary sovereignty and counter citizens' lose of confidence in the national currency (International Monetary Fund, 2003; Cohen, 2004), as was the case recently in Zimbabwe and Ghana, where three and four zeros were removed from the old Zimbabwean dollar and cedi respectively (Admowa, 2007); or when countries are experiencing hyper-inflationary pressures which have the effect of making its local currency unattractive, as was the case before redenomination in Brazil, Argentina and Peru (Ajayi, 2007; Lead Capital Limited, 2007; Martinez, 2007).

In a bid to ensure macroeconomic stability and efficient payment system, Nigeria joined the league of countries that adopt currency redenomination. The Central Bank of Nigeria (CBN), through its governor Professor Charles Soludo, on August 14th 2007 made public its proposal to restructure the naira by dropping two zeros or moving two decimal points to the left from the currency and issuing more coin denominations, thereby making the old N100 note equivalent to N1, while N1 equate N0.01 or 1 kobo. The plan to restructure the naira was a

deliberate effort to consolidate on the 13-point reform agenda designed to restructure, refocus, and strengthen the Nigerian banking and financial system.

According to CBN (2007), a totally new currency structure with N20 being the highest and 1 kobo being the lowest will be introduced and implemented from August 1st 2008. The thrust of the reform is to the apex bank is to stabilise exchange rate, reduce inflation, reform microfinance, restructure the lower denominations of our currency and re-introduce coins, as well as promote the efficiency of the payments system.

Soon after the announcement, Nigerians and other observers greeted the new reform agenda with mixed feelings resulting public debates and arguments on the desirability and workability or otherwise of the proposed scheme. While some are of the view that CBN deserve commendation for the bold step, which in their view will not only stabilise the naira and checkmate capital outflow but also control looting of public funds to easily become millionaires/billionaires, others are condemning the entire proposal either because they are traditional opponents or for lack of due process and consultation, yet another group try to synthesise the various views from political economy perspectives.

Although, the new scheme was later put in abeyance due to politico-economic and juridical reasons, Nigerians and other observers continue to express their views on both the announcement and suspension of the new reform for the naira. It suffice to state that a private dedicated website for the proposed scheme, www.nairaland.com, has in less than three month since the pronouncement recorded over 8836 views. Similar to this are found in other electronic and print fora.

The first concern raised by many people is whether the proposal is timely and even necessary. This concern may not be unconnected with questions such as what explains the use of redenomination by a country and why do some governments shelve it even in the face of, or after the resolution of, high inflation and/or other factors, while others embrace it immediately and why do some nations embrace redenomination but with a long lag?

A second concern relates to the workability of the currency redenomination and its ability to solve the pressing economic problems of massive unemployment, deep and severe poverty, insecurity of lives and property, infrastructure deficiency

(especially power and transportation), education crisis, low level technology and lack of institutions of compliance that are staring Nigerians in the face. The proponents of this concern might have borrowed a leaf from the experience of some Latin American countries like Brazil and Argentina that had more economic crisis even after currency redenomination some years back.

A third problem, though not very popular and strong that observers pointed out is the tendency for the new policy to bring confusion to the economy given the level of illiteracy and corruption in the country.

These and other related problems automatically raise the following questions: what are the reasons for and the benefits and costs of currency redenomination? Is redenomination desirable and timely in Nigeria? What pertinent factors must be addressed to successfully implement desired currency redenomination scheme in a country?

This paper appraises the proposed suspended naira redenomination scheme in the light of its objectives as announced by the CBN governor. The paper is descriptive with presentation based on literature survey and qualitative analysis. The paper adopts the seven hypotheses formulated and tested by Mosley (2005) to explain some of the reasons why countries opt for currency redenomination. The aim is to examine the underlying factors that characterise the new scheme in the light of the hypotheses. We consider this approach suitable given the fact that the CBN proposed policy has already been suspended and that no quantitative data exist in respect of the new reform for the naira.

The remainder of the paper is organised as follows. Section two gives the conceptual framework and reviews relevant literature. Section three discusses the financial and accounting impact of redenomination. Section four presents the proposed redenomination of the naira in perspective; it x-rays the objectives of the proposed scheme and tests Mosley's hypotheses in the light of the objectives. Section five concludes the paper and offers suggestions.

