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Report No. 14158

# PROJECT COMPLETION REPORT

REPUBLIC OF GHANA

FINANCIAL SECTOR ADJUSTMENT CREDIT I
(CREDIT 1911-GH)

MARCH 29, 1995

Industry and Energy Operations Division
Central-Western Africa Department
Africa Regional Office

## CURRENCY EQUIVALENT

(As of May 10, 1994)

| | | |
|---|---|---|
| Currency Unit | = | Cedis |
| US$1 | = | ₵920.75 |
| ₵1 | = | US$0.67 |

## ABBREVIATIONS

| | |
|---|---|
| ADB | Agricultural Development Bank |
| BBG | Barclays Bank (Ghana) |
| BCC | Bank for Credit and Commerce |
| BHC | Bank for Housing and Construction |
| COOP | Cooperative Bank |
| CDH | Consolidated Discount House |
| ERP | Economic Recovery Program |
| FINSAC I | Financial Sector Adjustment Credit I |
| FINSAC II | Financial Sector Adjustment Credit II |
| GCB | Ghana Commercial Bank |
| GDP | Gross Domestic Product |
| GSE | Ghana Stock Exchange |
| ICAG | Institute of Chartered Accountants of Ghana |
| IFC | International Finance Corporation |
| MB | Merchant Bank |
| M2 | Broad Money |
| NIB | National Investment Bank |
| NPART | Non-Performing Assets Recovery Trust |
| NSCB | National Savings and Credit Bank |
| ODA | Overseas Development Authority |
| PCR | Project Completion Report |
| PEED | Private Enterprise and Export Development |
| SCB | Standard Chartered Bank |
| SSB | Social Security Bank |

## FISCAL YEAR

January 1 - December 31

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THE WORLD BANK
Washington, D.C. 20433
U.S.A.

Office of Director-General
Operations Evaluation

March 29, 1995

## MEMORANDUM TO THE EXECUTIVE DIRECTORS AND THE PRESIDENT

**Subject:** **Project Completion Report on Ghana**
**Financial Sector Adjustment Credit I (Credit 1911-GH)**

Attached is the Project Completion Report for the Ghana Financial Sector Adjustment Credit I (Credit 1911-GH) prepared by the Africa Regional Office, with Part II of the report contributed by the Borrower.

The main objective of the project was to support the first phase of a financial sector adjustment program aimed at: liberalizing the banking environment so as to improve the efficiency of resource mobilization and allocation; restructuring distressed banks; strengthening the banking regulatory and supervisory framework; and developing financial and capital markets.

The overall implementation of the project progressed well. The liberalization of the financial environment has now been largely completed with the removal of interest rate ceilings and sectoral credit targets. A new regulatory framework has been introduced by an amended Banking Law and the banking supervision function has been adequately strengthened. A banking restructuring program has also been initiated and the development of money and capital markets has had a modest start.

The reforms in Ghana's financial sector have resulted in the restoration of financial soundness in the banking system and have contributed to an increase in the range of available banking services as a result of the entry of new merchant banks. However, there has been little impact on financial deepening and banking competition remains stifled by the slow pace of privatization of the state-owned banks. The Bank's follow-on project—Financial Sector Adjustment Credit II, approved in FY92—supports the divestiture of some of these banks.

The project outcome is rated as satisfactory. Institutional development is rated as substantial and sustainability as likely.

The PCR is of good quality. It provides a good assessment of the project's implementation experience and results. A combined audit of this project and the follow-on operation is planned.

Francisco Aguirre-Sacasa
Acting Director-General

Attachment

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# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

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**REPUBLIC OF GHANA**
**FINANCIAL SECTOR ADJUSTMENT CREDIT I**
**(Credit 1911-GH)**

## PREFACE

This is the Project Completion Report (PCR) for the first Financial Sector Adjustment Credit I (FINSAC I) to Ghana for an original amount equivalent to US$100 million approved on May 31, 1988. This amount was subsequently increased to US$106.6 million equivalent through a supplementary IDA Credit. The Credit was signed on June 14 and declared effective on August 11, 1988. The original closing date of September 30, 1990 was subsequently extended to December 31, 1992 to allow the Government additional time to complete disbursements for the technical assistance components. The Credit was followed by a second Financial Sector Adjustment Credit (FINSAC II) for US$100 million equivalent approved by IDA on December 19, 1991.

The PCR was prepared by the Industry and Energy Division (AF4IE) of the (then) Western Africa Department (Evaluation Summary, Parts I and III) and the Borrower (Part II).

Preparation of this PCR was based on the Report and Recommendations of the President, the Development Credit Agreement, Supervision Reports, correspondence between IDA and the Borrower and internal Bank documents.

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## EVALUATION SUMMARY

### Background

1. To arrest the protracted economic decline which started in the 1970s, a new Government in Ghana adopted, in 1983, an Economic Recovery Program (ERP) containing several bold reforms. It devalued the currency, eliminated subsidies, deregulated most price and distribution controls and introduced some necessary fiscal and budgetary measures. The economy's response to the ERP has since been very positive, with economic growth averaging about 5% per year over the period 1984-93. IDA has supported these reforms with three Structural Adjustment Credits (SACs) approved, respectively, in 1988, 1989 and 1991.

### The Financial Sector

2. IDA's work on the Ghanaian financial sector started in 1985, at a time when the latter was in severe distress. This situation represented a serious constraint to growth in the real sectors of the economy which had begun to show promising signs of recovery under the ERP. A major financial sector review was carried out in 1987, which identified a large number of sector deficiencies. These included an insolvent banking system dominated by State-owned banks and saddled with huge non-performing loans and excessive intermediation costs; a low level of financial intermediation reflecting a poor record in domestic resources mobilization; inefficient credit allocation partly on account of Central Bank-directed interest rates and sectoral credit targets; the virtual absence of a money market and capital market, and the weakness of the supervision of the banking system by BOG and the overall inadequacies of the regulatory framework. The above mentioned diagnosis formed the basis for the formulation and adoption of a comprehensive Action Program containing measures aimed at restructuring distressed banks, strengthening the regulatory and supervisory framework, developing financial and capital markets, and more generally, liberalizing the financial sector environment so as to improve the efficiency of resource mobilization and credit allocation. That initial Action Program was supported by the Financial Sector Adjustment Credit (FINSAC I) approved in 1988, and was followed by an enhanced reform program supported by the subsequent FINSAC II approved in 1991.

