

## **Comments on “The Golden Age of Business: The Role of the Banking Sector”<sup>\*</sup>**

**Nii K. Sowa, CEPA, Accra**

### **Introduction**

Mr. Chairman, ladies and gentlemen, it gives me great pleasure to participate in this important seminar. This series of lectures presents a good opportunity for the discussion of topical issues germane to policy making in this country. I think both the organizers – ISSER and the sponsors – Merchant Bank Ghana Limited should be congratulated for initiating and keeping the spirit of the lecture series up.

Mr. Chairman, we have just been presented with a very interesting analysis of the role of the banking sector in the Golden Age of Business. The Deputy Governor took us through a review of the post independence development policy of the various governments and their relations with the private sector. He then gave his interpretation of the phrase “Golden Age of Business” and the challenge that dream offers. The rest of the lecture was devoted to addressing the main issue of the role of the banking sector. He suggested that the banking sector could help promote the Golden Age of Business by, among other things, helping government to provide a stable macro environment, extending credit to the private sector, nurturing SMEs and informal sector operators into viable entities. He also went into some constraints which may hamper the operation of the banks and the private sector and how these may be tackled.

### **The Golden Age of Business**

Mr. Chairman, after such a brilliant delivery, there is very little to add. My comments are intended to facilitate the general discussion. I will crave your indulgence first to allow me a broader interpretation of the “Golden Age of Business”. I think we limit ourselves unduly when we interpret the “Business” to refer to just the “Private Sector”. In his opening address at the National Economic Dialogue on May 14, 2001, the initiator of the idea, President J. A. Kufuor, interpreted the Golden Age of Business to mean

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<sup>\*</sup> Prepared as discussant comments on paper presented by the Deputy Governor of the Bank of Ghana, Mr. E. Asiedu-Mante, at the ISSER-Merchant Bank Annual Economic Lecture and Roundtable Discussion,

“...that we all, labour, private sector, civil society and government should work together as Corporate Ghana with a shared, common vision that will allow all to win.”

He went on to say

“The entrepreneur who risks his or her capital should gain benefit. Labour should obtain fair, living wages as compensation for quality time working in a conducive environment. Civil society should benefit by way of services that cater for the disadvantaged, the weak and the aged in our nation. Government should gain benefit from taxes and the ability to ensure meaningful growth, the rule of law and the creation of a prosperous but kind nation”

Mr. Chairman, I submit that the Golden Age of Business makes us all partners and actors in the development of Corporate Ghana.

As the Deputy Governor rightly pointed out we have tried our hands at different development techniques depending basically on the political ideology of the party in power. Thus, political rhetoric on development issues had varied from ‘dirigiste’ socialist leaning to 'laissez-faire' inclinations. Yet, the rhetoric aside, actual development strategy was most of the time dictated by international development experts and was usually in consonance with development thoughts of the period.

Nkrumah had as advisers the greatest development economists of the time - Sir Arthur Lewis and Nicholas Kaldor. Busia relied on a team of Economic advisers from Harvard University. Acheampong, of course, was self reliant and domesticated economic advice. Since the 1980s the course of development in Ghana has been more or less directed from Washington by the IMF and the World Bank. So, after receiving advice from all these development experts, why have we not made much progress? How did countries like Malaysia, Taiwan and South Korea who we were either ahead of or at par with overtake us?

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There are many answers to these questions and delving into all of them will cause us to deviate from the topic of the day. But, among other things, our problems with underdevelopment can be traced to (i) poor governance characterized by coup d'états and corruption; (ii) absence of a focussed development strategy; (iii) poor economic management leading to fiscal excesses, monetary accommodation and weak currency; (iv) weak legal systems relegating business dealing to only personal trust; and (v) distaste for prosperity. Mr. Chairman, these are the very elements of the pre-Golden Age era.

What then are the elements of the “Golden Age of Business”?

Mr. Chairman, I suggest that a “Golden Age of Business” should be an era in which democratic principles are made to prevail. Ghana’s recent democratic dispensation in which change in government is by the expressed will of the people through the ballot box typifies this era. It should be an era in which human rights are respected and the rule of law is paramount. It should also be an era in which business disputes are (I don’t want to say ‘fast-tracked’) settled expeditiously in a court of law. This should be an era in which there should be “zero tolerance for corruption”. It should be an era in which genuine wealth creation and prosperity are desirable objectives.

Mr. Chairman, ladies and gentlemen, the “Golden Age of Business” should also be an era in which economic management is at the optimum. There should be absolute avoidance of fiscal excesses, with central bank independence ensuring zero tolerance for monetary accommodation. Without undue interference in the foreign exchange market, prudent trade and payments policy should produce a “cedi” whose external value commands international purchasing power. This should also be an era in which inequality in the sharing of national wealth is at the minimum.

