Ghana - Reaching the Next Level Through Global Competitiveness
A Public/Private Partnership
A Report To the Vice President

October 1999

Sigma One Corporation

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October 1999 **Sigma One Corporation**

Ghana- Reaching the Next Level Through Global Competitiveness
A Public/Private Partnership

A Progress Report to the Vice President
Accra, October 1999

Executive Summary
Ghana is not on the path to achieving Vision 2020. Even if cocoa and gold prices were to recover to historic highs, the current policy framework will not propel the economy to the goals set in Vision 2020. The present impact of the dramatic change in the terms of trade highlight the continued vulnerability of the economy to changes in supply or demand for primary commodities. The continued problems of fiscal imbalance are a drag on private sector growth. The impact of monetary policy to counteract the fiscal deficit has resulted in an appreciation in the real value of the exchange rate and continued high interest rates. As a result, the local manufacturing and export sectors are disadvantaged with declining growth in the non-traditional export sector and increasing calls from local industry for protection. The spirit of public-private partnership has suffered as a consequence. This turning inward is the opposite of the export-led growth strategy required for Vision 2020. While Ghana is not presently on the path to accelerated growth, there has been partial success in implementing some of the strategic elements agreed upon by the public/private partnership that met in North Carolina in June 1997.

Economic growth, investment and savings are all substantially below the annual rates that were specified in Vision 2020, and the country lacks a united thrust toward achieving the next level of economic performance through increased international competitiveness. In fact, international competitiveness, as judged by performance of its fundamental determinants, has deteriorated overall.

There has been partial progress in reducing inflation and establishing a framework of improved monetary management; in broadening of the tax base through the implementation of the value added tax; in increasing domestic savings; and in improving the pricing of publicly provided services. There are also initiatives where positive progress may be expected in the near future: these include labor market flexibility and financial sector reforms needed to facilitate rapid growth.

The strategy agreed upon at North Carolina appears to have been supplanted by attention to short-term issues with insufficient attention to the long-term effects of policies and sustaining dialogue with the private sector. Efforts need to be directed at re-invigorating the reform agenda, especially on the fiscal front and instilling discipline to the budgetary processes, and also with respect to removing the impediments to trade and investment, financial intermediation, labor market flexibility, as well as improving the legal framework and effective governance. Initiation of these actions could serve as a basis for reinvigorating the public-private partnership if lessons learned from the North Carolina and National Economic Forum experience are applied.

The Strategy for Rapid Growth
Members of Government and the private sector convened at Chapel Hill, North Carolina in June 1997 to forge a partnership to make the difficult choices needed for Ghana to achieve the rapid growth called for in Vision 2020. Ghana's ambitious objective, to become a middle income country by the year 2020, requires sustained economic growth of 8% p.a. from 1995-2020, a doubling of the rate thus far achieved under the Economic Recovery Program. The participants at the North Carolina Conference committed Ghana to international competitiveness as the way to promote such broad-based economic growth. The role of Government is crucial to the growth process. Government policies are fundamental in

determining the effectiveness with which human efforts and natural resources can be converted into goods and services that are internationally competitive.

Elements of a Strategy for Reaching the Next Level of International Competitiveness

The Ghanaian Delegates to the 1997 North Carolina Conference agreed on the following twelve principles as elements of a strategy for rapid economic growth and the achievement of Vision 2020; a brief assessment of each is provided below.

> ***In Ghana, inflation is a monetary phenomenon that arises primarily from monetary accommodation to the Government's expenditures in excess of receipts. The broad budget of Government must, therefore, be financed in non-inflationary manners, primarily from recurring revenues.***

Reduction in inflation is one of the areas of progress since North Carolina. The year-on-year rate of inflation has fallen from 40% in June 1997 to 12% in August 1999. The dominant force producing this downward trend in inflation has been a sustained reduction in the rate of growth in the money supply in the last two years. In June of 1997, the Bank of Ghana's monetary target, "broad money" (M2+), was growing at a year-on-year rate of 77%, whereas by March 1999 it was growing at 17%. This result was achieved through the Bank of Ghana moving toward strict adherence to its announced monetary targets. In 1998, monetary targets were met for the first time since 1990. Figure 1 shows the close correlation between the annual inflation rate and the excess of money growth above targets for the preceding year.

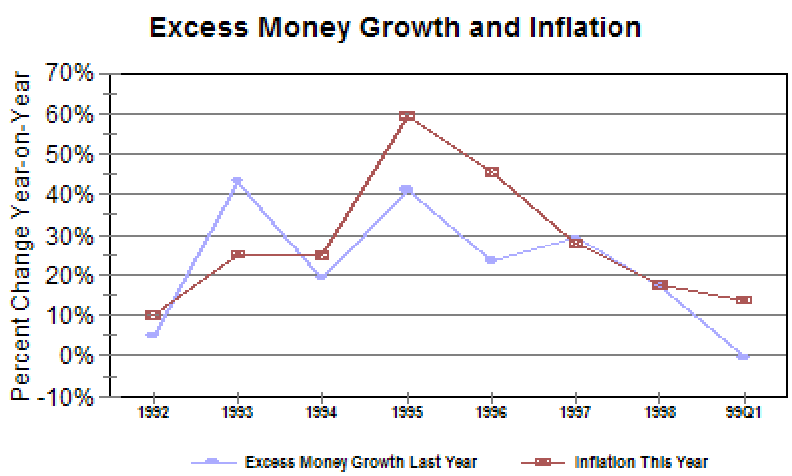


Figure 1: Excess Money Growth and Inflation

The performance by the Bank of Ghana in the last two years demonstrates clearly what was emphasized at the North Carolina Conference: that, in Ghana, inflation is primarily a monetary phenomenon, and that the adherence to monetary targets, which are set consistently in terms of expected real growth in the economy, can produce aggregate price stability. Low inflation produces significant benefits in that it encourages development of the financial sector and lowers the implicit taxation to holders of domestic financial assets, particularly poor people that must hold the bulk of their financial assets in the form of currency. Conversely, excessive monetary growth creates domestic demand pressures that erode international competitiveness directly and induce non-competitive conditions in financial and foreign exchange markets.