3. The formal financial system which has grown and diversified in recent years is comprised of the Central Bank, the Bank of Ghana (BOG), six commercial banks, three specialized banks, three merchant banks, a cooperative bank and over 100 rural banks. The six commercial banks, including Ghana Commercial Bank (GCB), Standard Chartered Bank of Ghana (SCB), Barclays Bank of Ghana (Barclays), Social Security Bank (SSB), National Saving and Credit Bank (NSCB) and the recently established Meridien-BIAO of Ghana, have over 80% of the total assets and deposits in the system. GCB continues to dominate the system with over 50% of the assets and deposits of the banking system, but its market share of net loans has declined to about one-third and is expected to decline further with growing competition and the entry of new banks in the market. The three former development finance institutions, Agricultural Development Bank (ADB), National Investment Bank (NIB) and Bank for Housing and Construction (BHC) have introduced commercial banking services. Pending the forthcoming banking divestiture program, most banks are either partly or wholly owned by the Government, although the latter's shareholding in some major banks (e.g., SCB, Barclays) is small and the management of these banks rests entirely with its private shareholders. Two private merchant banks, Ecobank Ghana Ltd. and Continental

Acceptances, were established in 1990. These institutions and the previously existing Merchant Bank, take corporate deposits, finance trade and industry, provide advisory services and manage money and capital market activities such as underwriting, trading on the Stock Exchange, privatization, mergers and acquisitions and debenture issues. There are a number of significant non-bank institutions in Ghana that are not regulated by the Banking Act, but came under the jurisdiction of a separate Non-Bank Financial Institutions Act promulgated recently in 1993. The capital market is in its embryonic stage. A newly formed Stock Exchange commenced trading in November 1990.

**Processing of Credit**

4. The preparation of FINSAC I was preceded by intensive economic and financial sector work. A first financial sector mission, in 1985, identified fundamental problems and recommended a wide-ranging program of reforms, embodied in an Action Program agreed with the Government and subsequently incorporated in the Policy Matrix under FINSAC I. The Initiating Memorandum was approved by the Operations Committee on December 10, 1987, followed immediately, in late February, by appraisal. The Credit was negotiated in April, approved by the Board on May 31 and declared effective on August 11, 1988. The original amount of US$100 million equivalent was subsequently increased to US$106.6 million through a Supplementary IDA Credit. The adjustment program was cofinanced by a loan in Japanese yen equivalent to US$93.9 million from the Overseas Economic Cooperation Fund, and a grant in Swiss Francs equivalent to US$11.8 million by the Government of the Swiss Confederation. The second tranche (US$30 million) was released in June 1990, and the third tranche (US$20 million) in December 1990. The original closing date of September 30, 1990 was subsequently extended to December 31, 1992, to allow additional time for disbursements of the technical assistance component. That significant delay was attributable to the initial over-optimistic estimate of implementation pace, and to the Government's deliberate and, therefore, time-consuming approach to implementing complex reforms, such as bank restructuring.

**Design and Objectives of Program**

5. The financial sector adjustment program supported by FINSAC I was designed to deal selectively, and in priority, with the more fundamental and urgent problems confronting the Ghanaian financial sector back in 1988. These included:

(a) the potential collapse of some major banks which were technically insolvent;

(b) the lack of confidence in the banking system on the part of the public;

(c) the absence of an appropriate regulatory and prudential framework for banking activities; and

(d) the weakness of banking supervision by Bank of Ghana, the central bank.

Consequently, the main objectives of the Credit were to:

(i) liberalize the environment for banking operations through the removal of interest rate controls and sectoral credit targets;

(ii) enhance the soundness of banking institutions by putting in place a new legal, regulatory and prudential framework;

(iii) strengthen the banking supervision function of BOG;

(iv) restructure financially distressed banking institutions following the adoption of a suitable framework and the formulation of institution-specific restructuring plans; and

(v) attempt to recover to the extent possible, the non-performing assets taken over from distressed banks.

In addition, other objectives supported by the Credit included:

(vi) initiating the development of the money and capital market

(vii) initiating a study on the need and modalities for corporate restructuring;

(viii) strengthening the accounting and auditing profession; and

(ix) training of bank managers and staff.

**Implementation Performance**

6. Notwithstanding some delay attributable to the complexity of the reform program (para 4 above), implementation of the Credit has been, generally, highly satisfactory. IDA's satisfaction with the results of FINSAC I led it to approve a follow-on operation, FINSAC II, some three years later, in December 1991. As noted below, each of the specific program objectives, as listed in the preceding paragraph 5, by-and-large, has been satisfactorily achieved:

(e) The ***liberalization of the financial and banking environment*** has now been largely completed, with the removal of ceilings on banking interest rates and other charges, and the abolition of all sectoral credit targets. The more liberal environment has probably been a factor encouraging the recent establishment in Ghana of new banks, of a merchant/investment type. This has resulted in a broadening and diversification of the banking system, enhancing the range of banking services available to enterprises.

(f) The new ***legal and regulatory framework*** for the banking activities introduced by the Amended Banking Law of August 1989 is appropriate. The new legislation provides the banks with a set of prudential regulations to comply with in order to ensure their sound financial operations, and the BOG with the necessary monitoring instruments for exercising its supervisory function over the banks. Furthermore, as of end-1993, all banks operating in Ghana, including the seven State-owned restructured banks (with the exception of the small COOP Bank) are in compliance with major prudential guidelines (e.g., capital adequacy, minimum capital).

(g) The *banking supervision function* of the BOG, previously deficient, has been adequately strengthened. The Banking Supervision Department of BOG has developed its capacity both qualitatively and quantitatively, and by 1993 has been able to comply with the requirement, set out in the 1989 Banking Act, to undertake the inspection of all banks on a yearly basis. BOG's regular and systematic monitoring of the prudential ratios of individual banks has enabled it to ascertain that by 1992 and 1993, all Ghanaian banks, including the seven State-owned banks with the exception of the COOP Bank (slated for merger with a stronger bank) are in compliance with all major prudential regulations, such as capital adequacy, liquidity, minimum capitalization and lending and exposure limits.

(h) The ***bank restructuring program***, a key component of FINSAC I, so far, has generally been implemented successfully. Six of the seven State-owned banks are now operating profitably following their restructuring. They have experienced a steady improvement in their operational efficiency (as reflected in operating ratios) and in the condition of their loan portfolios. The only exception is the relatively small Cooperative Bank, which, up to 1993, has not been included in the Government's banking restructuring program. This bank remains insolvent following its recent receivership by Bank of Ghana, and it is in the process of being merged with one of the stronger State-owned banks. The restored sound financial condition and profitability of these six banks is expected to facilitate their forthcoming privatization, in particular, that of the two largest, namely GCB and SSB, which are scheduled for the initial phase of divestiture under the follow-on FINSAC II. The longer-term sustainability of the restructured banks' good performance, however, remains to be seen as it would depend to a large extent on the eventual outcome of their planned privatization.

