

Moving Toward a Single Currency

Moving toward a single currency has often been debated in Trinidad & Tobago (T&T). Before, there were talks about 'dollarization' which meant that T&T would adopt a major international currency such as the United States dollar (US) and therefore our economy would be tied to that country. Today, with greater interest put toward a Regional Stock Exchange coupled with the movement toward the Caribbean Single Market and Economy (CSME), it is of interest to the region to consider a Monetary Union.

As we all know, there are currently Caribbean countries that have adopted a single currency. The East Caribbean dollar (XCD) was adopted by eight of the nine members of the Organization of Eastern Caribbean States (OECS). The member states are Anguilla, Antigua & Barbuda, the British Virgin Islands, Dominica, Grenada, Montserrat, St Kitts & Nevis, St Lucia and St Vincent & the Grenadines. The only member that does not use the XCD is the British Virgin Islands which uses the US dollar. The XCD has been pegged to the US dollar since 1976.

What are the benefits of a single currency among the Caribbean countries? Firstly, of direct benefit to citizens would be the ease of use when traveling between the islands. This is because travel in the Caribbean would no longer involve the conversion of currencies when traveling from one country to the next. In addition, a Caribbean national would be better able to compare prices among the different countries rather than having to convert prices to get a relative value.

A common monetary unit would then create a competitive environment with respect to pricing which would also benefit citizens. As consumers are better able to compare prices it would then be easier to purchase goods from the cheapest source. Therefore, companies that charge higher prices in each national market would be pressured to reduce their prices thus benefiting consumers.

This price transparency would also be a major benefit to businesses as imports and exports among the member states would be easier as they would be expressed in the same currency. In addition, businesses would no longer have to worry about fluctuations in the exchange rate or having to convert its domestic currency to a more internationally recognized dollar for exports.

This would in turn eliminate various transaction costs associated with the exchange of currencies. For example, costs associated with the buying and selling of foreign exchange would now be eliminated as both consumers and businesses would no longer lose money as a result of the bid-ask spread of the currency.

Of further benefit to companies is the fact that they would no longer need to manage several currency accounts which complicates currency management and internal accounting systems. For example, a company domiciled in Trinidad with businesses in Barbados and St. Lucia would have to manage its accounts in four different currencies:- the Trinidad & Tobago Dollar, the Barbados Dollar, the Eastern Caribbean Dollar and the United States Dollar. This is because, even if a Company opts to do business in a major international currency such as the USD, if it has established subsidiaries in the other two countries, the company would be conducting transactions in the currency of the country. Hence, it would have to account for such foreign exchange losses or gains when consolidating its accounts. However, if all these countries operated under a single currency, all of these transaction costs and complications would no longer exist. In addition, this would mean that businesses trading among the countries would not have to worry about exchange rate fluctuations as there would be a single currency.

This environment would make the Caribbean more attractive to foreign investors as confidence in the stability of the Caribbean countries is increased. In addition, foreign investors would then be able to conduct business throughout member states with greater ease.

In order for the establishment of a single currency to work however, certain measures would have to be put in place. Firstly, in order to guard against inflationary pressures there has to be mobility within the region. An environment of wage inflexibility and labour immobility for instance would severely cripple the success of one currency. However we are already seeing measures of this nature being put in place with the ease of movement of skilled workers as we move toward the CSME.

Another requirement for a single currency would be the need of the countries involved to have low levels of inflation prior to coming together. With inflation being controlled prior to moving toward a single currency, this would mean that inflationary expectations would be low and the countries would then benefit from a lower level of interest rates and improved control of government debt. The lower level of interest rates would be a major advantage for the securities market as investors move their holdings from low interest bearing accounts to the more rewarding stock market. In addition, the increased size of the securities market together with improved borrowing possibilities due to the low level of interest rates would help improve liquidity.

The loss of the national monetary policy is also a major issue to be considered as the region would now rely on monetary policy for the interests of the region as a whole. In this case decision makers would have to form a Monetary Union in order to have a common policy that would be beneficial to all the member states and that would be agreed upon by all involved. Leaders would have to carefully consider the Caribbean's strengths and weaknesses and implement policies so that the region would be able to benefit from different economic environments. For example, consideration would have to be given to deal with situations such as a drop in oil prices, or declines in tourism sectors etc. Given the diversity of the Caribbean economies however, the decision makers should be able to put measures in place to account for future events ensuring that we are not overly dependent on any one sector. In this way a decline in one sector would be cushioned by another. In addition, the member states would be better sheltered from external shocks. For example, if a hurricane was to devastate Trinidad, it would have a lesser effect on the region compared to Trinidad as a single entity.

Also important would be the psychological effects of losing one's national currency to a completely new unit. This would be especially important for a country whose currency might have been valued higher than the new monetary unit. In addition, nationals in countries whose dollar was worth less would have to understand that even though when they convert to the new currency they would mathematically receive less money; the value of the money remains the same. These psychological issues can be managed with proper education on the conversion to a single currency. The transition to a single currency therefore has to be properly managed on all levels.

Consideration would also have to be given to the administrative and legal costs associated with moving toward a single currency.

Ultimately, the need for a single currency would be essential to the integration of a single market and economy. While there are many benefits to be gained from a single monetary unit for citizens, businesses and the economy, there are support mechanisms that have to be put in place in order for it to function effectively. The proper management of this Union however would

enable the region to reap rewards that would be greater than what would be achieved by a single country.