CONCEPTUAL FRAMEWORK AND LITERATURE REVIEW

Currency redenomination is the process where a new unit of money replaces the old unit with a certain ratio. It is achieved by removing zeros from a currency or moving some decimal points to the left, with the aim of correcting

perceived misalignment in the currency and pricing structure, and enhancing the credibility of the local currency (CBN, 2007). According to Mas (1995), redenomination also extends to adding of zeros to the currency as recorded in the immediate post-independence period by South Africa (1961), Sierra Leone (1964), Ghana (1965), Australia (1966), The Bahamas (1966), New Zealand (1967), Fiji (1969), the Gambia (1971), Malawi (1971) and Nigeria (1973). According to CBN (2007) however, adding of zeros to the currency is called decimalization, which in management of currencies, is the process of converting from traditional denominations to a “decimal” system, usually with two units differing by a factor of 100.

This reduction or addition, unlike revaluation and devaluation, does not in any way translate to any change in the currency’s value or worth hence purchasing power remains the same. Currency revaluation is an increase in the value of a currency vis-à-vis other currencies under a fixed exchange rate system, that is when the government or monetary authorities arbitrarily fix the exchange rate. Devaluation, the opposite of revaluation is a decrease in the value of a currency vis-à-vis other currencies under a fixed exchange rate system (CBN, 2007; Ojameruaye, 2007).

Redenomination has a long history. It dates back to the 19th century when governments faced shortages of gold or silver, they sometimes adjusted the value of their coins accordingly but the most spectacular one was that of the German currency in the 1920s (Mosley, 2005; Ojameruaye, 2007). According to Mosley (2005), redenominations varied in size, from removing one zero from the currency (14 instances) to removing six zeros (9 instances); the median redenomination was three zeros, dividing the currency by 1000.

In all, nineteen countries have used redenomination on one occasion, while ten countries have redenominated twice, sometimes, with many years in between, as in Bolivia, in 1963 and 1987; in other cases, redenominations follow rather quickly, as in Peru in 1985 and 1991; Argentina (4), the former Yugoslavia/Serbia (5), and Brazil (6) are the most frequent users of redenomination (Mosley, 2005; Martinez, 2007). According to Tarhan (2006), Brazil redenominates 18 zeros in 6 operations (1967/70/86/89/93/94); Argentina 13 zeros in 4 operations (1970/83/85/92); Israel 9 zeros in 4 operations (1980/85); Bolivia 9 zeros in 2

operations (1963/87); Peru 6 zeros in 2 operations (1985/91); Ukraine 5 zeros in 1 operation (1996); Poland 4 zeros in 1 operation (1995); Mexico 3 zeros in 1 operation (1993); Russia 3 zeros in 3 operations (1947/61/98); and Iceland 2 zeros in 1 operation (1981).

There are many reasons why a country will decide to redenominate its currency ranging from credibility and identity to domestic and international politics (International Monetary Fund, 2003; Mosley, 2005; Martinez, 2007). Specifically, though not exhaustive, inflationary pressures, psychological effect, control of currency substitution and domestic politics are identified as the main reasons for redenomination (Cohen, 2004; Mosley, 2005; Tarhan, 2006; Lead Capital Limited, 2007).

Currency redenomination is usually done when countries are experiencing hyper-inflationary pressures which have the effect of making its local currency unattractive. Tarhan (2006) cites a clear case of hyper-inflation with Turkey where a bottle of drinking water costs 300,000 TL, Movie ticket 7,500,000 TL, Toyota Corolla: 32,900,000,000 TL (32 billion), and GDP in 2002: 273,463,167,795,000,000 TL (273 quadrillion) before the old Lira was redenominated by removing six zeros. Also, Aluko (2007) cites the example of Zimbabwe that experienced years of inflation that hit 1200% a year.

Redenomination to address hyper-inflation is however carried out after the country has put in place certain monetary and fiscal policy reforms aimed at ensuring some level of macroeconomic stability (Lead Capital Limited, 2007). According to Mosley (2005), such redenomination can be used at the end of a stabilisation policy to signify to citizens and private markets that the days of inflation are over, as was the case with Russia (1998) and Turkey (2004) after experiencing single-digit inflation rate; or used directly in the stabilisation process as part of an effort to change citizens' inflationary expectation, as was the case with Israel (1985), Chile (1975), Croatia (1994) and Yugoslavia (1993). Yugoslavia slashed nine zeros from the *dinar* during its redenomination.