(i) In regard to the ***recovery of non-performing assets***, the performance of NPART (the specially created collection agency) to date has been adequate. As of September 30, 1993, it has effectively collected ₵9.0 billion, or 50% of the overall target amount (₵18 billion) but about 95% of the prorated recovery target, which was based on an account-by-account review of its portfolio, and therefore, reflected in a realistic assessment (with the concurrence of IDA staff) of the extent of recoverable assets.

(j) With respect of the development of ***the money and capital market***, a satisfactory, albeit modest, start has also been made. Money market operations are now transacted by two specialized financial institutions, namely Consolidated Discount House which was subject to an institutional strengthening action plan supported by FINSAC I, and the subsequently established Securities Discount Company Limited. Both these are operating profitably and in the process of broadening the range of their operations. In regard to the capital market, the Ghana Stock Exchange, established under and supported by FINSAC I, is providing an infrastructure necessary for the future development of the securities market, although the scale of its operations remains modest.

(k) The study on ***corporate restructuring*** (i.e., restructuring of potentially viable enterprises) was carried out under FINSAC I, although the results of the consultant study are not evident beyond the identification of a number of potentially viable enterprises. Restructuring assistance to the latter was intended to be provided under separate IDA-supported investment project (PEED), although the extent of such assistance to date cannot yet be determined.

(l) The objective of strengthening the ***accounting and auditing professions*** has been pursued systematically, and this has resulted in significant improvements in the institutional capability of the Institute of Chartered Accountants of Ghana (ICAG), and the latter's ongoing work toward the development of a uniform set of accounting standards.

(m) The emphasis on ***training*** and more generally on human resource development under FINSAC I has resulted both in the strengthening of the Ghana Institute of Bankers, an educational institution common to Ghanaian banks, and the professional training of a significant number (260 by 1992) of staff from both BOG and the Ghanaian banks.

7. While implementation performance has been highly satisfactory in terms of the specific program components (e.g., bank restructuring, regulatory framework, banking supervision), there remain areas in the Ghanaian financial sector overall in which further improvements are needed. These include:

(n) the need for the Central Bank to pursue open market operations only to smooth seasonal variations and not be used to fund the Government's overall deficit;

(o) the need to aggressively speed up the divestiture and privatization process of the Government banks to increase the level of competitiveness within the financial sector;

(p) the degree of financial deepening of the economy (M2/GDP), which remains shallow in Ghana, at 17% in 1992;

(q) gross domestic savings, which are low at 2% of GDP in 1992; and

(r) private sector credits were 4.6% of GDP in 1992.

**Sustainability**

8. The sustainability of the reforms and actions undertaken under FINSAC I derives, amongst other things, from the fact that the reform program was not conceived of as a one-shot undertaking. Rather, it was designed as the first phase of a continuing sectoral adjustment process. In line with that thinking, some three years after its inception (in 1988) and following its successful implementation, FINSAC I was followed by the subsequent FINSAC II approved by IDA in December 1991. Apart from introducing additional sector reforms (e.g., privatization of restructured banks, non-bank financial institutions; improvements in monetary control), FINSAC II included the explicit objective of helping

Ghana ***consolidate*** those reforms already initiated under the preceding FINSAC I. Thus, the bank restructuring program started under FINSAC I continues to receive IDA's support under FINSAC II toward the forthcoming provatization of most of the restructured parastatal banks. In regard to the recovery of non-performing assets, the preparatory and legal work toward establishing NPART started under FINSAC I, but NPART actually started its operations under FINSAC II. The extensive institution - building and training programs (e.g., Institute of Chartered Accountants, Ghana Institute of Bankers) initiated under FINSAC I continue to this day to receive support under FINSAC II. This continuum between these two successive operations goes a long way in ensuring the sustabability of reforms and action undertaken under the initial program. Apart from the foregoing, the sustainability of reforms is enhanced by the Government's continuing strong commitment to the reform process. To further ensure sustainability, it would be advisable for IDA and other Donors to be prepared to continue providing technical assistance (e.g., logistical support, training) on a gradually diminishing scale over the next few years to selected program implementation agencies (e.g., BOG, ICAG, GSE, Institute of Bankers).

**Lessons**

9. The main lessons drawn from FINSAC I implementation are:

(s) intensive economic and sector work preceding preparation/appraisal of a financial sector adjustment operation helps expedite its processing without sacrificing quality;

(t) a financial sector adjustment operation stands a better chance of success when it is implemented in the aftermath and in the broader context of a broader macroeconomic adjustment program;

(u) it would have been useful to have a pre-established set of financial sector performance indicators (e.g., financial savings, private sector credit, portfolio classification of banking sysxtem), as a built-in device for periodically monitoring sector performance during program implementation;

(v) in parallel with IDA's assistance for restructuring seven State-owned distressed banks, it would have been appropriate from the outset to press for a more forceful rationalization of these banks (i.e., a reduction in their number) through mergers and/or liquidations;

(w) it may be operationally useful to undertake a cross-country comparative review of the relative effectiveness of the alternative modalities for recovering the non-performing assets of distressed or failed banks; and

(x) the important role of technical assistance in implementing this financial sector adjustment program.

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## I. PROJECT REVIEW FROM THE BANK'S PERSPECTIVE

### 1. Project Identity

| | |
|---|---|
| NAME: | Financial Sector Adjustment Credit I (FINSAC I) |
| CREDIT NUMBER: | 1911-GH |
| RVP UNIT: | AFR Region |
| COUNTRY: | Ghana |
| TYPE OF LOAN: | Sector Adjustment Loan |

### 2. Background

#### a. The Economy

2.1 Ghana once enjoyed a relatively high standard of living compared with other West African countries, but poor economic management during the 1970s and the early 1980s led to a protracted economic decline. Expansionary fiscal and monetary policies caused inflation to accelerate. This, together with a fixed nominal exchange rate caused a substantial real appreciation of the currency, leading to external payments imbalances and encouraging policy makers to impose a range of administrative controls on prices, imports, foreign exchange use and the distribution of goods and services. The cumulative effect of these developments precipitated a downward economic spiral from 1970 to 1982, with Gross Domestic Product (GDP) declines of -2% per annum.

2.2 In 1983, the new Government adopted an Economic Recovery Program (ERP) and introduced several bold measures. It devalued the currency, dismantled most price and distribution controls, eliminated subsidies, raised taxes selectively, improved tax collection and provided more adequately for maintenance and capital expenditure. Despite infrastructure bottlenecks, delays in aid flows and the temporary but crippling drought of 1983, the economy's response to the ERP was almost immediate. Economic growth has averaged about 5% a year over the period 1984-92.

