Inflation and Public Debt Reversals in the West African Monetary Zone (WAMZ) Economies

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Abstract

The research focused on the causes of inflation and public debt reversal in the West African Monetary Zone (WAMZ) economies. Several factors influencing public debt reversal and inflation, including weak institutions, high government spending, influence from external shock and lack of proper revenue mobilization, were discussed. The impact of these factors on the WAMZ economies has also been examined. These countries suffer from high inflationary pressures, increasing borrowing costs and slow economic growth. Policies and other methods implemented by the WAMZ economies to address these challenges have also been evaluated. The last section of the research looks at the challenges these economies face in implementing the policy responses stipulated to address public debt reversals and inflation.

Keywords: Inflation, Public Debt Reversals, West African Monetary Zone and Economies

1.0 Introduction

The Covid 19 pandemic together with other economic and political factors led to inflation in both developed and developing countries with the developing countries being the most affected. Inflation refers to the increase in price of goods and services in an economy. In the WAMZ, inflation has been a persistent issue and was only further sparked by covid. As a result, the cost of living in these countries is high and there is reduced foreign investment. Over the years, these countries have suffered from high levels of public debt due to economic factors such as weak revenue mobilization and allocation and high government spending. Reducing public debt through
measures that can contain or reverse the situation while controlling the adverse effects of inflation is a crucial step for these economies if they have to develop at the same rate as others or even attain economic stability and growth. One such measure is the fiscal response by WAMZ economies meant to address the devastating effect of the pandemic on the health and economic front of the people, but the high-level public debt reduced the possibility for further fiscal support, which was a concern in respect of debt sustainability after the pandemic in the WAMZ countries.

2.0 Theoretical Framework

The West African Monetary Zone refers to a block of 6 countries in the West African region working towards a common currency and monetary goal (Ajibola et al 2019). The relationship between public debt reversals in the West African Monetary Zone and inflation can best be explained through the concept of fiscal dominance and the quantity theory of money, which stipulates that the price level in an economy is dependent on the amount of money in circulation. This implies that an increase in the supply of money (more money is in circulation) leads to a rise in price levels, resulting in inflation. A decrease in the supply of money leads to a decrease in price levels and, subsequently, deflation (Ozekhome and Hassan, 57-80). The fiscal dominance concept, on the other hand, is where the government's fiscal policies dominate the economy (Babalola and Abdurrauf, 150-159). This often happens when the government relies heavily on inflation to reduce the value of its debt. This situation often arises when a government cannot control its spending, forcing the central bank to print more money or keep interest rates low, causing inflation (Abubakar et al. 47-57). In Nigeria, for example, the central bank has had to accommodate government spending by printing more money due to high government spending on fuel subsidies
and the country’s defence (Ahmed et al. 485-506). This has, for years, contributed to inflation in the country.

3.0 Inflation and Public Debt in the WAMZ

The West African Monetary Zone (WAMZ) refers to a block of countries within the West of Africa working towards a common goal of economic integration in their region as well as monetary cooperation within the region (Englama et al., 61-94). The countries within the zone include Gambia, Ghana, Guinea, Liberia, Nigeria, and Sierra Leona, and. The Monetary Zone was formed in 2000 with leaders from the 6 countries signing a treaty to create a common monetary unit while promoting economic development within the region. The goal is for the countries to have a single currency and one central bank for the region (Okafor et al., 57-68).

Even with the treaty and intentions of economic development, the countries within the block have experienced significant inflation for years. High public debt levels have been a cause for concern for individual countries within the West African Monetary Zone, as is the case with many other developing countries (Jarju et al.). Public debt in these countries keeps rising due to uncontrolled government spending and the countries have a low ratio of public debt to GDP. High inflation has, for years, brought about challenges concerning economic growth, citizens' purchasing power, and investment. Some common factors contributing to inflation within these countries include weak fiscal and monetary policies, external economic shocks such as rising prices of oil, and high government spending, which in turn leads to high public debt (Oyelami et al., 69-84).
4.0 Causes of High Public Debt and Inflation in WAMZ Economies

All the countries within the block have government spending patterns that are unsustainable from the budgets within the country, forcing the countries to rely heavily on external debt and grants (Adeve et al. 105-118). In Nigeria, for example, the government spent over 2 trillion Naira on oil subsidies and defence for 2020. The amount spent on the two was twice what was allocated for health and education in the country for the year. Such spending often leads these governments to keep borrowing, increasing public debt (Tama and Habila). In 2020, Ghana spent over 2 billion dollars on the construction of infrastructure (a new oil refinery), a move that increased public spending and contributed directly to high debts for the country.