The Bank of Ghana has been able to meet its monetary targets because it instituted several important policy changes regarding its role in financing government expenditures, such as absorbing Government accounts that had been held with the commercial banks. This action reduced the extent of Government's overdrawn position with BoG and reduced its interest payments. In addition, the BoG closed its retail window and converted its own bills and bonds into Government securities, thus shifting the financing of the budget away from the central bank and making it more transparent.

The Bank of Ghana rigorously employed various monetary mechanisms to achieve money growth targets, including the use of indirect monetary policy instruments, such as the newly introduced repurchase agreements and foreign exchange swaps. Repurchase agreements, which amount to short-term loans to commercial banks by the Bank of Ghana secured by the temporary transfer of title of T-bills, allowed the Bank of Ghana to quickly intervene in the markets to moderate fluctuations in liquidity and keep reserve money close to targeted levels. As a result, the growth rate of reserve money fell from 33% in 1997 to 17% in 1998. By maintaining a restrictive monetary policy, which engendered high interest rates, the BoG sought to "mop up" excess liquidity in the economy, while encouraging private savings and allowing the market to prioritize the allocation of bank credit.

Ghana's Government absorbs too large a share of the economy for its stage of development. There was a clear consensus on the need for expenditure control and for rigor in using non-inflationary means of financing the Government.

Insufficient progress has been made in the area of expenditure reduction. Government expenditure as a share of total economic activity has declined since 1996, when it absorbed 29.7% of the gross domestic value of goods and services produced within Ghana (GDP). In 1997, Government's expenditure as a share of GDP had fallen to 28.6%, and it remained at that level in 1998. In 1999, it is expected to decline to 26.8%. Unfortunately, recorded budgeted expenditures are not a true reflection of actual expenditures due to the continued problem of arrears.

The domestic financing of the Government deficits has been "crowding out" the private sector from access for finance needed for productive investments. Government and public institutions increased by 69% their indebtedness to the banking system during 1998, after a 170% increase in indebtedness during 1997. This served to continue reducing the private sector's share of bank credit, which had been nearly 100% in 1996, down to 63% at the end of 1997, and to 53% at the end of 1998. Data for March 1999 show the private sector's share of commercial bank credit fell to 51%.

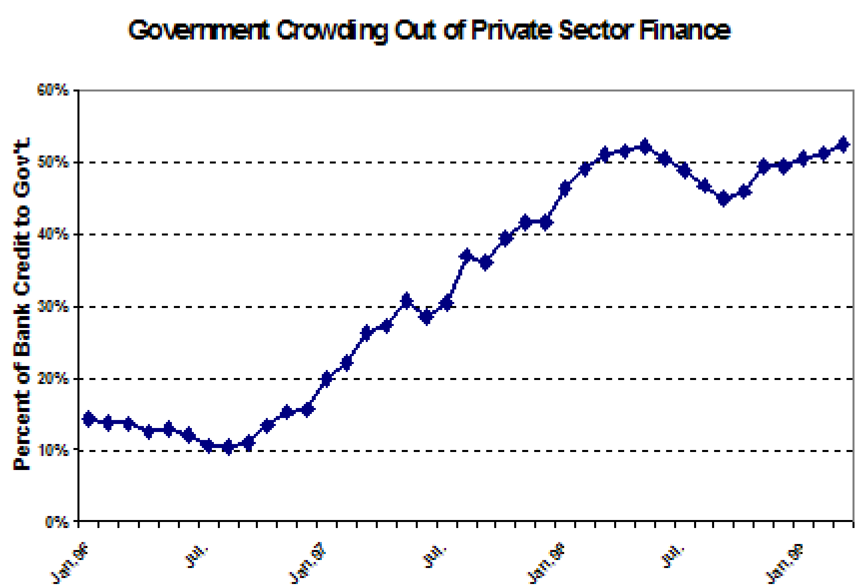


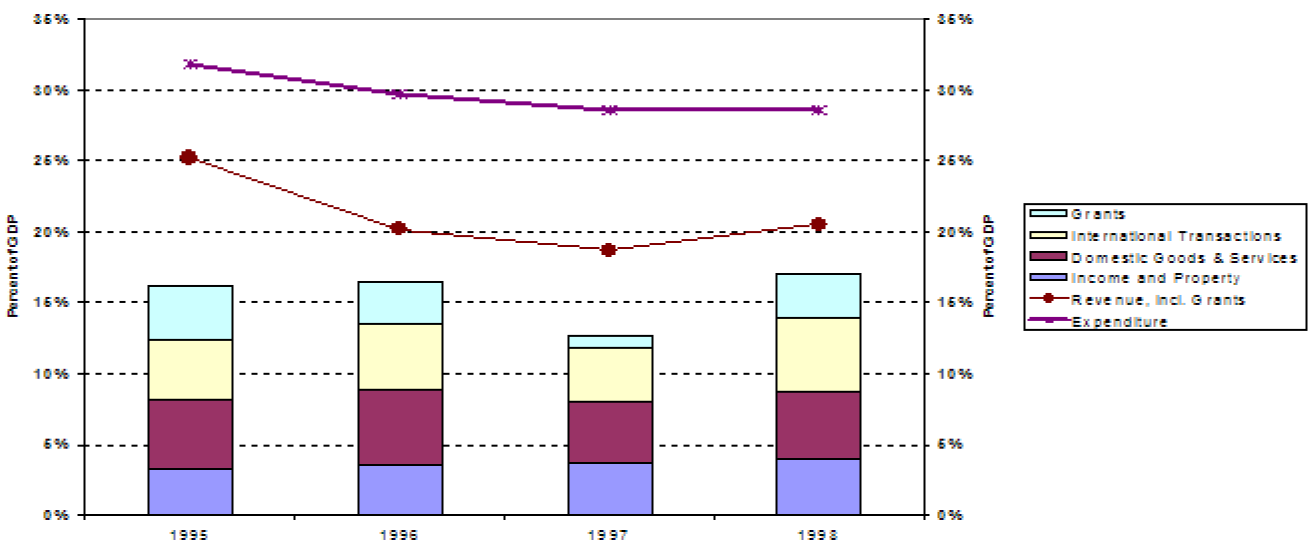
Figure 2: Government Share of Bank Credit