#### b. The Financial Sector

2.3 The formal financial system which has grown and diversified in recent years is comprised of the central bank, the Bank of Ghana (BOG), six commercial banks, three specialized banks, three merchant banks, a cooperative bank and over 100 rural banks. The six commercial banks, including Ghana Commercial Bank (GCB), Standard Chartered Bank of Ghana (SCB), Barclays Bank of Ghana (Barclays), Social Security Bank (SSB), National Saving and Credit Bank (NSCB) and the recently established Meridien-BIAO of Ghana, have over 80% of the total assets and deposits in the system. GCB continues to dominate the system with over 50% of the assets and deposits of the banking system, but the GCB market share of net loans has declined to about one-third and is expected to decline further with growing competition and the entry of new banks in the market. The three former development finance institutions, Agricultural Development Bank (ADB), National Investment

Bank (NIB) and Bank for Housing and Construction (BHC) have introduced commercial banking services. Pending the forthcoming banking divestiture program, the majority of the banks are either partly or wholly owned by the Government, although the latter's shareholding in some major banks (e.g., SCB, Barclays) is small and the management of these banks rests entirely with its private shareholders. Two private merchant banks, Ecobank Ghana Ltd. and Continental Acceptances, were established in 1990. These institutions and the existing Merchant Bank, take corporate deposits, finance trade and industry, provide advisory services and manage money and capital market activities such as underwriting, trading on the Stock Exchange, privatization, mergers and acquisitions and debenture issues. The three merchant banks have about 7% of the total assets and 5% of the deposits in the system.

2.4 There are a number of significant non-bank financial institutions in Ghana that are not regulated by the Banking Act. The non-bank financial system is comprised of a Stock Exchange, 21 life and non-life insurance companies with some 3,000 insurance brokers and agents, the Social Security and National Insurance Trust (SSNIT), two discount houses, building societies and a leasing company. Several non-bank financial institutions, life insurance companies and pension/provident funds in particular, are potential sources of long-term investment capital. The follow-on FINSAC II (para 2.10) included among its objectives the establishment of a new legal and regulatory framework for these non-bank financial institutions.

2.5 The capital market is in its embryonic stage, as yet unable to make a substantial contribution to the mobilization of long-term resources. Until very recently, the few private placement transactions were usually in long dated Government stocks and shares of private companies. A newly formed Stock Exchange commenced trading in November 1990. Trading volume is still small, with few listed securities. However, the volume is expected to grow with the divestiture and privatization initiatives being pursued by the Government.

2.6 IDA's work on the Ghanaian financial sector started in 1985, at a time when the latter was in severe distress. This situation represented a serious constraint to growth in the real sectors of the economy which had begun to show promising signs of recovery under the ERP launched by the Government in 1983. A major financial sector review was carried out in 1987, which identified a large number of sector deficiencies. These included an insolvent banking system dominated by State-owned banks and saddled with huge non-performing loans and excessive intermediation costs; a low level of financial intermediation reflecting a poor record in domestic resources mobilization; inefficient credit allocation partly on account of Central Bank-directed interest rates and sectoral credit targets; the virtual absence of a money market and capital market; and the weakness of the supervision of the banking system by BOG and the overall inadequacies of the regulatory framework. The above-mentioned diagnosis formed the basis for the formulation and adoption of a comprehensive Action Program containing measures aimed at restructuring distressed banks, strengthening the regulatory and supervisory framework, developing financial and capital markets, and more generally, liberalizing the financial sector environment so as to improve the efficiency of resource mobilization and credit allocation. That initial Action Program was supported by FINSAC I, and was followed by an enhanced sectoral reform program supported by the subsequent FINSAC II.

## 3. Project Objectives, Design, Preparation and Execution

### a. Objectives

2.7 The FINSAC reform program was intended to complement the structural adjustment program initiated by the Government in 1983. The latter aimed at establishing an appropriate macroeconomic and incentive framework to stimulate growth, encourage savings and investment, strengthen the balance of payments and improve the efficiency of resource use while ensuring fiscal and monetary stability. The ***main objectives*** of the Credit were to:

(i) liberalize the environment for banking operations through the removal of interest rate controls and sectoral credit targets;

(ii) enhance the soundness of banking institutions by putting in place a new legal, regulatory and prudential framework;

(iii) strengthen the banking supervision function of BOG;

(iv) restructure financially distressed banking institutions following the adoption of a suitable framework and the formulation of institution-specific restructuring plans; and

(v) attempt to recover to the extent possible, the non-performing assets taken over from distressed banks;

2.8 In addition, ***other objectives*** supported by the Credit included:

(i) initiating the development of the money and capital market;

(ii) initiating a study on the need and modalities for corporate restructuring;

(iii) strengthening the accounting and auditing profession; and

(iv) training of bank managers and staff.

### b. Design and Phasing of Reforms

2.9 The reform program supported by FINSAC I was appropriately designed, with due consideration given to the need to deal with urgent and/or priority matters first, and to the borrower's implementation capacity. It was intended to focus selectively on the more fundamental and urgent problems facing the Ghanaian financial sector back in 1988. These included: (a) the potential collapse of the major, insolvent banking institutions; (b) the lack of confidence in the banking system on the part of the public; (c) the absence of an appropriate regulatory and prudential framework for banking operations; and (d) the weakness of banking supervision by the BOG. Accordingly, this initial reform program excluded from its scope a number of financial sector issues which, although important, were deemed less urgent, such as: (e)non-bank financial institutions; (f) the informal financial markets, notwithstanding their relative prominence in Ghana; (g) the legal framework (e.g., bankruptcy laws, laws on

collaterals and securities, judicial system concerning the enforcement of financial contracts) relating to banking operations; and (h) improvement in the modalities for monetary control.

2.10 Although the restructuring of distressed, State-owned banks constituted a key component of FINSAC I, their eventual privatization was not envisaged as part of the initial reform program, on the justifiable grounds that there was a need first to restore these banks' financial viability as a pre-requisite for their subsequent privatization. Most of the objectives thus left out of the initial reform program of FINSAC I (including banking privatization, non-bank financial institutions, the informal financial system, and improvement in the monetary control system) were pursued in the follow-on operation, FINSAC II, which was approved in December 1991, approximately three years after FINSAC I. Accordingly, FINSAC I should be seen not as a comprehensive, once-and-for-all attempt at adjustment of the Ghanaian financial sector, but as the first phase of a sector adjustment process that is still ongoing. In recognition of the need for capacity building, the FINSAC I program included a sizeable technical assistance component amounting to US$5 million (supplemented by cofinancing from Switzerland), for training, consultancy services and other implementation-related hardware and software expenditures.