The overall objective of redenomination in this sense is to ensure credibility (Mosley, 2003; International Monetary Fund, 2003). Enhanced credibility can improve government electoral fortunes, as citizens reward economic growth and macroeconomic discipline (Armijo, 1996; Stokes, 2002 in

Mosley, 2005); and it can improve a government's treatment as a borrower, as a location for private investment, and as a defender of an exchange rate in the eyes of global capital markets (Leblang, 2002; Jensen, 2005).

It should be noted however, that not all countries suffering from high inflation and/or are having very high local currency dollar ratios find it necessary to redenominate their currency. Some countries are very cautious about redenomination (Ishiekwene, 2007). For example, South Korea's *won* to a dollar is 932 since the beginning of this year, Hungary's *forint* is 216 and Japan's *yen* is 117, yet these countries deem it not appropriate to redenominate their currencies (Araki, 2001; Mosley, 2005).

Psychological effect, which creates sense of identity, is the second and one of the most common reasons for a country engaging in currency redenomination. According to Lead Capital Limited (2007), the *feel good effect* of such reconstruction in currency basically presumes that the perception of the local currency would be enhanced because people invariably begin to subconsciously relate currency redenomination to revaluation. Cohen (2004) posits that national currency not only facilitates economic transactions but affects citizens' identity and subsequently the legitimacy of the national government. Thus, from the social phenomenon perspective, money serves as a means of creating and cementing political identities, and bringing about psychological satisfaction.

Certain governments adopt redenomination strategies in order to improve their monetary sovereignty and control tendency for currency substitution. If people do not value their local currency, they begin to use foreign currency, particularly those with greater prestige. Aluko (2007) provides list of many African and non-African countries whose citizens almost lost confidence in their currencies. According to him, as at July 2007, a US dollar (\$1) exchanges 9270 *cedi* in Ghana, 9426 *rupia* in Indonesia, 9861 *franc/ariari* in Madagascar, 10184 *kip* in Lao and 15921 *dong* in Vietnam. Mosley (2005) further cites Turkey, Caballero (2002) cites Argentina and Federal Research Division of Romania (2006) cites Romania among the nations that adopt redenomination to save their currency from absolute neglect and restore some regard to it. In 2003, 1982, and 2003, one US dollar was equivalent to 1,500,890 *lira*, 180,000 *pesos ley* and 33,200 *leu* respectively. According to Central Bank of the Republic of Turkey

(2004), Turkey used to have a 20,000,000 single local currency bill; while Indonesia, Cambodia, Lebanon, Mozambique, Paraguay and Vietnam have 100,000 local currency units in circulation.

Another reason for redenomination, though not often cited is domestic politics. Mosley (2005) argues that the use of redenomination as a means of improving credibility is ultimately an account rooted in domestic politics. According to him, governments may want to keep inflation low because they want to be rewarded by voters, during election, for economic performance; impress international market to enable them borrow more cheaply and attract foreign investment that in turn will facilitate government spending and domestic economic growth. However, it should be pointed out that going by this reason advocated by Mosley in the light of the first intent will only hold water where voters through their genuine votes determine who rule them, hence the need for the assumption *ceteris paribus*.

It is clear from the above review that the decision to redenominate a national currency is influenced by both economic and political factors. What then are the benefits of currency redenomination?

A cursory look at the literature shows that currency redenomination has some benefits as well as costs and risks associated with it (Hausmann and Rigobon, 2002; International Monetary Funds, 2003; Central Bank of the Republic of Turkey, 2004; Zabuliene, 2005; Calomiris, 2006; Tarhan, 2006; Martinez, 2007; Ishiekwene, 2007). Redenomination leads to a more efficient local currency by knocking off some zeros; facilitates business transactions because it leads to the use of smaller units of money; leads to a more portable currency and a significant reduction in the dead weight of the money people carry and the associated risk, e.g. attack by robbers; reduces the phenomenon of money illusion that people suffer from when there are many zeros, which even tends to generate inflationary pressure; leads to greater confidence in the currency; can sometimes reduce inflationary tendencies in an economy if the underlying causes of chronic or hyperinflation and low valued local currency are resolved before the redenomination exercise and if the process is well managed; and enhances book-keeping and reduces the drudgery in transactions, record keeping and banking activities.