The pervasive and persistent government arrears problems, discussed further below, indicate that a substantial portion of the domestic credit going to the private sector is merely an indirect (and somewhat non-transparent) means of providing additional credit to Government.

The budget and its financing mechanisms should be vetted in advance of the budget year with guaranteed adherence unless legislative approval is granted for exceptions.

In spite of constitutional requirements, it does not appear that either Parliamentary or Ministry of Finance approval are being sought for approval of expenditures exceeding approved budget levels. While the differences between the annual expenditures proposed in the budget and those that actually occurred has narrowed in the last three years, there remains a fundamental problem of failure to seek Parliamentary approval for supplementary expenditures. In 1994, actual expenditures exceeded the approved level by 2.9% of GDP. In 1995, actual expenditures exceeded that approved by 2.0%; in 1996, actual expenditures were above the level approved by 0.8%; and in 1997, actual expenditures were 0.9% less than that approved. In 1998, while actual aggregate expenditures were less than the amount approved, actual recurrent expenditures exceeded the level approved.

Revenues, Expenditure and Fiscal Balance



As noted earlier, the expenditure data do not tell the whole story. A serious budgetary problem is the inability to control Government arrears. While there is agreement that there are arrears, there is disagreement as to their magnitude. In recent years, budget overexpenditures have been masked by increasing arrears to, inter alia, contractors and SSNIT. Unprogrammed budget deficits have fueled inflation or have resulted in a continuing problem of arrears. The former imposes implicit taxation on the rest of the economy and dilutes the real expenditures made to other sectors. The latter, arrears, results in further crowding out of the private sector, in effect, making forced loans to Government. The pressure placed on the economy by Government spending in excess of revenues keeps rates of interest high, and forces the private sector to bear the burden of Government budgetary indiscipline. Even adherence to strict monetary targets by the Bank of Ghana cannot achieve macroeconomic stability and the conditions needed for rapid and sustained private sector growth in the absence of fiscal discipline.

With respect to road construction arrears, these were estimated by the IMF at ¢ 130 billion (US$54 million) at the end of 1998. This number would appear to be substantially underestimated because a World Bank review of the problem in late 1998 identified US$63.3 million of arrearages on just seven projects. Admittedly, these are the projects with the largest arrearages; but, given that there are more than 50 projects under construction, the road arrearage problem was probably closer to US$100-$120 million in late 1998, or about 1.7% of GDP. A reason for believing that arrearages are at the higher level is the experience with the roads sector budget in recent years, when expenditures have consistently exceeded budget allocation. While we do not have the 1998 numbers, a comparison of road sector budget allocations to expenditures for 1995-1997 indicated the size of the problem. The average overexpenditure over that period exceeded 140% of the original allocation, resulting in the accumulation of arrears.

In the case of the Social Security and National Insurance Trust, the arrears problem is that not all the money budgeted by the Government to pay the SSNIT contributions for government workers is paid in the fiscal year for which the money was budgeted. In December 1998, SSNIT was owed ¢ 85 billion by the Government as delayed contributions.

All sectors, including Government, should strive for efficiency in their revenue generating and taxation role. There was recognition that a broader tax base would be consistent with increased international competitiveness. The prices of publicly provided goods and services, such as petrol and energy, should be priced to insure full cost recovery under efficient delivery systems. This would promote competitiveness by reducing the risk of off-budget expenditures, stimulating the efficient use of scarce resources, and improving the availability and reliability of public services.

The present narrow tax base leaves the economy vulnerable to large swings in revenue collections which in turn result in large unexpected budget deficits or surpluses. In 1998, government tax revenue sources were as follows: 27% from income and property taxes; 32% from taxes on domestic goods and services; and 41% from taxes on international trade. In 1998, taxes as a percent of GDP rose for the first time since 1993, to 15.6% of GDP. The increase was due primarily to increased cocoa tax receipts, which increased from 1.8% to 2.3% of GDP, due to a combination of increased world cocoa prices and expanded domestic production. This reliance on trade taxes not only reduces competitiveness; it also highlights the vulnerability of the tax system to a narrow tax base.

The introduction of the VAT in late December 1998 was intended to provide a broader tax base that would reduce the dependence on trade taxes and reduce inter-sectoral distortions arising from the tax and tariff regimes. In the six months since introduction, VAT revenues are within 3% of the target, producing approximately the same share of GDP as the tax it replaced, with a rate two-thirds as high. It would thus appear that the purpose of broadening the tax base at lower rates is being served by the VAT.

