New Central Banks*

Sixteen new central banks have opened their doors since the beginning of 1959—the Central Bank of the States of Equatorial Africa and of Cameroon, the Central Bank of the States of West Africa, the Bank of Morocco, and the Central Bank of Nigeria in 1959; the Bank of Sudan, the Bank of the Republic of Guinea, and the Somali National Bank in 1960; the Bank of Jamaica, the Malagasy Bank of Issue, and the Bank of the Republic of Mali in 1962; the Central Bank of Algeria and the Central Bank of Cyprus in 1963; the Bank of Lebanon, the National Bank of Rwanda, the Bank of the Kingdom of Burundi, and the National Bank of the Congo (Leopoldville) in 1964. The central banks of Morocco, Nigeria, Sudan, and Guinea were described in a previous article in this *Review*;[1] the other twelve new central banks will be discussed here.[2]

The Central Bank of the States of Equatorial Africa and of Cameroon serves the newly independent states of Cameroon, the Central African Republic, Chad, Congo (Brazzaville), and Gabon. (This bank will be referred to as the Equatorial African central bank.) The Central Bank of the States of West Africa serves Dahomey, Ivory Coast, Mauritania, Niger, Senegal, Togo, and Upper Volta. (This bank, which will here be termed West African central bank, also served Mali until 1962.) Both of these institutions were organized under French auspices before the independence of the countries concerned. After becoming independent in 1960-61, these countries signed agreements with France (during 1960-62) under which all (except Mali) have continued to use the facilities of the existing central banks, whose organization and powers have been considerably modified to conform to the changed situation.

All but two of the countries served by the twelve new central banks had a monetary authority or currency board prior to the establishment of the new banks; the exceptions were the Malagasy Republic and Lebanon, where the note-issuing privilege had in each case been held by a commercial bank. While all the new central banks retain some of the attributes of the institutions they replace, they have generally been given a wide variety of additional monetary control powers.

The countries served by the new central banks vary considerably with respect to the degree of their financial and economic development. In some of the new states many economic transactions take place outside the monetary sphere, while in others such as Lebanon and Jamaica the banking systems are highly developed. The share of currency in the total money supply—a rough inverse measure of the use of banks in a country—varies from roughly 30 per cent in Lebanon and Jamaica to around 40 per cent in Cyprus and Senegal, 50 per cent in Somalia, and reaches about 65 per cent in Mali and Upper Volta. (The United States figure is about 20 per cent.)[3] There is also considerable variation in the degree to which financial institutions other than commercial banks have taken

* Dorothy B. Christelow had primary responsibility for the preparation of this article.

[1] See "International Developments", this *Review*, October 1960, pp. 181-83. The article also treated the Bank of Ghana, established in 1957, and the Central Bank of Malaya and the Central Bank of Tunisia, established in 1958.

[2] Another group of new central banks—not here discussed—will begin operations in the near future. These include central banks for Sierra Leone, Jordan, and Trinidad and Tobago. Furthermore, with the coming into being of the Federation of Malaysia in 1963, the Central Bank of Malaya became the Central Bank of Malaysia, with responsibility for the entire new country. Conversely, the breakup of the Federation of Rhodesia and Nyasaland into three countries will lead to the emergence of three separate central banks to replace the Bank of Rhodesia and Nyasaland. One of these, the Reserve Bank of Rhodesia (for Southern Rhodesia), has already opened its doors. While its powers and functions resemble those of the predecessor institution in most respects, it has been given the added power to require banks to maintain cash reserves against advances rather than against deposits.

In another group of countries—including Ethiopia, Iceland, Iran, Nicaragua, and the United Arab Republic—where the central banks had exercised both central banking and commercial banking functions, these institutions have in recent years been converted into central banks proper and their commercial banking operations transferred to existing or newly established commercial banks. These central bank reforms and conversions are also outside the scope of this article.

