The "Eco" Currency: A Boost or Bane for International Project Financing in West and Central Africa?

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I. Introduction

Amidst the dynamic economic landscape of West and Central Africa, currency reform has emerged as a driving force shaping the region's financial future.[1] International project financing is driving a significant amount of development in both the Economic and Monetary Community of Central Africa (EMCCA) and West African Economic and Monetary Union (WAEMU) zones, enabling a wide range of infrastructure projects, including "roads, airports, power plants, and mines."[2] However, the bankability of infrastructure projects that use international project finance (IPF) is impacted by the volatility and fluctuations in different currencies and exchange rates.[3]

Investment opportunities and developmental projects are offered by emerging markets in West and Central Africa, which are grappling with population growth, urbanization, and environmental challenges.[4] Unstable revenue streams and lack of international commitments to back investors hinder project attractiveness.[5] As Africa is projected to account for 58% of global population growth by 2050, understanding and pricing for these challenges is crucial for closing the infrastructure gap in the region to propel economic growth and continued development.[6]

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[1] *See* Ali Zafar, *CFA Franc Zone: Economic Development and the Post-COVID Recovery*, BROOKINGS (Aug. 5, 2021), https://www.brookings.edu/blog/africa-in-focus/2021/08/05/cfa-franc-zone-economic-development-and-the-post-covid-recovery/ [https://perma.cc/ZX5A-4ZZE].

[2] *See* Segun Faniran, *Project Finance in Africa: A New Investment Opportunity*, CONSTRUCT AFRICA (July 4, 2021), https://www.constructafrica.com/blog/project-finance-africa-new-investment-opportunity [https://perma.cc/VKV6-W34A]; *see also* Paule Biensan & Alain Chan Hon, *International Project Finance and Currency Reforms in West and Central Africa*, WHITE & CASE LLP (Sept. 17, 2020), https://www.whitecase.com/insight-our-thinking/international-project-finance-and-currency-reforms-west-and-central-africa [https://perma.cc/VKV6-W34A] ("Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo belong to the WAEMU, while Cameroon, Central African Republic, Chad, Republic of Congo, Equatorial Guinea and Gabon are members of the EMCCA.").

[3] *See* Esawar Prasad & Vera Songwe, *Monetary Meld: A Currency Union Encompassing All of West Africa Promises Benefits but Faces a Multitude of Obstacles*, IMF (June 16, 2021), https://www.imf.org/external/pubs/ft/fandd/2021/06/future-of-west-africa-currency-union-prasad-songwe.htm; *see also International Project Finance*, ESFC INVESTMENT GROUP https://esfccompany.com/en/articles/project-finance/international-project-finance-pf-funding-model/ [https://perma.cc/JCJ9-8X6H] ("According to the Basel Committee on Banking Supervision, project finance (PF) is a form of financing the construction of capital facilities based on debt repayment through cash flows generated by the facility. . . . International project finance refers to the cross-border method of realizing capital intensive investments through a legally and financially independent project company (SPV).").

[4] *See* Dominic Spacie, *Project Financing in Emerging Markets: Four Pertinent Issues That Can Affect the Success of a Project*, DENTONS (May 7, 2020), https://www.dentons.com/en/insights/articles/2020/may/7/project-financing-in-emerging-markets-four-pertinent-issues-that-can-affect-the-success-of-a-project [https://perma.cc/3N6E-SKHQ].

[5] *See id.*

[6] *See id.*

Therefore, one possible solution is to move forward with implementing a unified currency known as the "Eco."[7] This currency reform could significantly impact key aspects of international project financings in the region, including project costs, financing structures, and foreign exchange risk management.[8] This essay aims to briefly describe the proposed reform for establishing a single currency, Eco, in West and Central Africa and examine how this reform may affect various aspects of international project financings for infrastructure projects.