Mr. Chairman, ladies and gentlemen, we all have a hand in this game. We are the principals and the agents in this business venture. This means that the role of the banks must be such as to generate positive benefit for all to win, and not just the private sector.

### **The Role of the Banks**

Mr. Chairman, we live in a world of surpluses and deficits. At any period in time there are people who have more than their immediate needs demand, and others who need more than their resources can provide. Those with excess funds would like to save their idle funds to earn some interest on them. On the other hand, there are those who need funds and would like to borrow some to use. A bank is that institution which intercedes between borrowers and savers. It collects funds from those who have excess supply and gives it to those with excess demand. In other words, it acts as an 'agent' between the savers and the investors. By performing this function, therefore, a financial intermediary can re-channel idle balances into productive sectors where they are most needed. One begins to see in this the important role that financial institutions must play in the economic development of a country.

Finance is the oil for growth. It is indeed the life-blood of the economic system. The financial system is the vessel that carries this life-blood through the economic system. Faulty vessels prevent the life-blood from reaching essential parts of the economic system. Ladies and Gentlemen, could our inability to develop also be traced to weaknesses in our financial system?

In the pre-Golden Age, state interference in our banking system seriously undermined confidence in the system. For example, in March 1979, the government of the Supreme Military Council decided to mop-up excess currency in the system by changing the cedi-notes. This exercise was aimed at only those with cash outside the banking system. People with amounts not exceeding 5,000 cedis received back only 70 percent of what they exchanged; whilst those with amounts exceeding 5,000 cedis received back only 50 percent. Bank deposits were unaffected and thus the exercise affected mostly the poor. But in 1982 when the PNDC decided to vet those with account deposits exceeding 50,000 cedis, it was the turn of the rich to suffer. The country is still nurturing back the loss of confidence in the banking system which occurred.

The banks also suffered directly in the pre-Golden Age. State-ownership in most of our banks also meant direct interference in the management of the banks. This meant that the management of the banks were dictated more by political patronage than by competence. But, even more seriously, the mismanagement of the economy and its consequent decline led most banks into a distress situation. The high rates of inflation and the large devaluations of the currency undermined the capital base of the banks.

Thus, in the pre-Golden Age the banks had little opportunity to play their proper role in the development process. Most banks were themselves struggling for survival.

Mr. Chairman, the transition to the “Golden Age of Business” is a gradual one. During the preparatory stages, free-market policies and liberalization of markets gave the banks a measure of management control. Banks were allowed to determine their rates of interest. However, fiscal excesses by government and the consequent borrowing from both bank and non-bank public saw rates of interest persistently high. Most banks were, however, sitting well during the transition period. Banks were very happy to invest in the low-risk Government Treasury bills rather than risk-prone lending. A number of banks year after year reported huge profits.

But, the high rates of interest were inimical to business development. Most businesses could not afford rates of interest over 40 percent. Mr. Chairman, such high rates of interest introduce problems of adverse selection and moral hazard in the allotment of credit. As the saying goes “He that is down needs fear no fall”. When rates are too high it is those who have least chance of being able to pay back who take the loans. No wonder, default rate in the banking system is said to have reached about 20 percent of total outstanding loans.

Mr. Chairman, in the “Golden Age of Business” government has decided to watch its fiscal position. Excessive borrowing by government is finally becoming an anathema. Inflationary expectations are on the decline. It is, therefore, imperative that banks reciprocate by bringing down the rates of interest.

There have been moves in this direction but it is not enough. With the central bank Prime Rate currently pegged at 24.5 percent, the major banks have set their base lending rates at about 2.5 percent above prime. In reality after other processing fees and charges are added on we have minimum lending rates in excess of 32 percent. Compared to an official rate of inflation of around 18 percent, the real rate of 14 percent is excessive. Is it the case that the central bank's prime rate is insensitive to the rate of inflation or that we do not believe in the official rate of inflation.

What is even more worrisome is the spread between lending and deposit rates. Depositors receive interest rates ranging from negative (penalties below minimum thresholds) to 15 percent (for really large accounts). In addition, the banks have introduced all kinds of charges and levies. There are, in addition to the usual bank charges, processing fees even when there is no transaction on the account, use of ATM charges, and so on. Further, most of the banks have raised their minimum deposit levels beyond the reach of the average Ghanaian. Clearly, the signal is for small depositors to move elsewhere. Unfortunately, there are very few small and medium banks that can take on the rejects.

Mr. Chairman, Ladies and Gentlemen, the Golden Age of Business calls for the banks to do active banking. Mobilize and canalise resources into productive use. Banks should be prepared to take reasonable risks so as to let credit flow to desirable sectors of the economy. As the Deputy Governor said, it is not only the big companies that need credit but also the small and medium-scale enterprises and the actors in the informal sector. To make the Golden Age of Business meaningful, the banks must ensure that the essential life-blood – finance – flows to all vital sectors of the economy that all must win.