While the tariff system has been simplified and consolidated, an area for concern is that of exemptions (about 40% of imports are exempted from duties). Exemptions presents problems of transparency, efficiency and lost revenue, that combine to reduce Ghana's international competitiveness. Exemptions at present can be granted under a number of different authorities, under terms and conditions that are often poorly specified. Such processes invite rent-seeking and abuse, especially when combined with the weak monitoring and control system presently in place. In addition, the users of imported goods brought in under exemption have a market advantage over users of the same good imported under the statutory tariff rate. This creates an arbitrary differential in profitability across firms. It also encourages rent-seeking (and corruption) as importers lobby for exemptions, rather than engaging in market competition. In addition exemptions represent a significant loss in tax revenue of ¢25-¢40 billion, which aggravates the fiscal deficit. For all of these reasons, the exemption issue should be addressed.

Revenue generation efficiency is important for competitiveness, not only in the area of tax collections, but also in the pricing of publicly provided goods and services. This is an area in which Ghana has made significant progress since the North Carolina Conference.

In the period since North Carolina, accumulated losses to electricity providers are being addressed with major changes in the pricing of publicly provided electrical services. The 1998 reduction in the supply of electricity due to drought, at the same time that demand was growing rapidly, signaled a wake-up call to review energy sector policies. The resulting review cited the need for increased investment in capacity, mainly from the private sector. The increased supply of energy will come primarily from thermal sources. This will mean that Ghana's future energy costs will be more dependent on petroleum/natural gas prices. In February 1998, the Public Utilities Regulatory Commission increased the weighted-average tariff rate by about 90%; and in September 1998, a further increase of 100% was approved. While substantial, these increases have not been sufficient to allow the present producer to cover operating and capital costs. Further increases to achieve full cost recovery will be required in 2000.

While posing short-run difficulties, a movement to full cost pricing, based on the actual cost of servicing each sector (e.g., households, commercial and industrial sectors), will promote competitiveness and efficiency by signaling to users the real cost of energy. In addition, the Public Utilities Regulatory Commission should promote transparency in energy costs and pricing, and reduce the risk of off-budget expenditures to subsidize energy by having each sector pay its marginal cost of service. While the rate increases for electricity may lead to an apparent loss of competitiveness for energy-intensive enterprises and users, the alternative is continued shortages, with reliance on rationing and "blackouts" to manage the excess demand. The move to full cost pricing and the introduction of the VAT represent two situations where the Government, in collaboration with the private sector, made difficult choices that will result in a stronger, more competitive economy in the long-term.

> ***The nominal exchange rate should not be used as an anchor for inflation, but rather strict monetary targets should be set and fulfilled. Interventions in the foreign exchange market add costs and risks to all private enterprise activities.***

A policy of using foreign exchange reserves and other measures to restrain currency depreciation has been used by a number of countries as a means for repressing inflation. This practice is referred to as using the nominal exchange rate as an anchor for inflation. While not an official policy of the Bank of Ghana, the stability of the exchange rate experienced during 1998 would suggest that this policy was de facto used by the Bank of Ghana in the fight against inflation.

This de facto use of the exchange rate has had negative consequences for competitiveness. Prices in Ghana from 1994 to 1998 rose faster than prices in major trading partners, but the Cedi exchange rate did not depreciate sufficiently to offset that inflation differential. This permitted foreign products to gain a competitive advantage over Ghanaian products, eroding the profitability of Ghanaian producers of exports and import substitutes. This resulted in lower export growth, especially of non-traditional exports, and higher import growth than would have otherwise obtained if Ghana had maintained a competitive exchange rate. As a consequence of this deteriorating competitiveness, not only was there a larger trade deficit, but investment in agriculture and industry was increasingly discouraged. The erosion in competitiveness reduced the opportunity to diversify the economy's export base, leaving the country more vulnerable to shocks to the markets for its major traditional exports of cocoa, gold and timber, and increasing dependence on international donors and creditors.

The increasingly uncompetitive exchange rate, while attractive to consumers, importers and short-term investors, is not sustainable. At some point, more painfully the longer adjustment is delayed, the exchange rate will adjust to restore external balance; but, by that time much damage may have been done to the opportunities for Ghanaian producers to employ local resources profitably to produce goods for export markets or to compete with imports.

But, adjusting the nominal exchange rate, by itself, is not an effective means to restore domestic competitiveness to domestic producers, and external balance to the economy, because other factors, such as the terms of trade, the level and stability of capital flows, real wages, excess money growth, tariff and non-tariff barriers, and the output-expenditure gap, are at work in determining whether the economy really has a competitive exchange rate. To restore competitiveness to an economy that has allowed its exchange rate to become overvalued requires concerted action and a coordinated macroeconomic policy framework, getting fiscal policy, monetary policy, wage and labor market policy, trade policy and financial policy all to work together.