[3] The uniform definition of the money supply used for this comparison is that of the International Monetary Fund in its *International Financial Statistics:* currency outside banks, demand deposits, post office checking deposits, and private-sector deposits with the central bank where these exist; government deposits are excluded.

root. On the other hand, almost all the countries concerned display certain common characteristics: they are notably dependent on international trade; foreign capital has played or is expected to play a considerable role in their economic development; and foreign commercial banks are a major element in their banking systems.

The objectives of the new central banks as set out in their statutes are to assure the external and internal stability of the currency and to foster a monetary environment conducive to economic development. To this end, all the central banks are given the exclusive right of note issue, the obligation to act as fiscal agent and banker for the government, the power to buy and sell gold and foreign exchange, and the authority to discount, purchase, and sell specified types of financial obligations. In addition, most of the new banks have at least some of the following powers of control and supervision over commercial banks: to establish minimum cash reserve requirements, to set limits on lending and deposit rates, to prescribe the asset distribution and the total volume of credit outstanding, to examine the books and to require statistical reports, and to set minimum capital requirements.

CENTRAL BANK-GOVERNMENT RELATIONS

All the new banks are owned by the respective governments (except that the French government still holds all the capital of the Equatorial African central bank and half the capital of the Malagasy bank). In most cases, the presiding officer and the boards of management are appointed by the respective governments for a fixed period and are subject to reappointment. The exceptions are the three central banks whose member countries—all former French colonies—belong to the African Financial Community. The West African central bank's administrative council includes a minority appointed by the French government, and its presidency rotates every two years among council members representing the member states. Half the council members of the Malagasy Bank of Issue are appointed by France, and the president is chosen by the council, subject to the approval of the governments of the Malagasy Republic and France. The French government also appoints one half the members of the governing council of the Equatorial African central bank and, in addition, the President of the French Republic appoints the president of that institution.

Many of the new central bank statutes include further provisions to assure the harmonization of central bank action with the government's general economic policy. Some statutes provide that government officials or their representatives are to be members of the central bank's policy-making body. In Lebanon, two high government officials are minority members of the central bank's governing board; in Algeria, the law is sufficiently flexible to allow the chief of state to appoint government officials to a minority or majority position on the governing board. In Mali, five of the ten-member governing board represent government departments and two represent the national assembly. Other statutes provide for government approval or supervision of certain aspects of central banking. In Cyprus approval by the finance minister is required, if commercial bank reserve requirements are to be raised above a certain level. In Jamaica, the finance minister may "from time to time after consultation with the governor give to the bank in writing such directions of a general nature as appear to the minister to be necessary in the public interest". In Somalia, a committee consisting of the prime minister and key cabinet members is designated to supervise the operations of the central bank. In Burundi, major policy decisions of the central bank must be approved by the finance minister. In the Congo, a representative of the ministry of finance attends meetings, but is not a member, of the bank's governing board.

At the same time, a majority of the statutes limit central bank financing of their governments; the limitations typically apply to direct financing (i.e., through short-term advances or direct purchases of securities) and to indirect financing (i.e., through open market purchases or discounting of government securities offered by banks or others). Algeria, the West African countries, and Malagasy all limit the total volume of government indebtedness that may be held by the central banks to a specified proportion (varying from 10 per cent to 15 per cent) of ordinary government revenues during the previous fiscal year. In the Congo, direct and indirect advances may each equal 20 per cent of average government receipts over a past three-year period. Cyprus and Jamaica set more complex limits. Thus, in Cyprus the government's total direct and indirect indebtedness to the central bank may amount to 20 per cent of annual revenues plus 6 per cent of the bank's sight liabilities plus the government securities the bank took over from a note security fund. In Jamaica, in addition to central bank short-term advances up to 15 per cent of annual government revenue, 50 per cent of the assets backing the currency may be in securities of the Jamaican government; moreover, the bank may hold government securities in amounts up to seven times the bank's capital (which itself may be increased by the bank's board of governors with approval of the Jamaican House of Representatives). The Burundi bank's limit is an absolute amount. The Somali National Bank is limited only with respect to direct short-term advances to the government, while the Bank of Lebanon and the National Bank of Rwanda are subject to limits that may be exceeded in circumstances of "exceptional gravity". The remaining two central banks (namely, the Bank of the Republic of Mali and the Equatorial African central bank) are not limited as to the total government indebtedness they may hold.