### c. Project Preparation

2.11 The preparation of FINSAC I stemmed directly from IDA's financial sector work in Ghana. A preliminary sector mission visited the country in 1985, as the adjustment process was underway, when it appeared that shortcomings in the financial sector constituted a potential constraint to growth in the real sectors. This culminated in April 1987 in a major review by a joint working group of Ghanaians and IDA staff which identified fundamental problems and recommended a wide-ranging program of reforms, embodied in an Action Program that was discussed and substantially agreed with the Government. The priority measures contained in the Action Program were subsequently incorporated in the Policy Matrix (Annex A) agreed under FINSAC I. The Initiating Memorandum was reviewed and approved by the Operations Committee in February 1988, followed immediately by appraisal. The Credit was negotiated in April, approved by the Board on May 31 and declared effective in August 1988. That expeditious processing schedule was made possible, without sacrificing quality, by the intensive sector work preceding appraisal. The original amount of SDR72.1 million (US$100 million) was subsequently increased to SDR77.2 million (US$106.6 million) through a Supplementary IDA Credit for SDR5.1 million. The adjustment program was cofinanced by a loan of Japanese Yen, 12.558 billion (US$93.9 million equivalent) from the Overseas Economic Cooperation Fund of Japan and a grant of Swiss Francs 15 million (US$ 11.8 million equivalent) by the Government of the Swiss Confederation, with IDA acting as Administrator of the Swiss contribution. The second tranche (of US$30 million) was released in June 1990, about 17 months after effectiveness compared with the 9-month interval anticipated in the President's Report. This significant delay appears attributable to the large number (10 in all) of specific conditions stipulated for the second tranche release and the over-optimistic initial estimate of their implementation pace. On the other hand, the third tranche (US$20 million) was released in December 1990, or 6 months after the second tranche compared with the initially envisaged 9-month interval. This early release of the third tranche was probably on account of the fewer conditions (5) attached to it.

## 4. Implementation Performance

### a. Liberalization of Financial and Banking Environment

2.12 The process of gradual liberalization and deregulation of the financial system actually started before the inception of the Credit and was substantially completed under it. The objective was to improve the mobilization and allocation of financial resources and to increase financial intermediation. Control of interest rates was gradually removed and full interest rate liberalization was achieved in February 1988. With inflation declining in the mid-1980s, deposit rates became positive in real terms for the first time in more than a decade, although in later years, fluctuating inflation rendered them negative from time-to-time. In compliance with a specific agreement under the Credit, BOG also started decontrolling all banking charges (e.g., fees and commissions) in October 1990. On the side of resource allocation, all sectoral credit targets were gradually phased out starting in 1987, except for agriculture, for which the lending floor was abolished in November 1990 in compliance with a condition for third tranche release.

### b. The Legal and Regulatory Framework

2.13 Preparation work for the program disclosed that the then prevailing Banking Act of 1970 did not provide adequate guidelines to banks and the banking authorities on, inter alia, minimum capital requirements, risk exposure and prudential lending limits for banks, provisions for possible loan losses and methods of interest accrual on non-performing loans. Accordingly, the Government undertook a comprehensive examination of the Act during 1988 with a view to establishing a more effective basis for banking activity in the country. As a result, an interim Legislative Instrument was enacted on December 30, 1988. It covered minimum capital requirements, provided a new basis for computing capital adequacy, introduced uniform accounting and auditing standards and improved reporting requirements to the BOG, for all banks and future banking activities. Subsequently, the authorities continued to develop a comprehensive legal and regulatory framework for banking activities through extensive consultations with banking, accounting and other professional bodies in Ghana and abroad, as well as with the Association. This process resulted in the enactment of the Amended Banking Law on August 8, 1989, replacing both the Banking Act of 1970 and the Banking and Financial Institutions Decree of 1979. The new Act and its regulations provide sound prudential and regulatory bases for the country's banking system. It contains an appropriate set of prudential banking provisions, broadly patterned upon those of the Basle Guidelines, it requires banks to maintain a minimum capital base equivalent to 6% of asset base adjusted for risk assets, and to limit secondary capital. It sets penalties, including restrictions on dividend payments, for banks that do not achieve their capital adequacy ratios. Guidelines are provided for determining provisions for bad and doubtful loans and for the treatment of related accrued interest. The Act also establishes for banks risk exposure limits to a single financial group or individual as a percentage of net worth, and sets limits on loans and advances to directors and employees of banks. It also contains restrictions on the extent of direct exposure in commercial, agricultural and industrial and real estate activities. The provisions of the new Act considerably strengthen the BOG's ability to effectively manage and oversee the banking sector. The BOG is empowered when necessary, to require banks to hold specified levels of liquid assets, direct banks to observe specified lending policies and take remedial measures (including receivership), if banks are not being managed in the interest of their depositors and/or creditors.

### c. Bank Supervision by Bank of Ghana

2.14 In parallel with the putting in place of a new legal and regulatory framework for banking activities, a major specific objective of FINSAC I was to strengthen banking supervision by the BOG, which previously was considered deficient. Under the new Banking Act, BOG was required to undertake the on-site inspection of each bank at least once a year. Standard auditing and accounting principles were introduced in late 1988 which follow International Auditing Guidelines and International Accounting Standards. Since then, the accounting records of banks must be examined by qualified external auditors at least once a year, and both statutory and long-form auditors' reports are required for all banks. These reports are also to be submitted to the BOG promptly. These revised standards and procedures are now being enforced by the BOG's Banking Supervision Department. The reporting format introduced by the Bank of Ghana in 1988 require banks to provide considerably more data than was being submitted previously for off-site monitoring purposes. Besides data on their liquidity and the volume and nature of credit granted, banks are now regularly providing information on the composition and maturity of all their assets and liabilities, the quality of portfolios, their profitability and information that permits the calculation of their capital adequacy ratios. The BOG's Banking Supervision Department has started to computerize this database and its operations in order to monitor more effectively the performance of banks individually and in relation to the sector.

2.15 Until 1988, the Banking Supervision Department carried out few on-site inspections of banks and relied mainly on each bank's internal control mechanisms and on external auditors' reports to analyze and assess bank performance. Reporting requirements from banks were chiefly concerned with monitoring liquidity and compliance with credit allocation guidelines. To cope with the supervisory responsibilities under the new Act, the Supervision Department has been strengthened significantly. Two high-level advisors from the Reserve Bank of India were retained to provide formal as well as on-the-job training to staff working on bank supervision; all the Department's bank inspectors have now participated in a basic training course and manuals for both on-site and off-site inspection have been substantially revised and expanded. Regular on-site inspections of banks were initiated in early 1989 with the direct participation of the advisors, and the quality of the resulting reports has improved considerably. To cope with the requirement of annual on-site inspection of each bank, the Department has gradually built up its staffing, from 20 bank examiners in 1988 (of whom only five were considered as having suitable experience) to 63 examiners (with adequate field experience) by 1993.