II. Background

The member states of both EMCCA and WAEMU belong to Organization for Harmonization of Business Law (OHADA), which aims to harmonize business law in Africa to secure access to legal and judicial resources for its investors.[9] This is vital for complex legal structures and financing arrangements related to IPF. Many OHADA member states focus on implementing the common currency, Eco, which is intended to replace the CFA franc.[10]

The proposal for the Eco currency is to have a monetary instrument that is backed by the member states' reserves, which would help stabilize the currency and make it less vulnerable to external shocks.[11] Historically, the CFA franc has been used in West and Central Africa and is currently pegged to the Euro at a fixed exchange rate backed by the French Treasury, creating a link between these currencies.[12] Thus, the depreciation of the Euro would also lead to a depreciation of the CFA franc, potentially hindering West African countries reliant on IPF.[13]

However, the Eco will be pegged to the Euro, but member states will not need to keep 50% of their reserves in the French Treasury,[14] promoting economic independence and reducing reliance on France and the European Union, which has faced criticism.[15]

III. Benefits of Implementing the ECO Currency

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[7] *See* Louise Dewast, *West Africa's Eco: What Difference Would a Single Currency Make?*, BBC (July 6, 2019), https://www.bbc.com/news/world-africa-48882030 [https://perma.cc/PD2D-L97K].
[8] *See* Biensan & Hon, *supra* note 2.
[9] *See General Overview*, OHADA, https://www.ohada.org/en/general-overview/ [https://perma.cc/L86N-6MS3].
[10] *See* Aloysius Uche Ordu, *An Evaluation of the Single Currency Agenda in the ECOWAS Region*, BROOKINGS (Sept. 24, 2019), https://www.brookings.edu/blog/africa-in-focus/2019/09/24/an-evaluation-of-the-single-currency-agenda-in-the-ecowas-region/ [https://perma.cc/8L9H-N2H5]. Nine of the fifteen ECOWAS states are members of OHADA. *Compare General Overview*, *supra* note 9, *with International Project Finance*, *supra* note 3.
[11] *See id.*
[12] *See* Adam Hayes, *CFA Franc Definition,* INVESTOPEDIA, https://www.investopedia.com/terms/c/cfa-franc.asp [https://perma.cc/AV7Y-GA54].
[13] *See* Landry Signé, *How the France-Backed African CFA Franc Works as an Enabler and Barrier to Development*, BROOKINGS (Dec. 7, 2019), https://www.brookings.edu/opinions/how-the-france-backed-african-cfa-franc-works-as-an-enabler-and-barrier-to-development/ [https://perma.cc/T7QL-FW9V].
[14] *See* Mandia Xuba, *The Eco-Currency: A New Chapter for West Africa*, FUTURE AFRICA FORUM (Jan. 14, 2021), https://futureafricaforum.org/the-eco-currency-a-new-chapter-for-west-africa/ [https://perma.cc/AFK5-WZNQ]
[15] *See* Signé, *supra* note 13.

Implementing a common currency—Eco—could benefit OHADA member states economically by preventing currency fluctuations, mitigating foreign exchange risk, and promoting investment through greater monetary stability and common monetary policy.[16] Consequently, this would enhance the member states' ability to secure financing for infrastructure projects as it would ease debt servicing and improve their credit ratings.[17] Harmonized financial regulations would improve transparency, member states' credit ratings, and reduce risks, making financing for development initiatives easier.[18]

Moreover, a strong or improved economy can increase a country's credit rating, lower borrowing costs, and attract more investment for infrastructure projects via international project finance.[19] It can also reduce risks for investors and lenders by indicating a stable political environment and signaling a commitment to regional economic integration and reduce transaction costs associated with currency exchange. A stable and unified currency can further facilitate member states' access to the international capital market—as this reduces the risks associated with investing in multiple currencies that may fluctuate and introduce volatility to the cost and return on investment for such projects.[20]