Lead Capital Limited (2007) further identifies developmental effect of redenomination. It posits that the government by reducing the denomination in its currency, would ordinarily introduce 'high valued' coins into its system. Such coins would help facilitate the introduction of vending machines, car parking meters and other more sophisticated payment systems which may hitherto have been inexistent.

The costs and risks of redenomination are also replete in the literature Tarhan (2006) groups the associated problems of redenomination into four: inflationary effects of rounding off prices (for example N5 = 1k); menu and administrative costs, which include changing prices in labels, changing laws/regulations, cost of printing new notes and minting new coins, cost of disposing of the old notes and coins, cost of public education and advertising the change to citizens especially in rural areas where there is little or no access to proper information channels such as electronic and print media and the literacy level is low, changing software and balance sheet/accounting record; psychological effects of lower income levels; and extra cost to the economy if multiple zeros are gone back to due to inflation.

Ishiekwene (2007) adds to the list the uncertainty and instability that is inherent in major changes in economic policies in most developing countries that could lead to increased speculation, capital flights, drop in foreign remittances, increased risk aversion, adoption of "wait-and-see" attitude by investors and increased sharp practices. According to Zabuliene (2005) however, some of these costs do not directly relate to the new currency. For example, unfit currency must be withdrawn from circulation and replenished with new printed money or information technology systems must be regularly updated. Therefore, the net cost effect is significantly lower than may be assumed.

Review of empirical studies on the outcome of currency redenomination especially in Latin America reveals that where it is employed but overall economic reform is ineffective or stabilisation policies are just underway, redenomination will not be panacea to economic problems (Araki, 2001; Caballero, 2002; International Monetary Fund, 2003; Calomiris 2006). This suggests why it should be implemented in the latter stages if not at the end of an economic stabilization package or reform. According to Ishiekwene (2007),

historical evidence suggests that redenomination had been very successful in an environment of macroeconomic stability, declining inflation, stable exchange rates, fiscal restraint and prudence and rational expectations of policy credibility.

Corroborating the above assertion, Mosley (2005) cites Angola, Argentina, Azerbaijan and Democratic Republic of the Congo among the countries that employed redenomination to address hyper-inflation but high rates of inflation persist afterward for want of adequate fiscal and monetary stabilisation policies. At the time of redenomination, inflation rate was 2672% (1995), 672% (1985), 912% (1992) and 1987% (1993) but roused to 4145% (1996), 3080% (1987-1989), 1129% (1993) and 2377% (1994) in these countries respectively. Further, Argentina's currency was 1100 to a dollar in 1962 and 3500 in 1969, and in 1980 and 1982, after redenomination in 1970 it was 18,000 and 180,000 respectively. Also, large ratios persist in Azerbaijani from 0.06 US cents to a *manat* in 1994 (before redenomination) to 0.02 cent in 2003 (after redenomination).

Similarly, Mosley (2003) and Mosley (2005) cite a number of researches conducted at local and cross-country levels suggesting that where redenomination is a purely technocratic exercise, it seems to have few real costs, beyond the short-run expense of printing new notes and advertising the change to citizens and financial markets.

By and large, studies of other countries' experience at currency redenomination have shown that it is not an approach that works in isolation of the real productive sector of the economy. The empirical studies of Caballero (2002), the International Monetary Fund (2003) and Calomiris (2006) are in agreement that no currency redenomination theory can transform the economy where mass unemployment persists, currency depreciates in value, imports exceed the exports, local industries are collapsing, and cost of production is prohibitive. However, it should be noted that studies on performance and effectiveness of currency redenomination are still inconclusive.

FINANCIAL AND ACCOUNTING IMPACT OF REDENOMINATION

Generally speaking, currency redenomination has no any direct impact on the economy. Since the value of the currency will remain absolutely constant, and purchasing power will remain the same, the real impact on the economy in micro

and macro terms will be zero: demand and supply of goods and services will not change; net investment, government spending, balance of payments and net exports will only experience *cosmetic changes* with no economic impact whatsoever; and on household consumption level, any possible effect on spending habit will be purely psychological as there will be no economic difference between the pre and post redenominated currency (Mosley, 2002; Zabulienė, 2005; Ncube, 2007; Lead Capital Limited, 2007). Accordingly, it is only redenomination of all economic values: prices of goods and services, financial assets and liabilities, salaries and social benefits, etc.