### d. The Restructuring of Distressed Banks

2.16 Under FINSAC I, the approach to bank restructuring was quite systematic. The Government's Statement of Financial Policies, agreed with IDA, provided the basis of the framework for the restructuring of banks. The main guiding principles were that: (i) the basic objective of bank restructuring was to foster the growth of a sound, dynamic banking system in which all banks, irrespective of ownership and purpose, will compete freely and operate by rules of the market; (ii) pending the completion of bank restructuring, measures will be taken to arrest the financial deterioration of banks; (iii) to ensure the proper use of resources in the future and avoid the repetition of past mistakes, financial restructuring will not be attempted in isolation from managerial and organizational changes; (iv) restructured banks were to have independent and professional managements with sufficient autonomy to make day-to-day decisions, and the boards of directors are to include suitable representation

from the private sector to broaden the experience and enhance their capabilities and contribution and; (v) the Government will consider reducing its share of the ownership of banks by seeking private Ghanaian and/or foreign shareholding in restructured banks. In addition, subject to proper safeguards, entry into the banking system of new privately owned domestic or foreign banks will be encouraged. The Government retained a firm of consultants to help develop a framework for restructuring seven of the nine major banks. The guidelines for restructuring distressed banks were formulated and elaborated in the General Framework document in early 1989. It was approved by the Government in July 1989, and reviewed and agreed by the Association. The framework established a one-time financial package of measures for each of the seven distressed banks to restore solvency, and to provide sufficient capital and adequate liquidity to enable them to operate in a self-sustained manner following their restructuring. The measures were tailored to the requirements of individual banks and the degree and kind of distress experienced by them. Restructuring was achieved by removing from the banks' portfolios all non-performing loans made to the Government or to State-owned enterprises, which totalled ₵22.6 billion at the end of 1988, and to the extent needed, converting into equity Government loans or other claims (deposits). The banks' non-performing loans to the private sector amounting to about ₵36.4 billion at the end of 1988 were to be replaced through the issuance of Government bonds. The non-performing assets of distressed banks were to be transferred to a newly created and wholly-owned Government agency, the Non-Performing Assets Recovery Trust (NPART), whose function would be to realize such assets to the extent possible. To facilitate NPART's work, a special judiciary tribunal was appointed and given the necessary powers to speed up the asset recovery process.

2.17 Implementation of the bank restructuring program to date has been generally satisfactory. Individual restructuring plans for six of the seven distressed banks, following their review by IDA, are under implementation and have resulted in significant improvements in both the financial and operational performance of five of these banks (GCB, SSB, NIB, ADB, NSCB), since 1991. These restructuring plans included changes in the banks' management team, staff reduction, closure of unprofitable branches and reduction of operating costs. For the seven restructured banks, the combined work force has been streamlined by 35% to about 7,000 by end-1992. 2 presents the financial statements of these banks, and 3 their loan portfolio classification. Their ratio of operating expenses to operating income improved from 64% in 1990 to 53% in 1992 and further to 45% in 1993 (first nine months). Starting with a loss situation in 1990, these banks recorded a combined profit (before tax) of ₵9.9 billion in 1991, and ₵10.4 billion in 1992, and ₵22.3 billion in 1993 (first 9 months) thus enabling the Government to derive a tax revenue of ₵13.9 billion for these three years. More importantly, the combined loan portfolio of the restructured banks continues to show improvement. As shown in 6, the ratio of non-performing loans to total portfolio steadily declined from 72.5% in 1989, to 60.6% in 1990, 40.6% in 1991, 32.8% in 1992 and further to 28.5% as of end-September 1993. One of the seven banks, BHC, however, continues to be in need of further improvement, particularly in its management team. Finally, the small COOP Bank remains in a precarious condition. It has recently been taken over by BOG and is to be merged with a stronger bank following its forthcoming financial restructuring. The satisfactory outcome of the restructuring of GCB and SSB, which are the two largest Ghanaian banks and candidates for the initial phase of the Government's banking divestiture program, is expected to facilitate their planned privatization.

e. **Recovery of Non-Performing Assets**

2.18 In early 1989, during the course of drafting the General Framework (i.e., guidelines) for bank restructuring (para. 2.16), extensive technical discussions took place between the Government, IDA and the consultants on the alternative modalities for recovering the non-performing assets of the seven distressed banks which were slated for restructuring. On the basis of detailed portfolio audits previously undertaken by independent experts, the aggregate amount of these non-performing assets was estimated at approximately ₵60 billion. The need was felt to attempt to recover as much of this amount as possible in order to reduce the fiscal burden of the Government. These discussions led to the conclusion that the best modality would be the establishment of NPART (para. 2.16), as a Government-owned agency whose function would be to take over and to realize such assets to the extent possible. In February 1990, agreement was reached between the Government and IDA on a document titled, "NPART Operating Policies", which outlined in considerable detail the financial and operational guidelines for this institution as well as its organizational structure. The law establishing NPART was enacted on February 28, 1990 and NPART became operational later that year. From its inception, NPART has received extensive technical assistance from IDA, mainly for financing a team of expatriate experts, two of whom had previous relevant experience with the Resolution Trust Corporation (RTC) of the U.S. The special judicial tribunal, created to facilitate NPART's recoveries, was subsequently established and became operational by June 1992.

2.19 Taking into account the six-year timeframe set in the 1990 law establishing NPART (including a built-in one-year extension), the Government and IDA agreed in 1991 on an action program to achieve an appropriate level of debt recoveries by NPART. The action program set an Aggregate Recovery Target (ART) of ₵18 billion (compared with a total portfolio of about ₵50 billion), based on an account-by-account review of its portfolio by NPART. This target amount was to be recovered by NPART in accordance with annual recovery targets: 12% in 1991, 22% in 1992, 26% in 1993, 23% in 1994 and the remaining 17% in 1995. NPART's actual collection performance to date by and large has been adequate in relation to the agreed recovery targets. It collected ₵3.3 billion in 1991, ₵3.4 billion in 1992 and ₵2.3 billion in the first nine months of 1993, for a total amount of ₵9.0 billion, or about 95% of the prorated target amount of ₵9.6 billion (for the period from 1991 up to September 30, 1993). There are, however, some indications that future recoveries might be more difficult to achieve than in the past, on account of the fact that collections in the early phase tended to concentrate on the easier accounts. The special tribunal became operational by mid-1992 and NPART has so far submitted to it 150 cases (involving ₵9.8 billion) for evaluation, of which the tribunal has rendered 96 judgements (involving ₵8.9 billion) in favor of NPART. The extent to which the tribunal might have actually helped expedite NPART's recovery process, however, remains unclear.