According to (Ada et al. 16-26) second cause of high inflation and high public debt for the economies is poor revenue mobilization and allocation. In Sierra Leone, tax revenue accounts for less than 10% of the country’s GDP as the government struggles to expand its tax base and improve tax administration. Such low levels of revenue collection, according to (Iliyasu et al., 1-10), are
attributed to poor policies around revenue and poor implementation of the already existing strategies. High government spending that is out of proportion to revenue is making the situation in the nation worse (Blommestein et al.). In Liberia, tax administration is often a challenge due to the fact that the informal sector in the country accounts for the largest portion of the economy. The government faces challenges in collecting taxes from the informal sector. This, coupled with the country’s complex and outdated tax code, makes it very difficult to enforce tax laws (Tarawalie et al., 178-186). As a result, the government loses revenue from the informal sector through tax evasion, which accounts for the largest part of the economy.

High public debt and inflation in the WAMZ economies are also closely associated with weak public financial management systems. Most countries in the zone have high levels of corruption, often leading to the loss of government resources. In Gambia, the government has for years been criticized for the misappropriation of public funds and lack of accountability and transparency in government spending and budgeting (Moseley et al., 5774-5779). In 2020, for example, the government was accused of misappropriating funds meant to relieve the country from the impact of covid 19.

The corruption level is not only in WAMZ countries but in franco phone west Africa including for example, Mali and Ivory Coast. Mali’s financial systems have been described as porous, with loopholes that lead to corruption and embezzlement of public funds (Moseley et al., 5774 -5779). In 2020, government officials were accused of misappropriating over 100 million dollars allocated to purchase military equipment. Once funds are misused, the country needs services and infrastructure, forcing the government to borrow more.
External debt burdens have, for years, pulled these countries down in economic growth. According to (Mosley et al.), Côte d'Ivoire's external debt accounts for over 40% of the country’s GDP. This huge external debt has put a burden on the economy of the country. In Senegal, over 20% of government revenue for 2019 went to servicing external debts. External debt for these countries has raised questions about their viability, especially since substantial borrowing is sometimes coupled by improper spending.

Economic shock, especially after the covid 19 pandemic, has also contributed largely to slow economic growth in these countries. The pandemic resulted in serious shortfalls in revenue for these countries and increasing spending needs that were not part of the government’s budget. In Nigeria, the pandemic’s effects led to a sharp drop in the price of oil, a commodity the country relies on heavily for revenue (Ezema, 11-16). Climate change is yet another economic shock that has impacted these countries economically. As a result of the changes in climate in these regions, the countries now experience unusual spans of drought, impacting agricultural activities adversely. Siddique et al., 874-894, stipulates that most of these countries heavily rely on agricultural production, and changes in rain pattern from climate change have led to food insecurity (Edo et al., 173-187). Governments in the zones have had to increase government spending on social safety net profits to shield the citizens from hunger. In most cases, this kind of spending is funded by debts (Meniago et al., 399-419).

The causes of inflation and public debt reversals in these countries are a multifaced problem that requires long-term solutions in terms of policies and implementation of these challenges and as indicated in the figure below, countries in the region experience inflation at different rates due to differences in internal and external economic factor. The formation of the
West African Monetary Zone is one such move by these countries to address the common problem of inflation and public debt reversals. Coordinated efforts and the comprehensive economic approach by the governments aim at improving governance, increasing revenue mobilization, improving resource allocation and having in place productive investments for the countries to reduce their borrowing.