In monetary terms however, the situation is slightly different. Currency redenomination will reduce the physical monetary cash in circulation even though the real value will remain the same.

Similarly, the policy has no quantifiable effect on a country's capital market. The prices of all quoted stocks, both in the primary and secondary market, will simply be reduced to reflect the new structure. Since the nominal value of the money used to acquire those stocks will be adjusted, the total effect will be nil, thus making market capitalisation, turnover, traded values, and other market indicators have the same number of zeros removed from their pre-redenomination values. It is worth mentioning that there might be a slight drop in trading activity as investors might begin to trade cautiously and in fact, risk-averse might even want to dispose off shares as a result of the uncertainties on the outcome of a redenomination policy.

On the other hand, if well implemented and managed, redenomination may improve capital inflow. Foreign investors could begin to place more confidence in the general investment climate of the country and be encouraged to inflow more money into the capital market in anticipation of healthier returns in real terms (assuming a reduction in inflation rate and an improvement in macroeconomic policy). This is however a long term effect and is dependent on the government's ability to consolidate on the complimentary effect the strategy would have on its existing reforms and policies. The long run effect on the capital market should therefore be positive if all hands are on deck to ensure its success.

In the Accounting sphere, redenomination reduces time taken to input financial data and time spent by management to review it. It also reduces the cost

often incurred in customising standard packages that are purchased by businesses. Currently, many businesses report financial and accounting data in millions or billions of naira in order to gain some efficiency in managing the information.

Also most of the current accounting packages are developed in jurisdictions where values, at a maximum, tend to be in millions. The present situation in Nigeria where some organisations, especially banks record values of tens of billions of naira requires further customization of such packages to widen data fields. Thus, an effort to reduce the zeros and limit the extent of customization of standard packages will be of great benefit to businesses, as it will bring about simplification of financial data entry and also simplify the reporting of financial information and processing of business transactions. However, this benefit is to be compared with the costs of reconfiguration of business and accounting software, costs involved in changing business processes and procedures, and cost of printing new stationery (invoice, receipt books, cheque books, etc.).

From the perspective of effective date, redenomination raises two questions in relation to accounting records and reporting: what happens at the subsidiary ledger level – where individual accounting transactions are recorded? The second is: what happens at the general ledger level – where accounting transactions are summarized and reported in the form of financial statements and other reports? The conversion process will be particularly challenging for companies that process significant volumes of transactions and maintain many ledger accounts. Be that as it may, since redenomination simply involves knocking off some zeros; the accounting methods, principles, policies and standards already in use by organisations will not be breached.

REDENOMINATION OF THE NAIRA IN PERSPECTIVE

The CBN announced a 4-point agenda designed to make the Naira the “Reference Currency in Africa”, as part of the Financial System Strategy 2020 (FSS2020). The objectives of the suspended redenomination project include to restore the value of the Naira (in the short-term) close to what it was in 1985 before the commencement of the Structural Adjustment Programme (SAP) in 1986; to better anchor inflationary expectations; to strengthen public confidence in the Naira; to make for easier conversion to other currencies; to reverse tendency

for currency substitution; to eliminate higher denomination notes with lower value; to reduce the cost of production, distribution and processing of currency; and to promote the usage of coins and thus a more efficient pricing and payments system.

These objectives, as laudable as they are, raise a number of issues that need to be analysed in order to establish the merit or otherwise of the CBN proposal. A careful analysis of most of the objectives in the light of political economy parameters is therefore necessary.

To start with, redenomination of the naira to its pre-SAP units is not the same thing with restoration of its value. Theory has it that exchange rate is something that evolves through development of the microeconomic fundamentals of the economy such as the rate of growth of the economy and its involvement in international trade. Put simply, exchange rate is not determined by administrative fiat. To say that the naira will go back to its pre-1986 value through mere redenomination therefore is like a nightmare. Assuming it is possible, the question will be: what about the prices of commodities in pre-SAP era relative to post-redenomination era?

Redenomination can be used directly in the stabilisation process as part of an effort to change citizens' inflationary expectation, especially after achieving single-digit inflation rate. According to Mosley (2005), the rationale for using redenomination in this way is that the physical act of using large-denomination notes has an impact on agents' expectations. When a bag of rice costs N6000, consumers and firms are constantly reminded that prices increased dramatically in the past, and they continue to expect such increases in the future. When the highest banknote in circulation is N20, on the other hand, citizens may grow more confident that a return to high inflation is unlikely.