DEVELOPMENT OF THE FINANCIAL SECTOR

All the new central banks have been given a general mandate for promoting economic development—often including special responsibilities for developing financial institutions, credit instruments, and domestic money markets. For this reason, these banks tend to have at their disposal legal powers going beyond the traditional tools of rediscounting and open market operations, which themselves can of course also be used to promote certain types of credit instruments and to encourage specific types of loan transactions by increasing the liquidity of the instruments involved.

Thus, central bank powers to prescribe the distribution of assets in commercial bank portfolios may be of considerable importance: the Bank of Jamaica has the power to prescribe a minimum ratio of domestic assets to total commercial bank deposit liabilities; the central banks of Cyprus and the Congo have the broader power to prescribe the purposes for which commercial bank advances and investments may be made; and the Rwanda central bank is empowered to enter into agreements with commercial banks in this same regard.

Furthermore, where the existing financial sector is relatively small, it may be deemed advisable—indeed necessary—for the central bank to be able to deal directly with the borrowing and depositing public. This power has been a feature of the early years of many established central banks. Limited direct central bank contact with the borrowing public through discounting and advances on government securities is provided by all the statutes discussed here, except those for Lebanon and Cyprus. And the Algerian and West African central banks may accept noninterest-bearing deposits from the public in certain cases, although such deposits have in fact been small.

Broader powers have been given the central banks of Jamaica, Somalia, Mali, and Burundi—namely to discount for and make advances to, as well as to accept deposits from, nonfinancial customers. The Bank of Jamaica, to be sure, has indicated its intention to abstain from such commercial banking operations. But, in Somalia, the central bank's claims on the private sector are about two-thirds as large as similar commercial bank claims, while its rediscounts for commercial banks are negligible. The Mali central bank's claims on private borrowers are approximately four times as large as those of commercial banks, and it also discounts heavily for the commercial banks. In many countries where the central bank has not been given such broad powers to deal directly with the public, as well as in some of the countries where the central bank has such powers, separate government development banks tend to perform some of the same functions.

The specific types of paper eligible for discounting, rediscounting, loan collateral, or outright purchase are in themselves of considerable importance in the process of financial development, as already noted. In addition to discounts of and loans against government securities, all the central banks here discussed may discount or loan against first-class paper drawn to finance trade, industry, and agriculture. The maximum allowable maturity of the underlying paper is 90 days in Lebanon, but more usual limits range from 180 days to one year.

A number of statutes also provide for longer term commitments on the part of central banks to assist in the growth of negotiable securities markets and to finance economic development. Following the French tradition, the Central Bank of Algeria, the Equatorial African and West African central banks, and the Malagasy bank may extend credit to commercial banks and other financial institutions for as long as five years in order to finance industrial exports, housing, or other projects included in national development plans. Cyprus permits central bank investment in first-class, fixed-maturity, fixed-interest securities in amounts up to 5 per cent of the bank's liabilities (exclusive of government deposits). The central bank of Mali has taken over the functions of the government-owned Popular Bank of Mali for Development. The Bank of Jamaica may, with the approval of the finance minister, buy and sell shares of companies specially authorized by the government to develop a local money or securities market or to improve "the financial machinery for financing of economic development". The Burundi bank may commit amounts equal to the sum of its capital, reserves, and amortization accounts to the purchase of long-term obligations issued or guaranteed by the government and, with agreement of two thirds of the bank's governing board, of long-term obligations of other borrowers and shares in newly organized government-sponsored financial institutions.