**Figure 2: Annual Consumer Inflation Rate of West African Countries (Sasu, 2023)**

5.0 Impact of High Public Debt and Budget Deficits on the WAMZ Economies

According to (Senadza et al.), the impacts of high public debts and deficits on the WAMZ economies are adverse and hurt these economies both in the short and long run. One such impact of these problems is that governments often suffer from reduced fiscal space. This implies that
governments in these situations have reduced ability to finance public goods and services, as is the mandate of any government. This condition often affects the economy adversely and hurts the social welfare of the citizens. The implication is that goods and services that the government funds do not receive the required resources and are hence strained. Hospitals and schools, for example, end up with no proper resources such as staff and medicine. In the long run, the quality of services the public sector offers (health care and education) becomes questionable. As an example, Ghana has very high levels of debt, a situation that has forced the government to cut down spending on social services such as education and health care. As a result, the quality of these services has reduced greatly.

Secondly, high levels of external public debt often come at a cost. The implication is that increased borrowing leads to increased borrowing costs, and as a result, it becomes more expensive for the government to continue borrowing from international capital markets (Ibrahim and Zayyanu 01-15). According to (Moseley et al., 5774 -5779), Gambia has, over the years, suffered from high costs of borrowing resulting from uncontrollable levels of high public debt. Once a government cannot access funds internally and externally, it becomes very difficult for it to finance public goods, investments and services. This leads to a cycle of poor services and public goods in these countries, affecting the citizens' social welfare in the long run.

High levels of public debt often affect interest rates, especially for businesses and private investors (Mutenyo et al., 27-52). The implication is that with high borrowing debts come higher borrowing costs for both local and international investors. As a result, the attractiveness of a country to investors reduces. This, in turn, leads to reduced private investments and slow economic growth (Mwakalila and Enock, 123-135).
Lastly, these countries suffer from macroeconomic instability, which leads to currency depreciation, reduced economic growth and speeds up the vicious cycle of inflation (Agri et al.). Macroeconomic instability also creates an unconducive economic environment for businesses making it difficult for them to plan and invest as inflation keeps rising (Dey and Mohammad, 185-204). In the long run, the implication is slowed economic growth and more public debt.

6.0 Policy and Other Responses to Public Debt and Inflation in the WAMZ Economies

The West African Monetary Zone (WAMZ) has put in place various policies to address the challenges they face on inflation and public debt reversals. One such policy is the fiscal consolidation policy which involves reducing government spending while increasing revenue mobilization and resource allocation in a bid to reduce deficits and reduce public debt levels (Nwakoby et al. 2019). This approach helps reduce inflationary pressures on these countries and, at the same time, improves fiscal sustainability (Ceesay et al. 19-26). The implementation of this policy aims at ensuring economic growth and the improvement of social welfare for the citizens of the country.

These countries have also adopted a policy of monetary tightening which entails increasing interest rates and reducing the supply of money in an attempt to reduce inflationary pressures (Olusegun and Famoroti, 20-42). This, however, affects the cost of doing business in the countries and can only be effective in the short term as governments seek economic stability (Ndombi A, et al. 2021). The countries must understand the implication of very high-interest rates on local and international investors and the impact of such investments on the country's GDP (Chugunov et.al., 42. A balance must hence be attained in the short term to ensure the policy is effective and helps the business to manage inflation short term.
The second strategy these countries implement to address the challenges is debt restructuring. This entails re-negotiating the terms of an already existing debt with lenders to reduce costs associated with debts. The policy aims at reducing the burden of debt on economies and improving a country's fiscal position (Omojolaibi et al., 277-309). The disadvantage of this policy is that if not implemented correctly, it can adversely affect the costs of borrowing for the country in the future. These governments have also put in place some structural reforms to help improve the efficiency and competitiveness of their economies (Ayesy E, et al. 2021). One such approach is government improvement on transparency, reducing corruption, proper governance of public institutions and promoting economic development. This strategy helps countries address the underlying causes of public debt reversals and inflation while rippling to sustainable economic growth.