The problem with this logic however, is that it may assign too great role for the physical currency in the reduction of inflationary pressures at the wake of economic stabilisation, thereby resulting in a new currency with unaddressed inflation. In 1998 for example, the Russian government redenominated the *ruble* with three zeros removed from the currency with a view to assuring the public that Russia's economic crises were behind it; inflation was on the decline, falling from 875% in 1993, to 200% in 1995 and further, to 15%, in 1997. However, the

redenomination did not mark the end to the country's hard times, as annual inflation returned to 86% in 1999.

Experts pointed out that redenomination has little economic significance, beyond the one-time transition costs it imposes on countries, and in the absence of sound monetary reform, redenomination will not halt inflation or change individual's behaviour. This is why; looking at the impact of redenomination on credibility, adopting it at the end of a reform process is more likely to reassure investors and citizens. This analysis could be extended to the issues of strengthening public confidence in the naira and reversal of tendency for currency substitution.

Elimination of higher denomination notes with lower value is a good objective, except that it carries along with it some psychological effects. Imagine the psychological trauma of a civil servant that earns, in a pre-redenomination era, N50000 a month that will in post-redenomination era go home with N500. Economically, the poor stand to lose the more. For instance, the poor will pay more for a sachet of pure water that currently sell for N5.00 because the nominal unit of N5.00 which ought to be half a kobo is not accommodated by the proposed new coins whose lowest unit is 1k. Therefore, all consumables under N10 now will automatically attract higher price of 1k in a redenominated currency regime.

Reduction in the cost of production, distribution and processing of currency is one of the objectives of the CBN new naira reform. No doubt, Nigeria will make some savings in this regard especially when one considers the amount expended in printing currency. According to a report posted on www.newswatchngr.com in October 2005, foreign bank note printer De La Rue printed 120 million units of the new N1,000 note at the cost of about N939 million. The questions are: can we justify redenomination merely on the basis of printing cost saving? Would it be timely to embark on the new project now after spending billions of naira to print new currency in 2005 and 2007? We argue that reduction in the cost of printing Nigerian currency can be achieved without redenomination of the naira through other optional choices that include but not restricted to: a greater use of cheques; through transfer payments as done in electronic banking, and by using credit cards. Some banks in Nigeria charge extra

on small withdrawals to decongest bank halls and encourage the use of ATM cards.

Promoting the usage of coins is a good thing. The only problem is that redenomination and by extension decimalization could even create artificial inflation, particularly for low value commodities, which the poor might be mostly saddled with. For example, a N163 commodity in the present naira becoming N1.63 may suddenly be charged at new N2 if the coins which would need to be used for the new transactions are not well-accepted, as it appears to be the case with the coins currently in circulation.

It is obvious from the fore going that even though some of the objectives of the CBN suspended proposal are good, it takes more time to justify the policy than it appears to be. Accordingly, one of the critics of the proposed naira reform contends that it appears to the CBN governor, for the foreseeable future, Nigeria's rate of economic development is dependent on its monetary and price stability, and its monetary and price stability is in turn dependent on naira redenomination.

Before concluding whether Nigerians should support the new agenda or not, we test the Mosley's adopted hypotheses in the light of the above analysis hereunder. We present the hypotheses in italics and assess each to see if it applies to the Nigerian situation.

Hypothesis 1: Both authoritarian and democratic governments may have political reasons for redenomination. Democratic governments are likely to redenominate in response to high inflation. Authoritarian governments may redenominate even without high inflation, particularly in the presence of civil conflict.

Currently, Nigerian government is democratic and high or hyper-inflation is now a thing of the past. Since the proposed redenomination is neither a response to high inflation nor to a civil conflict, this hypothesis does not apply to Nigeria. More so, with the autonomy granted CBN in the 2007 CBN Act, the proposal cannot be political except if there is more to the obvious.

Hypothesis 2: Redenomination is more likely following a period of high inflation and a subsequent stabilization. A dramatic downward movement in inflation increases the probability of a redenomination. This is particularly likely in countries that are more open to international capital flows, that are under an IMF adjustment program, and that have politically independent central banks.