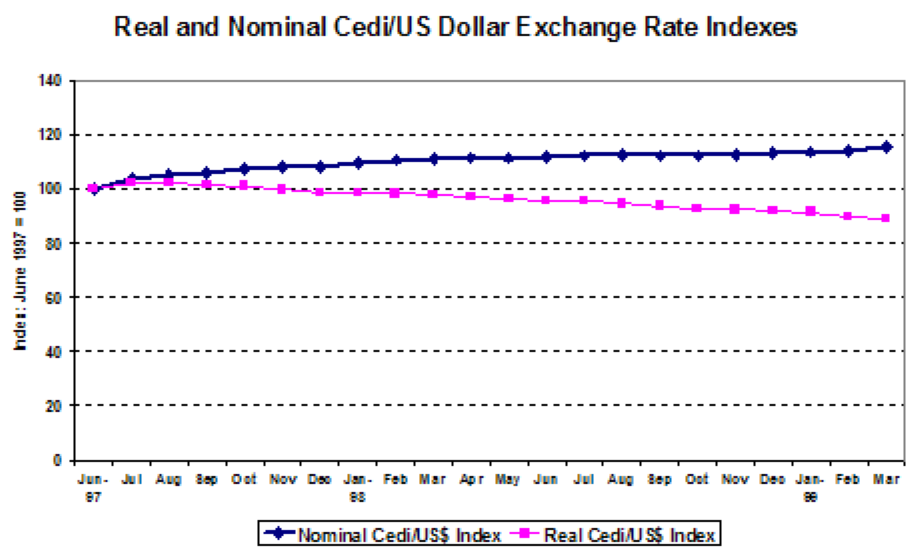


Figure 4: Real and Nominal Exchange Rates

Regardless of the origin of the current situation, the existing conditions in the market for foreign exchange reduce the incentives to export, since the number of Cedis paid per unit of foreign exchange is artificially low and does not provide adequate incentives for exporters. The real appreciation that has occurred since 1994 is, in effect, a tax on gross revenue, and comes mainly from profits, and reduces or negates the impact of government and/or donor investments. For example, the reduction in Cedi gross income to the agricultural sector from agricultural exports in 1997 due to the real appreciation of the Cedi is estimated to be ¢ 190 billion, equivalent to total donor investments in the agricultural sector from 1995-1997.

The continuing erosion of competitiveness is not consistent with the strategy adopted at North Carolina, and has both short-term and long-term adverse consequences for Ghana's economic health. The short-term consequences are low foreign exchange earnings and balance of payment problems. The long-term consequences are more important. A small economy like Ghana must be part of the international economy to grow and prosper. New technologies and business methods must be brought in and adapted. Knowledge about new markets and commercial arrangements must be gained. Reduced incentives to produce exports and import substitutes mean that these linkages remain weak. As a result, new technologies, rewards for innovation, and the economic discipline to produce high quality goods in an efficient manner are limited in all parts of the economy -- tradable and non-tradable alike.

Domestic savings are too low to sustain rapid growth and to attract foreign investment. Chronically high inflation is a principal deterrent to higher savings rates. Rising incomes will generate higher levels and rates of domestic savings, if the financial institutions develop appropriate instruments and incentives for savers in Ghana.

Since 1993, when the level of gross domestic savings was negative 2.2% of GDP, there has been an upward trend in both the gross domestic savings rate and the rate of gross national savings (gross domestic savings plus the savings of Ghanaians abroad remitted to Ghana). In 1998, gross domestic savings increased to 13.2% of GDP from 9.8% in 1997. Gross national savings increased to 19.4% of GDP in 1998 from 15.4% in 1997. Private sector savings likewise increased from 7.1% of GDP in 1994 to 15.6% in 1998. This increase in the savings rate helped to fuel an increase in private sector investment from 3.1% of GDP in 1994 to 13.1% in 1998.

The growth in gross domestic savings and gross national savings in recent years was, in part, induced by major changes in the level of interest rates. In 1995, real domestic interest rates were highly negative (the real discount rate was -9%). By 1997, they had turned highly positive (the real discount rate was +13.4%); and in 1998, the real discount rate was 16.7%. This means that domestic interest bearing financial assets have been attracting real returns substantially higher than the real returns on international financial assets (for example, real returns on U.S. Treasury Bills have been below 4% in the same time period).

The increased rate of savings in recent years involves both good and bad news. The good news is that Ghanaians save when it is financially rewarding to do so. The bad news is that the increased level of savings, which is being encouraged by high real interest rates, is to a large extent being used to finance the government's deficit, rather than being used to support private sector investment. At the current high real interest rates, agricultural and industrial enterprises cannot afford to borrow to increase their level of operations. Thus, the high real interest rates and improving savings rate will not generate and sustain the growth needed to achieve Ghana's development goals. The high real rate of interest reflects the financial market's assessment that, with the current macroeconomic policy framework, Ghana is still a high-risk investment destination. With a more stable macroeconomic environment, that risk premium should fall. Until it does, little of the increased savings will be used to finance industrial and agricultural growth.

The financial policy reforms introduced have, however, served to strengthen the financial sector and foster greater public confidence in the monetary system and in the financial institutions supervised by the authorities. This has contributed to increased domestic savings. Not only have residents increased their holdings of money relative to GDP as soundness returned to the financial system, they also increased their savings through other non-bank financial institutions, such as the Ghana Stock Exchange, SSNIT, private pension funds, insurance companies, discount houses, venture capital funds, etc.

As positive real rates of interest re-emerged in the financial system in 1996, the ratio of broad money (M2+) to GDP, a measure of financial deepening, rose from 0.179 to 0.222, and increased further to 0.239 in 1997. This financial deepening indicates an improvement in confidence in the domestic financial system. At the same time, the incentives provided by higher positive real rates of interest induced the public to move more of their financial assets from non-interest bearing money to interest bearing financial assets, such as savings and time deposits, another sign of financial deepening. The additional domestic savings held in the form of money have been substantial, amounting to 6.3% of GDP over the period 1995 to 1998.