CREDIT CONTROL

The new central bank statutes suggest the existence of several distinct although overlapping approaches to the problem of general monetary control. In those countries that were formerly French colonies, primary reliance is placed on variation in central bank credit to banks and other financial institutions, mainly through changes in the discount rate and through variable ceilings on the over-all volume of such credit. The West African central bank and the Equatorial African central bank determine the discount rate and the credit ceilings for each state, while national monetary committees are responsible for the distribution of credit among the commercial banks and other eligible credit institutions in the individual states. It is therefore possible for these central banks to pursue differential credit policies in the individual member states, as circumstances may require, although the freedom of payments among these countries would tend to complicate such differential policies and, in fact, makes a concerted economic and monetary policy highly desirable. In all these former French colonies, commercial bank reliance on central bank credit is very heavy: the central banks tend to refinance from 30 per cent to 60 per cent of bank credit outstanding, there being of course considerable variation from country to country and over time. Changes in the commercial banks' external indebtedness to their French head offices or parent banks or to other French banks can, to be sure, offset changes in central bank credit to some limited extent. The statute creating the Burundi central bank, which commenced operations very recently, suggests a similar approach to credit control, although the concept of setting ceilings on the availability of central bank credit does not appear in the Burundi statute.

The new central banks in Lebanon, Somalia, Jamaica, Cyprus, Rwanda, and the Congo rely for purposes of credit control largely on a combination of variations in commercial bank reserve requirements, the rediscount mechanism, and open market operations, plus a varying array of direct controls. One reason for the addition of direct controls to the traditional central bank arsenal in less developed money markets is usually the problem of dealing with potentially large inflows of funds from abroad. These inflows can be offset by changes in required reserve ratios only within the limits set by law, while large central bank sales of commercial paper or government securities might prove unduly disruptive or altogether impossible in thin financial markets.

The statutes of five of the six central banks discussed in the foregoing paragraph specify the range or upper limit of permissible variations in reserve ratios. In Jamaica, the ratio may be varied from 5 per cent to 15 per cent of deposit liabilities. The upper limit in Cyprus, Rwanda, and the Congo is 20 per cent of deposit liabilities, with an additional 10 percentage points permitted in Cyprus in exceptional circumstances. In Lebanon, the maximum required reserve ratio is 25 per cent for demand deposits and 15 per cent for time deposits. As for direct controls, the Bank of Jamaica may set limits both upon the over-all volume of commercial bank credit outstanding and upon specific types of credit; the Cyprus and the Congo banks have the same power with respect to commercial banks and other designated financial institutions; and the Rwanda bank may accomplish the same end through agreements with commercial banks and other financial institutions. The Lebanon bank may set variable liquidity ratios and other asset-liability relationships for commercial banks and other financial institutions. The central banks of Cyprus and the Congo also may set commercial bank lending and deposit rates.

Central banks which make substantial use of their powers to deal with the nonbank public—those in Somalia, Mali, and Burundi—possess an additional instrument of monetary control. By altering the volume of central bank credit to the nonbank public, these banks have a direct means of influencing the liquidity of the nonbank sector as well as that of the bank sector of the economy.

INTERNATIONAL FINANCIAL RELATIONS

Many of the statutes specify the form in which the central banks' international reserves are to be held, as well as the minimum level to which these reserves may fall. These provisions are, of course, influenced by the special relation to a major currency area a country may have.

Jamaica and Cyprus are members of the sterling area and as such have generally tended to hold the bulk of their reserves in short-term sterling assets in London. Funds are freely transferable within the sterling area, while the sterling balances held by the area's monetary authorities are convertible into other currencies in accordance with each country's exchange regulations and general sterling-area policy. In Jamaica, the central bank law requires that reserves be held in the form of gold, sterling notes and coin, balances or money at call with banks in the United Kingdom, United Kingdom Treasury bills, or other securities issued or guaranteed by a government or territory of the British Commonwealth. The provisions in the central bank statute of Cyprus specify only that the bank's foreign assets are to consist of gold and such foreign exchange and foreign securities as the governing board shall from time to time designate. The statutory minimum level of foreign exchange reserves at the Jamaica central bank is stated in terms of its relation to the currency circulation. This reflects the practice of the former British-administered currency board which this new bank succeeds; but, whereas the currency board generally aimed at maintaining 100 per cent sterling cover for currency outstanding, the new central bank statute provides for 50 per cent cover in gold or eligible foreign exchange assets. In Cyprus, reserves must be 30 per cent of currency and central bank sight liabilities. These two statutes make no specific provision as to how and when the banks are to act to maintain these ratios.