Other than mutual policies to address these challenges, the members have also put in place other measures at the local government, regional, and international levels. According to (Salameh, 262-267), governments in the WAMZ block are implementing fiscal consolidation efforts at the local government level to reduce government spending while increasing revenue mobilization. Other governments are working towards recognizing the impact of the private sector on economic development and promoting efforts to spur growth in the private sector while also making conditions for business suitable for foreign investors. Other governments are working towards improving their debt management practices through proper governance and transparency (Jackson and Emerson, 126-128).

Regional efforts to address these challenges include implementing a convergence program that aims to promote the stability of these economies while reducing the impact of external shock
on its members (Saka et al. 2017). The program entails having a common monetary policy coordination and exchange rate stability for all the members. At this level, the African Development Bank (ADB) has in place the African Domestic Bond Fund, which aims to support developing countries in Africa to develop capital markets and increase the availability of affordable long-term financing to African countries for purposes of development (Orji et al., 971-983).

At the international level, these countries seek external support from stable and experienced financial institutions such as the world bank and the International Monetary Fund. The support provided is in terms of technical assistance on ways and models to implement to address public debt reversals and inflation. Such technical support includes monetary policy coordination, structural reforms to implement as well as fiscal consolidation. By seeking support from such institutions, members of WAMZ receive technical support hence addressing their challenges professionally and in a manner that does not hurt the economy. At the same time, these countries have benefited from debt relief through the Highly Indebted Poor Countries (HIPC) initiative and the Multilateral Debt Relief Initiative (MDRI).

7.0 Challenges and Limitations to Implementing Policy Responses in the WAMZ Economies

Even with the policies put in place to address the challenges of public debt reversal and inflation in the WAMZ economies, there are still many challenges in implementing these policies and efforts. One such challenge is the limited monetary policy autonomy brought about by the fact that these economies are largely dependent on monetary policy decisions of the Central Bank of
West African States (BCEAO) (Egbuna and Ngozi). This bank is highly influenced by the region's politics, worsening the situation. With this, individual countries in the zone find it difficult to implement the stipulated monetary policies.

Secondly, these countries suffer from weak public institutions, which often have poor governance, limited transparency and accountability and very weak regulatory frameworks (Ikue et al., 426-436). The implication is that corruption in public institutions is rampant, making it very difficult to control government spending, undermining efforts to address public debt reversal and inflation challenges.

Political and economic challenges also affect the implementation of monetary and fiscal policies for these countries. The political class in these countries, according to (Law et al., 26-40), often has vested interests in public spending, making it very difficult for public institutions to operate autonomously and implement the set-out policies. With this challenge, these countries lack political will, limited stakeholder engagement and, in some instances, resistance to reforms from the political class who lose when public debt is managed.

9.0 Conclusion and Recommendation

The WAMZ economies have, over the years, faced challenges in relation to high public debt and inflation which has, in turn, had a ripple effect on economic growth and social welfare for these countries. The countries suffer greatly from inflationary pressures and the high cost of
borrowing. One major factor leading to these challenges is the high government spending in these countries, often caused by a lack of proper governance, accountability and transparency of public funds. With the current challenges, it has become essential for the economies to address the complex relationship between political, economic and social factors in relation to public debt reversal and inflation to achieve sustainable solutions. Such solutions require coordinated efforts and resources from all regional stakeholders, including individual governments, international organizations, civil societies and central banks.

To address these challenges, it is recommended that the WAMZ economies put in place policy responses that include structural reforms within individual countries, debt restructuring strategies, external support in terms of technical support, monetary tightening strategies and fiscal consolidation. Individual countries should also towards strengthening public institutions by promoting accountability and transparency and improving revenue mobilization through the improvement of tax laws and structures. Even with the policies and strategies in place, these countries still expect to find it challenging to implement the reforms due to political interference (lack of political will), lack of autonomy on monetary and fiscal policies and challenges in coordinating the efforts for the success of all member countries. These underlying issues must also be addressed to enhance success in economic growth.
10.0 References


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