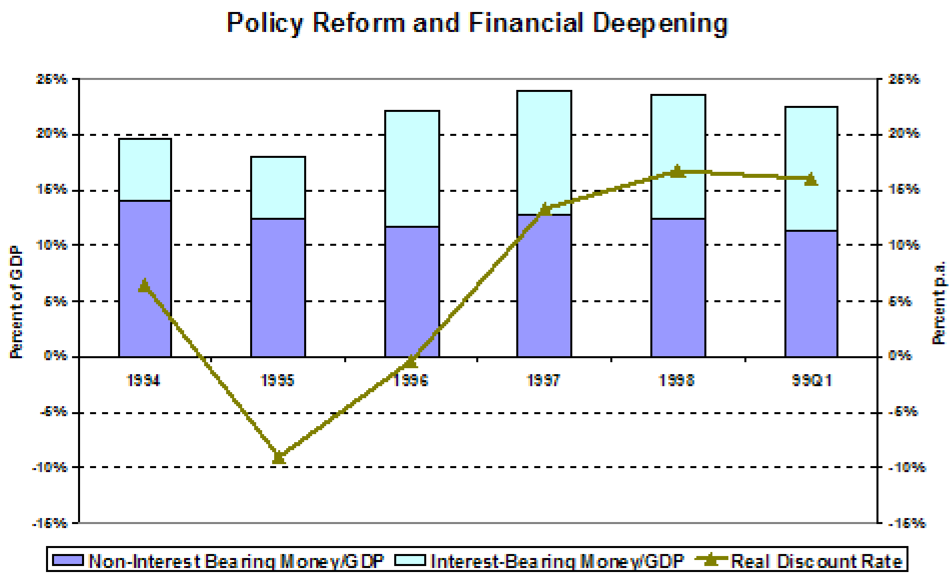


Figure 5: Policy Reform and Financial Deepening

Another example of financial deepening is the increased savings that have been accumulated in SSNIT's pension fund, which have grown from ¢296 billion at the beginning of 1995 to ¢1,175 billion at the end of 1998, a net increase of ¢879 billion in the fund, representing an average 1.8% of the annual GDP over the period. The market capitalization of the Ghana Stock Exchange also increased substantially over the period, from ¢1,968 billion at the end of 1994 to ¢3,246 billion at the end of 1998, raising the wealth of both domestic and international investors by ¢1,278 billion, equivalent to about 2.6% of average annual GDP over the period.

Thus, financial sector reforms have provided increasing opportunities and incentives for savers to mobilize resources for productive investments. But, the challenge remains to build on those reforms to provide the environment needed to mobilize the even higher levels of both domestic and foreign savings needed to finance the rates of investment needed to achieve Vision 2020 growth targets.

Financial sector reforms must be built upon sound macroeconomic management that insures stability in prices and exchange rates. The present system cannot attract or reward domestic savings in the range of 25% of GDP as required for Vision 2020. There are missing institutions and instruments in Ghana's financial system, and those that exist serve the financing needs of Government, primarily. Financial reform must include revisions of enabling legislation and specification of the legitimate roles of oversight and supervisory bodies and entities. Adequate financial supervision is needed to create confidence among savers and investors in Ghana's bank and non-bank financial institutions. Pension reform and transparency in the SSNIT investment portfolio are priorities in harnessing existing domestic savings. Increased privatization is called for throughout the system.

There have been a variety of measures adopted to reform the banking system, with efforts by Government to clean up the existing portfolio of non-performing loans in the banking system, to divest its shares in commercial banks, and to find strategic investors to strengthen management of weak banks. These reforms include new legislation and regulations to strengthen supervisory powers and streamline entry and exit from the banking industry, while adhering to strict professional and financial standards.

In spite of progress in the financial sector, there is need for further reform and innovation. The banking system has been able to make high and easy profits servicing the Government debt, rather than intermediating funds to productive private sector investments. Real interest rates fluctuate considerably, making it difficult for term lending to occur.

SSNIT is important, both as a source of investment funding for the economy, and as a provider of retirement income to pensioners. A challenge for SSNIT is to develop an investment portfolio that can maximize its impact on national growth, subject to meeting the long term income requirements of those who provide the funding; i.e., Ghana's present and future pensioners.

However, the policy regime facing SSNIT, including Government fiscal practices and interventions, has been having a deleterious effect upon SSNIT's performance, reducing its income, eroding its asset base and jeopardizing its ability to meet its pension obligations. Since 1991, the Social Security Pension Scheme has experienced a substantial growth in assets, from ¢60 billion to about ¢1,175 billion in 1998. But, in real, constant 1998 price terms, the assets of the Trust have been basically stagnant since 1993, despite the growth in contributors and contributions in excess of payments of pensions. In real terms, given the growing numbers of pensioners and contributors, the Scheme's ability to fund its growing obligations has deteriorated since 1994.

If Ghana were truly a good investment destination for investors, SSNIT, with its resources and local knowledge, should have been on the fast track to capture some of those high returns. Rather, the Trust's investment performance has been poor, with the return on investments for the cumulative eight year period ending December 1998 a negative real return, of –12% p.a. Part of the reason for this is that the Government is often in arrears to the Trust and does not pay penalty on delayed payments, thus reducing SSNIT's income.

The erosion of the real value of the Trust and of its ability to meet obligations is also due to certain development-oriented investments which yield low real returns. These activities include, but are not limited to, construction and rental of residential housing, as well as building schools, hospitals and industrial parks. While the objective of the Trust to support investments that are in harmony with the public interest is well-intentioned, the public interest will not be served by investing SSNIT's funds into projects that yield low or negative returns. SSNIT needs to separate its role as a social security scheme from its development-oriented role, and should not jeopardize its ability to meet its social security obligations by undertaking financially unsound investment projects.

> ***The investment regime remains over-burdened with regulations and bottlenecks. Further regulatory and administrative reforms are needed. Public entities in the investment promotion and administration network need to develop pro-business attitudes among their staff members. Such institutions should support the private investment process, not control it, i.e., "don't pick winners" (or losers), but support the private sector entrepreneurs once they take the risks.***

Annual gross investment rates have fluctuated between 20% and 24% in the last five years. Annual GDP growth rates of around 4% imply a capital-output ratio of 5 to 6, high by international standards. This high capital-output ratio may be due to a substantial amount of the investment going into residential and office building construction, rather than into manufacturing and other tradeable goods production.[1] Pursuing a path of capital intensive development, with such a high capital-output ratio, would require savings rates even higher than those contemplated by Vision 2020, if middle income country status is to be achieved.