IV. Costs of Implementing the ECO Currency and Proposed Solutions

Implementing Eco in the OHADA region has both advantages and drawbacks. It may increase project costs due to currency fluctuations and exchange rates, making financing difficult for international investors, especially those with tight profit margins, as the cost of importing equipment and materials for a project may increase.[21] Moreover, it would limit member countries' monetary policy autonomy, reducing their ability to respond to economic shocks and potentially exacerbating their effects.[22] Consequently, a weak economy can negatively impact a country's credit rating, making it more difficult and expensive to secure financing for infrastructure projects and deterring foreign investment and government spending.[23] Additionally, adopting Eco may lead to more financing through local currency to mitigate foreign exchange risk, but this could increase inflation, devaluation risk, and reliance on financial instruments such as currency swaps and options.[24]

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[16] *See* Prasad & Songwe, *supra* note 3.
[17] *See* Nora Chirikure et al., *How Are the 'Big Three' Rating Agencies Impacting African Countries?*, AFRICA POL'Y RSCH. INST. (Apr. 19, 2022), https://afripoli.org/how-are-the-big-three-rating-agencies-impacting-african-countries-54 [https://perma.cc/5685-4KFX].
[18] *See* Xuba, *supra* note 14.
[19] *See* Girum Abate et al., *Improving Economic Management Brings Many Benefits – Among Them Lower Sovereign Financing Costs*, WORLDBANK BLOG (June 22, 2022), https://blogs.worldbank.org/developmenttalk/improving-economic-management-brings-many-benefits-among-them-measurably-lower [https://perma.cc/RW7W-W48E].
[20] *See id.*
[21] *See* Prasad & Songwe, *supra* note 3.
[22] *See* Xuba, *supra* note 14.
[23] *See id.*
[24] *See* Chris Wellisz, *Digital Journeys: Africa - Freeing Foreign Exchange*, IMF: FIN. & DEV. 46, 47 (Sept. 2022), https://www.imf.org/en/Publications/fandd/issues/2022/09/Digital-Journeys-Africa-freeing-foreign-exchange-wellisz
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Introducing a common currency incurs substantial adjustment and implementation costs, affecting banking systems, tax structures, and financial regulations, which may have short-term adverse impacts on the region's economies.[25] This poses particular challenges for smaller member states with limited resources and may hinder infrastructure project implementation.[26]

A common currency may cause unequal distribution of benefits, creating tension and pressuring countries to leave the system due to varying economic conditions and needs among member countries.[27]

V. Conclusion

While it is important to acknowledge the potential drawbacks, it is imperative to undertake reforms for improving economic development among countries in OHADA. The decision to implement a common currency will depend on various factors, including economic and political conditions and the willingness of member countries to collaborate towards a shared objective. Nevertheless, exploring alternative solutions is still possible. Trade and financial arrangements are available to address economic and political issues without the need for a common currency.[28] Digital platforms, like the Pan African Payment and Settlement System, can enhance economic relations by enabling transactions to be conducted in local currencies and reducing dependence on hard currencies.[29] The Association of South East Asian Nations' (ASEAN) success in boosting their economies through structural reforms and free trade agreements shows that a common currency may not be necessary.[30]

[25] *See* Teniola T. Tayo, *Economics Alone Isn't Holding Back West Africa's Eco*, ISS AFRICA (Nov. 20, 2020), https://issafrica.org/iss-today/economics-alone-isnt-holding-back-west-africas-eco ("Mixed messages about a common currency have created policy uncertainty, hampering the ability of central banks to plan.").
[26] *See id.*
[27] *Id.*
[28] *See id.*
[29] *See id.*
[30] *See* Masahiro Kawai & Kanda Naknoi, *ASEAN Economic Integration Through Trade and Foreign Direct Investment: Long-Term Challenges* 3, 10 (Asian Dev. Bank Inst., Working Paper No. 545, 2015), https://www.adb.org/sites/default/files/publication/174835/adbi-wp545.pdf.