f. **Development of Money and Capital Markets**

2.20 Specific measures to achieve the above objective under FINSAC I included: (a) preparation and implementation of an action plan for strengthening the Consolidated Discount House (CDH), a newly established money market company with which banks could invest their surplus short-term resources; and (b) completion of a study on the potential and modalities for capital market development. It was hoped that the availability of short- and medium-term securities on an active money market would, apart from increasing resource mobilization, enable the BOG to improve its instruments of monetary control by gradually

moving away from direct controls (i.e., credit ceilings) toward an indirect system based mainly on open market operations. Following agreement with IDA in 1989 on an institutional strengthening program, CDH has continued to expand its business and to operate profitably. Its successful operation encouraged the establishment, in 1990, of a second discount house, the Securities Discount Company, Limited. The capital market study, completed in October 1989, led to the establishment of the Ghana Stock Exchange (GSE) in 1990. GSE has made commendable efforts to build up a minimal organizational structure and the requisite basic operational capacity and procedures. The level of its operations to date, however, remains extremely modest, increasing from a negligible trading volume of ₵105 million in 1991, to ₵173 million in 1992 and ₵2,892 million for the first nine months of 1993. There are only 15 companies listed as of end-1993 and only one new listing (Super Paper Company) since 1992. This disappointing operational performance is attributable mainly to the smallness of the market and to the fact that it takes time for the Ghanaian public to become familiar with securities transactions. In the coming months and years, however, a significant increase in business as well as in the role of GSE is anticipated with the forthcoming government divestiture program including the planned privatization of banks (para. 2.17). A much increased level of business will be necessary for GSE which, so far, has had to rely on IDA's technical assistance financing under FINSAC I, to start operating in a financially self-supporting manner and thus to ensure its long-term sustainability. In view of its potentially important role, GSE is an institution worth preserving and supporting.

### g. Corporate Restructuring

2.21 During FINSAC I preparation, the Government and IDA shared the view that banking restructuring, in order to be successful on a sustained basis, would need to be complemented by the restructuring of enterprises in the corporate sector. The financial situation of these enterprises had been severely adversely affected during the 1980s by massive devaluations, high rates of inflation and natural shocks resulting from necessary adjustment policies. The impaired capacity of such enterprises to service their banking debts in turn led to the heavy accumulation of non-performing assets in the books of Ghanaian banks and in the latters' financial distress. In recognition of the foregoing, the Government commissioned under FINSAC I, a study to assess the magnitude and nature of corporate distress, and to recommend a program to facilitate the restructuring of potentially viable enterprises. The study was carried out by an external consulting firm, M.S.A. of UK, and subsequently followed in 1992 by an updating study by Repim, a local consulting company. The first phase of the study was completed in late 1989 and reviewed the condition of a sample of 214 enterprises identified by Ghanaian banks as possible candidates for restructuring. It concluded that a significant proportion of these enterprises had good prospects for viable operation, if suitably restructured from a financial, technical and managerial standpoint. The second phase of the study, completed in mid-1990, examined the alternative institutional arrangements for carrying out the enterprise restructuring process. It proposed, inter alia, the establishment of a new corporate entity with private sector ownership to provide venture capital and other financial, managerial and technical services for the restructuring of distressed but potentially viable enterprises, together with a broad range of activities pertaining to a specialized financial institution, along the lines of an investment bank. That proposal, however, was subsequently abandoned by the Government, partly on account of practical difficulties in finding a group of suitable private investors with both a willingness and a capability to set up a new investment bank that would concentrate on restructuring distressed corporate enterprises. During discussions with the Government, IDA also expressed its reservations about that proposal, out of concern that the new corporate

entity (in which the Government would inevitably have to play a major role, at least in its initial stages) might be inappropriately used to bail out fundamentally non-viable enterprises, and in view of the fact that two new private merchant banks (Ecobank Ghana and Continental Acceptances) just opened in 1990 in Ghana, in addition to the previously existing Merchant Bank.The recommendations from the consultant report were subsequently revisited under a 1993 IDA investment project, the Private Enterprise and Export Development Project (PEED). It was concluded that, under PEED, a small pilot program focussing on 10-20 potentially viable companies would be developed and specific restructuring action plans developed in conjunction with local financial consulting firms.

### h. Strengthening the Accounting and Auditing Profession

2.22 Measures to improve the accounting and auditing professions were included under the program, and a comprehensive review by consultants of the training and professional development needs of the accountancy profession was completed in early 1989. The consultants' report made recommendations on, inter alia, reforming the regulatory framework for accounting and auditing, developing professional standards, improving training and professional development of accountants and strengthening the previously existing Institute of Chartered Accountants of Ghana (ICAG). With IDA's technical assistance under FINSAC I, ICAG has generally made good progress in implementing the consultants' recommendations, including reorganizing its Secretariat and ongoing work toward developing a uniform set of accounting standards. Furthermore, ICAG has succeeded in the past three years in gradually reducing its dependence on outside financial support (from FINSAC technical assistance and the Government) and increasing its own revenues, thereby enhancing its long-term sustainability. The ratio of its self-generated income (e.g., membership contributions and fees, other remunerations) increased from 12% in 1991 to 25% in 1992 and sharply to 73.5% in 1993 (first nine months).

### i. Training of Bankers

2.23 The need to introduce modern banking methods, upgrade the skills of bank staff and recruit and develop new talent was recognized during preparation of the program. Accordingly, the technical assistance component of FINSAC I included measures to assist both BOG and the Ghana Institute of Bankers. Under this assistance, BOG recruited a senior training specialist (from the Reserve Bank of India) who, at the end of 1989, completed an assessment of the training needs of the banking sector, and formulated training programs and course curricula. Simultaneously, training courses for staff of both BOG and the commercial banks (numbering 260) were conducted by external training experts in credit management, international banking, internal auditing and other core disciplines. In parallel, the Ghana Institute of Bankers (an educational institution affiliated with the Ghana Association of Bankers) received technical assistance under FINSAC I for upgrading its physical facilities and for funding of trainers' training by external training specialists. The Ghana Institute of Bankers appears to have made good progress toward developing its own expertise (notably in conducting professional examinations), and has lessened its previously heavy professional dependence on the London-based Chartered Institute of Bankers, U.K. The Institute now has some 3,500 students studying for its various levels of certification. This good progress notwithstanding, there is a need for the Institute to further ensure its long-term sustainability, in anticipation of an eventual reduction or discontinuation of external financial support from IDA and other sources, by generating a more adequate level of revenues from its services.