To reach Vision 2020 targets, the investment regime also requires further regulatory and administrative reform. One particular weakness is the court system, where it can take several years to reach a judgement on simple issues that should be resolved in several weeks. The complicated land tenure system, when combined with the present court procedures, makes investing a challenge. Likewise, for the Ghanaian private sector, especially the financial sector, the widespread delays and adjournments in the court system increase costs of doing business. There is no effective Bankruptcy Law in Ghana that would allow firms in financial difficulty to seek protection from creditors while undergoing a restructuring under court mandate. Other weaknesses in the investment regime that impede competitiveness include onerous procedures and regulations at borders, excessive numbers of permits required and long lead times in getting applications approved.

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[1] When a Sigma One focus group survey in August 1999 asked business people in which sectors they would invest additional capital, they uniformly responded construction. Construction included residential housing and institutional buildings like dormitories and offices. Housing is very close to a pure non-tradeable good, as its price in the market reflects almost entirely domestic factors. The fact that both resident and expatriate Ghanaians feel that the best place to invest their capital is in housing is strong evidence that incentives for exporting or producing import substitutes are depressed relative to the non-tradeable sector.

The trade infrastructure of ports, airports, roads and overland ports of entry must be upgraded to attract foreign direct investment. The financing of these upgrades will require private participation under the build, own and operate and build, operate and transfer concepts. These efforts are needed if Ghana is to be the Gateway to Africa.

While significant improvements have occurred, Ghana's inadequate infrastructure is still a constraint to competitiveness: it leads to higher transport costs that reduce the competitiveness of producers in the interior of the country and their ability to export; and the high direct and indirect costs of Ghana's ports further reduce Ghana's export competitiveness. There are a number of indicators of the severity of the problems. For example, the cost of loading input containers at the ports in 1998 ($168) was more than twice the international standard. Likewise, at 12 boxes per ship hour, the speed of unloading containers is 50% of what it should be, while the average dwell time for imported containers, at 25 days in 1998, was more than three times international benchmarks. Transport costs are a principal factor in the high marketing margins in Ghana. These increase prices to consumers, raise production costs and reduce the competitiveness of Ghana's exporters. The Gateway project will assist the Government to address these problems, but more investment will be needed.

Vision 2020 requires the efforts of all Ghanaians. In Ghana, the majority of the productive resources, particularly human resources, operate outside the formal system as a result of a cumbersome business environment and narrow tax base. Small enterprises must be incorporated into the growth processes through streamlining the legal and regulatory environment, broadening the tax base and reducing tax rates. The Conference adopted a concept called "Push-Pull" aimed at promoting effective business linkages based on mutual gain between small and large enterprises. "Push-Pull" requires a reduction in the riskiness of business and the creation of mutual trust through enforceable contracts and successful and profitable experiences among business partnerships.

The North Carolina Conference suggested the "Push-Pull" strategy as a means by which small firms, that lacked access to credit and improved technology, could be linked with larger firms through whom credit and technical expertise could be channeled more efficiently. These linkages between larger and smaller firms would enable the latter to serve as suppliers of inputs or outputs to the larger firms, while credit and technical support from the former would help the smaller informal sector firms to develop.

While this concept is being used to improve the linkages between informal sector and formal sector enterprises, the problem is more complex, involving macroeconomic instability and labor market imperfections, in addition to the problems of access to credit and technical expertise. Macroeconomic policies, combined with labor market rigidities, have created a high-cost/high-risk environment for Ghanaian entrepreneurs. The high costs of doing business in Ghana lead many entrepreneurs to remain outside the formal sector. Workers in these firms are disadvantaged by the lack of complementary tools and materials. As a result, they achieve lower levels of productivity than their skills and efforts would warrant, and consequently receive lower pay for the effort.

Low incomes, widespread poverty and many social ills are the direct result of not enough productive jobs being created in Ghana, because the economy is uncompetitive. As a result of the high costs, relative to productivity, of labor, formal sector employment has stagnated at fewer than one million workers in a labor force of more than eight million; and approximately half of formal employment is within the public sector or state owned enterprises. New entrants into the labor market number approximately 200 000 annually, the majority of which are forced to work informally as casual workers or petty entrepreneurs.

There are important participatory dialogue processes underway that show promise in addressing these interrelated issues, and improving the performance of the labor market. Labor code reform is being negotiated through an expanded Tripartite dialogue, which is intended to consolidate and update the labor laws so that they are easier to follow, as well as place them in compliance with ILO conventions and the Constitution. Efforts to improve labor market flexibility include delegating industrial relations issues to the firm level and preserving the rights to collective bargaining for negotiating compensation, terms and conditions of work.

Given the dominant role of Government in formal sector employment, Government wage policy sets the standard on the wages and conditions of employment throughout the formal sector. The reforms instituted by Government for its employees under the Ghana Universal Salary Structure go far toward rationalizing compensation and separating wage determination in the public sector from that of the private sector.

> ***The costs from "administrative hassles" and sluggish customs clearance procedures, etc. are a disproportionately larger burden on smaller enterprises, and such factors reduce the competitiveness of the economy in general. Much of the informality that exists is a response to these burdens as small firms attempt to avoid these costs of doing business in Ghana.***

Administrative hassles in dealings between the private sector and the public sector continue to reduce Ghana's international competitiveness. Among the inconveniences are customs clearance procedures that are unnecessarily lengthy and complicated. A recent review by the Association of Ghanaian Industries identified 62 separate steps required for clearing goods. This results in delays in getting goods cleared, as well as the need for constant oversight of the process. The procedures are not only costly in terms of time, but also involve substantial financial costs as capital, with interest costs of 3%-4% a month, is tied up longer than necessary. These costs are passed on to domestic consumers and increase the cost of doing business in Ghana.