Algeria, Mali, the countries of Equatorial and West Africa, and the Malagasy Republic are members of the French franc zone. With some exceptions, zone members hold most of their foreign exchange reserves in the form of French franc liquid assets. Algeria and Mali, whose central bank laws do not specify the form or size of their international reserves, may also hold gold and nonfranc foreign exchange. The countries served by the Equatorial African, West African, and Malagasy central banks, however, maintain their foreign exchange reserves in the form of "operations accounts" at the French Treasury, or they may hold French government securities. These members of the African Financial Community (CFA) have in exchange been given the guarantee of unlimited conversion of CFA currencies into French francs. The technical arrangement involves automatic overdraft facilities when a country's operations account shows a deficit. These accounts may be debited by CFA central banks for the purchase of nonfranc currencies by residents of CFA countries in conformance with these countries' exchange regulations, which generally resemble those of France.

French willingness to assure convertibility of CFA francs is related to the French voice in the management of the three above-named banks and to certain additional safeguards. For example, the statute for the West African central bank provides that an increase in the bank's discount rate and a reduction in rediscount ceilings must be considered when foreign exchange reserves remain for thirty days below 20 per cent of sight liabilities (currency and deposits combined); if the ratio falls below 10 per cent for the same period of time, these measures must be adopted immediately. Also, an agreement between the West African Monetary Union (the group of states served by the West African central bank) and the French Treasury provides that, if the operations account of the area as a whole is in debit for sixty consecutive days, the central bank's discount rate must be raised by 1 percentage point. For an individual country with a net debtor position in the operations account, the discount ceiling must be reduced by 20 per cent, while for a country whose operations-account credit amounts to less than 15 per cent of its currency outstanding, the ceiling is to be reduced by 10 per cent.[4]

The remaining five new banks—in Lebanon, Somalia, the Congo, Rwanda, and Burundi—are members of neither the sterling area nor the French franc zone, although the three last-named countries were members of the Belgian monetary area until 1960. The Lebanon bank is required to hold gold and foreign exchange reserves equal to 30 per cent of its currency and sight liabilities or 50 per cent of the currency issue, whichever is larger. The Somali bank must hold a reserve of gold and convertible currencies equal to 100 per cent of currency outstanding. Neither statute provides for special action in the event these ratios are not maintained. The Congo bank must maintain gold and foreign exchange reserves equal to 40 per cent of currency and sight liabilities, but this requirement may be suspended by the governing board of the bank for the first five years of the bank's operations. The Rwanda bank is to hold foreign exchange reserves in the form of gold, accounts with foreign central banks, or in readily marketable securities, but is under no obligation to maintain them at any specific level. The Burundi statute does not mention international reserves, although the bank has sufficient powers to acquire and maintain foreign exchange reserves.

CONCLUDING REMARKS

The broadening of the financial structure as a prerequisite for sustained economic development is one of the prime tasks of virtually all these new central banks. Such a broadening must in a number of cases necessarily accompany the effective exercise of central bank credit control. The tools given these institutions will, therefore, have to be used not only to encourage price and balance-of-payments stability, but also to promote the growth of sound and diversified financial institutions and to foster confidence in money and banks—efforts which will in turn aid economic growth in general. It may thus be expected that all the banks here discussed will gradually broaden their potential for judicious and flexible use of central banking instruments.

[4] It will be understood that ties concerning central banking are only one aspect of the continuing financial cooperation between France and her former African colonies. Thus, besides grants, the French also make loans, through the Caisse Centrale de Coopération Économique (CCCE), to CFA-area development banks, public corporations, and private enterprise. The CCCE is financed by French Treasury advances. It also serves as note-issuing authority for Saint-Pierre-et-Miquelon and in this connection maintains an operations account at the French Treasury.