Macroeconomic Convergence: What does it mean exactly, why is it needed, and what are the priorities?

Joint Conference on “Regional Integration in the EAC: Making the Most of the Common Market on the Road to a Monetary Union”

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Outline

- What does convergence mean?
- Why does it matter?
- Is the EAC different from the euro area?
- How is the EAC doing?
- The road ahead
The meaning of convergence

- Commonly refers to economic catch-up (real convergence)
- Roots in the OCA literature (Mundell, etc)
- Application in the euro area: nominal convergence criteria
Why does it matter?

- OCA theory: reduction in scope for asymmetric shocks:
  - synchronization of business cycles
  - trade integration
  - labor mobility

- EMU Maastricht criteria are different:
  - Deficit and debt limits
  - Inflation limits
  - Exchange rate stability; LT interest rate convergence

- Why this difference?
Is the EAC different from the euro area?

- Different degree of trade integration
- Financial depth and integration
- Labor mobility?
- Do LICs require less strong convergence?
How is the EAC doing?

- Inflation: OK
- Debt: OK
- Deficits: too high
- Reserves: more needed
Inflation: converging and below the ceiling

- **Headline Inflation**
  - Kenya
  - Burundi
  - Uganda
  - Tanzania
  - Rwanda
  - Ceiling

- **Core Inflation**
  - Tanzania
  - Burundi
  - Uganda
  - Kenya
  - Rwanda
  - Ceiling

Graphs showing inflation rates from 2011 to 2015 for various countries, with lines indicating trends and ceilings indicated by dotted lines.
Gross Public Debt: below the ceiling
Tax Revenue: below the target

PV of Gross Public Debt in 2015
(Percent of GDP)

Tax Revenue
(Percent of GDP)
Fiscal Deficits
1. Substantial adjustments needed
2. How to reconcile with planned capital spending increases?

Fiscal Deficit (including grants) (Percent of GDP)

Fiscal Deficit (excluding grants) (Percent of GDP)

1 For Burundi, calendar years; e.g., 2015/16 corresponds to 2015
International Reserves

1. Large variations among countries
2. Need to build up reserves

International Reserves
(In months of next year's imports)
The path ahead

- The EAMU Protocol: institutions, processes, etc
- Lessons from the eurozone
- Priorities
Thank you