Significant management time is spent resolving administrative issues. This may be one reason why many of the administrative procedures are short-circuited through appeals directly to senior civil servants. It may also explain why Ghana is ranked 18th out of 23 African countries in terms of time spent by senior management obtaining permits and licenses in the 1997 African Competitiveness Study. In fact, 21% of Ghana's senior managements' time was reported spent with officials negotiating or obtaining licences, regulations, permits or tax assessments. This contrasts with 3% of senior management time spent on these issues in Namibia and 12% for Nigeria.

While administrative hassles are costly for any Ghanaian entrepreneur, they pose especially difficult problems for the small firm. A large firm would have senior managers specialized in various aspects of the company, a manager of a small informal sector firm is often the only senior manager. Management in the informal sector firm may not be able to spend the more than 20 percent of its time on administrative inconveniences; thus, these impediments mean the firm is not able to move up to the next level of performance.

The Conference forged a public-private partnership for achieving the social, economic and political goals inherent in Vision 2020. The partnership calls for agreement on goals and open debate on the means needed to achieve these. The consultation between the partners will be frequent, informed, respectful, candid, polite, and inclusive. All constituencies are welcome to participate in the consultations, and all consultations will be open to all. The first consultation is to convene a summit for national economic consensus as soon as possible. The mandate of the first National Summit will be to address pressing economic issues that affect private sector performance and the performance of the national economy as a whole. The Private Enterprise Foundation was designated as the convener of the summit and the President of the Republic as the leader of the summit.

The spirit of public-private partnership engendered at North Carolina has diminished. Several factors help to explain the waning of enthusiasm for the public-private partnership. These factors involve both expectations and performance of the public-private partners.

The private sector perspective was that North Carolina acknowledged their key role in the attainment of the Vision 2020 goals. The frank discussions of the nature and causes of the problems in the macroeconomic environment signaled to the private sector a true sense of partnership and open dialogue (previously most such meetings had contained mere statements of policy, without a thorough discussion of the nature and causes of the problems). Implicit in the acknowledgment of the importance of their role was the belief that they would henceforth play a greater role in the policy debate. Furthermore, there was a statement in the report that "the consultations between the partners will be frequent, informed, respectful, candid, polite and inclusive." This expectation of a greater role for the private sector is also reflected in the call for the Private Enterprise Foundation to be the convener of a National Economic Summit, with the President of the Republic as the leader of the summit.

These expectations were, unfortunately, unrealistic. For example, with respect to National Economic Summit, it would have been more appropriate, and in the spirit of public-private partnership, to have named a Government agency as an equal partner to work with the Private Enterprise Foundation. This was not done and the Private Enterprise Foundation assumed they had the leadership role in the planning and preparation of the summit. The decision by Government, in response to a concern as to the direction of the summit, to assign to the National Development Planning Commission the role of convener of the Forum led the Private Enterprise Foundation to retreat from the role of full partner to that of participant, and weakened the spirit of public-private partnership.

The National Economic Forum temporarily revived the spirit of partnership, as evidenced by the level of attendance and vigorous discussions on the economy's problems and proposed solutions. Recommendations were formulated and an action plan prepared based upon what had been agreed at the Forum. However, the action plan assigned responsibilities to MDAs without their consent or agreement, and there was no means provided to enforce or support implementation of the recommended actions. As a consequence, those elements of the action plan that were implemented reflected what particular MDAs chose to implement. While nominally the NDPC was assigned the responsibility to monitor and report on performance, it had neither the authority nor the resources to carry out the tasks. Consequently, the failure to consult and report on the Forum is viewed as a lack of commitment by Government to the partnership, and has led to a general perception that few Conference and Forum recommendations were acted upon.

These impressions were reinforced, when soon after the Conference, the attention of Government leaders shifted from consensus building to coping with immediate economic difficulties, such as the energy crisis and concern for contagion from the Asian financial crisis. The immediacy of the problems forced the Government to adopt a tactical approach to problem solving, and the strategic perspectives of the conference were relegated to a lower level of priority.

While the bi-monthly consultation between the Vice-President and the Private Enterprise Foundation have maintained contact and have been useful as a communication mechanism, it has not served to maintain the strategic thrust of international competitiveness. Cabinet Ministers do not attend these meetings, so the private sector participants do not have the opportunity to engage the officials who will need to act upon their frustrations. This limits follow-up. As a consequence, individual associations have opted for more individual representations with Government, rather than through the Private Enterprise Foundation.

To revitalize the partnership, the initiative must come from the Government and it must be accompanied by new terms of engagement. The terms of re-engagement must be clearly established so as to clarify the role and responsibility of each side. The emphasis should not be on more meetings, but meetings that are focused and have the appropriate public and private sector officials in attendance that can address the problems under discussion. Likewise, there must be a capacity to monitor, follow-up and report on the implementation of policy reforms agreed at these meetings. This follow-up will allow the participants to be continually updated on actions and to provide reality checks on the consequences of the actions. Without more focused dialogue with all appropriate members present and monitoring and reporting on follow-up, the dialogue process will continue to lose credibility and increasingly become complaint sessions. It is not too late to change the process, but change is required if the public-private partnership is to be revitalized.

CONCLUSION

At the North Carolina Conference, Ghana renewed its commitment to the long-term goal of liberating the potential of the economy. It was recognized that the dynamic policy stance required to achieve this would be associated with significant short-term political and social costs. The different parties agreed that the success of the strategy would be dependent upon commitment by all parties to the process.

This review observes that the requisite political cooperation underpinning the strategy adopted at North Carolina has been absent, and that Government has not provided the dynamic leadership needed to address the fundamental weaknesses that exist in the policy framework. In a number of the areas agreed upon in North Carolina, there has not been sufficient progress. A lot still needs to be done in managing the budget, in desisting from using the nominal exchange rate as an anchor for inflation, in eliminating the nuisances associated with doing business in Ghana and in forging a public-private partnership for reform. A real commitment to resolving these issues is essential if Ghana is to overcome the weaknesses of the past.