This hypothesis applies to Nigeria. From CBN reports, the average annual inflation rate had fallen from 13.5% in 2006 to a single digit of 6.87% by mid-2007. This had been preceded by an increase in the average annual inflation rate from 12.26% in 1996-2000 to 14.9% in 2001-2005. Between 1986 (when SAP was introduced) and 1999, the average rate of inflation was about 35% per annum with very high rates of 56% in 1987, 50.5% in 1988, 57.2 % in 1993, 57.0% in 1994 and 72.9% in 1995. The reduction shows significant achievement and if redenomination can be based on only this, then going by the hypothesis, redenomination is justified. It worth mentioning however that South Korea has maintained single digit inflation rate since 1982 after years of hyper-inflation, but *won*-dollar rate was four digits from 1997 to 2004 and is now 932 from 965 in 2006.

Hypothesis 3: *Redenomination is more likely immediately after an election (or with many years remaining until the next election), less likely immediately before an election, and more likely in more fractionalized political systems.*

This hypothesis is also true in the case of Nigeria. The new strategic agenda for the naira was announced on August 14, barely four months after the general election. If the announcement was made before election, it would have reduced the chances of the ruling party to declare itself winner in spite of mass rigging and abuse of electoral process. Also the Nigerian political system is factionalized with about 50 registered political parties before the April 2007 elections.

Hypothesis 4: *Redenomination is less likely, all else equal, when left-leaning parties are in office, and more likely when right-leaning politicians hold office.*

This hypothesis applies to Nigeria because the self-asserted ruling party is more right-leaning than the major opposition parties. It is very unlikely for any of the opposition parties to have considered redenomination of the naira as a priority economic policy given the situation on ground.

Hypothesis 5: *Redenomination is more likely in nations where it has been used in the past. The total past experiences with redenomination increases the hazard of its use.*

Nigeria has never redenominated its currency through removal of zeros, and even though it adopted decimal system on 1st January 1973, changing from Pound, Shillings and Pence to Naira and Kobo, the CBN refers this to as decimalisation. This hypothesis therefore does not apply here.

Hypothesis 6: *Redenomination is more likely, all else equal, where foreign currency substitution is more prevalent in the domestic economy. This is more likely in nations with high inflation, with high local currency/dollar ratios; and foreign currency substitution is more likely after 1989 (as financial globalization expands) than before.*

This is not true of Nigeria because the rate of foreign currency substitution is still relatively low; the country did not witness more than two-digit inflation rate even at the wake of SAP; and the local currency/dollar ratio of about 126 is relatively low in comparison to other countries that have redenominated their currencies.

Hypothesis 7: *Redenomination is a more likely response to economic problems in more heterogeneous societies, and in younger nation-states.*

The challenge of heterogeneity, building a common national identity, does not apply to Nigeria, even after civil war. Also, Nigeria has been an “independent nation” since 1960. Based on the foregoing, this hypothesis does not apply.

CONCLUSION AND SUGGESTIONS

Generally, currency redenomination is based on some happenings within a country. Most of the countries that embarked on the policy now and in the past have done so on the basis of poor macroeconomic performance, in particular hyper-inflation. The outcome of any redenomination depends on various fiscal and monetary policies aimed at stabilising the economy.

Redenomination in Nigeria is not completely a bad policy; it worth trying despite all the problems associated with it as discussed in this paper. Although on August 24, 2007, the Federal Government announced the suspension of the planned redenomination of the nation’s currency for lack of due process, we hope that the suspension will not mean the end of the proposed redenomination. The

strategy should be thoroughly studied, understood, accepted and embraced by the entire Nigerian populace.

To be effective however, it has to go beyond the psychological and portability effects; it has to be associated with broader macroeconomic and fiscal reforms. It should be complimented with strict and disciplined fiscal policy measures. Government should not rely solely on monetary policy in its attempt to attain economic growth and development. Focusing on inflation targeting should not mean there will be a neglect of other broader objectives of macroeconomic policy such as output growth (or increased productivity), export promotion, job creation and favourable balance of payments position.

Further, the government should not use it in isolation of other complimentary efforts of the government including increasing the size of the formal economy relative to the informal. Redenomination should be seen as a means to an end and not an end in itself. Therefore, there should be increased infrastructural development especially in the rural areas and a certain portion of government expenditure should be devoted towards uplifting the general standard of living.

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