2.24 The technical assistance component of FINSAC I also provided financial support to the Ghana Association of Bankers toward the establishment of a Credit Clearing House (subsequently, renamed the Interbank Credit Data Bank). The objective was to develop a centralized and computerized data system on credits (above a given level) granted by all Ghanaian banks to all borrowers, so as to improve credit information and the transparency of credit risks, and to enable the banks to obtain accurate and up-to-date information on clients' indebtedness and, thus, to improve the quality of their lending decisions. Implementation of this proposal has been delayed, so far, partly on account of the Ghana Association of Bankers' ineffectiveness, but is expected to be completed sometime during 1994 under funding from FINSAC II.

## 5. Project Results and Sustainability

### a. Results in Regard to Specific Program Components on Financial Sector Overall

2.25 It is clear from the foregoing that, to a large extent, all the nine ***specific components*** of FINSAC I listed in paragraphs 2.7 and 2.8 have been implemented satisfactorily, as summarized below:

(i) The ***liberalization of the financial and banking environment*** has now been largely completed, with the removal of ceilings on banking interest rates and other charges, and the abolition of all sectoral credit targets. The more liberal environment has probably been a factor encouraging the recent establishment in Ghana of new banks, of a merchant/investment type, such as Merchant Bank of Ghana, Continental Acceptances Ltd. and Ecobank Ghana. This has resulted in a broadening and diversification of the banking system, enhancing the range of banking services available to enterprises.

(ii) The new ***legal and regulatory framework*** for banking activities introduced by the Amended Banking Law of August 1989 is adequate. One (relatively minor) area for further improvement in existing regulations relates to weighting of assets for the computation of capital adequacy: at present, banks are subject to only two categories of weighting - zero percent or 100 percent - whereas a more graduated scale of weighting similar to the Basle guidelines would assist the banks in the diversification of lending instruments. The foregoing notwithstanding, the new legislation does provide the banks with a set of appropriate prudential regulations to comply with in order to ensure their sound financial operations, and the Bank of Ghana with the necessary instruments for exercising its supervisory function over the banks. Furthermore (see para 5.1(c)), as of end-1993, all banks operating in Ghana, including the seven state-owned restructured banks (with the exception of the small COOP Bank) are in compliance with major prudential guidelines (e.g., capital adequacy, minimum capital). While it is true that the 1989 Amended Banking Act covered only banking institutions per se, thus leaving the non-bank financial institutions (NBFIs) largely unregulated until the Financial Institutions (Non-Banking) Law was promulgated in January 1993, this reflected a

deliberate (and justifiable) decision to address the NBFI situation under the second phase of reforms supported by FINSAC II.

(iii) The ***banking supervision function*** of the Bank of Ghana, previously deficient, has been adequately strengthened. The Banking Supervision Department of BOG has developed its capacity both qualitatively and quantitatively, and by 1993 has been able to comply with the requirement, set out in the 1989 Banking Act, to undertake the inspection of all banks on an yearly basis. BOG's regular and systematic monitoring of the prudential ratios of individual banks has enabled it to ascertain that by 1992 and 1993, all Ghanaian banks, including the seven state-owned banks with the exception of the COOP Bank (slated for merger with a stronger bank) are in compliance with all major prudential regulations, such as capital adequacy, liquidity, minimum capitalization and lending and exposure limits.

(iv) The ***bank restructuring program***, a key component of FINSAC I, so far, has generally been implemented successfully. As indicated in para 4.6, as a group, the seven state-owned banks are now operating profitably following their restructuring. They have experienced a steady improvement in their operational efficiency (as reflected in operating ratios) and in the condition of their loan portfolios. The only exception is the relatively small Cooperative Bank whose financial restructuring commenced in December 1993. This bank remains insolvent following its recent receivership by Bank of Ghana. It is intended to merge it with one of the stronger State-owned banks. This bank remains insolvent following its recent receivership by Bank of Ghana, and it is in the process of being merged with one of the stronger state-owned banks. The restored sound financial condition and profitability of these six banks is expected to facilitate their forthcoming privatization, in particular that of the two largest, namely GCB and SSB, which are scheduled for the initial phase of divestiture under the follow-on FINSAC II. The sustainability of the restructured banks' good performance, however, remains to be seen as it would depend to a large extent on the eventual outcome of their planned privatization.

(v) In regard to the ***recovery of non-performing assets***, the performance of NPART to date has been generally adequate. As indicated in para 4.8, up to September 30, 1993, it has effectively collected ₵9.0 billion or about 95% of the ***prorated*** recovery target, which itself was based on an account-by-account review of its portfolio and, therefore, reflected a realistic assessment (with the concurrence of IDA staff) of the extent of recoverable assets.

(vi) With respect of the development of ***the money and capital market***, a satisfactory albeit modest start has also been made. Money market operations are now transacted by two specialized financial institutions, namely Consolidated Discount House which was subject to an institutional strengthening action plan supported by FINSAC I, and the

subsequently established Securities Discount Company, Limited. Both these are operating profitably and in the process of broadening the range of their operations. In regard to the capital market, the Ghana Stock Exchange, an entity established under and supported by FINSAC I, is providing an infrastructure necessary for the future development of the securities market, although the scale of its operations remains modest.

(vii) The ideas of ***corporate restructuring*** (i.e., restructuring of distressed but potentially viable enterprises) was explored under FINSAC I, although the results of the consultant study are not evident beyond the identification of a number of potentially viable enterprises. Restructuring assistance to the latter was intended to be provided under a separate IDA-supported investment project (PEED), although the extent of such assistance to date cannot yet be determined.

(viii) The objective of strengthening the ***accounting and auditing professions*** has been pursued systematically, and this has resulted in improvements in the institutional capability of the ICAG, and progress is being made towards the development by the latter of a uniform set of accounting standards.

(ix) The emphasis on ***training*** and more generally on human resource development under FINSAC I has resulted both in the strengthening of the Ghana Institute of Bankers, an educational institution common to Ghanaian banks, and the professional training of a significant number (260 by 1992) of staff from both BOG and the Ghanaian banks.

**b. Impact on Financial Sector Overall**

2.26 As can be seen from the preceding paragraph, implementation of the FINSAC I reform program has been generally successful in regard to its specific components/objectives. On the other hand and on a broader plane, it is more difficult to assess the impact of FINSAC I on the ***performance of the financial sector overall***. For one reason, financial sector performance (e.g., savings mobilization, resource allocation, efficiency of financial intermediation) depends not only on reforms within the sector, but also on the broader macroeconomic environment. This makes it difficult to separate the effects of FINSAC I from those of the successive structural adjustment programs undertaken in Ghana since 1983. For another, the reform program of FINSAC I cannot be seen as a whole, but only as the first phase of a continuing sector adjustment process that includes also the follow-on FINSAC II (and probably some future operations). This being said, the following is an attempt at identifying sectoral improvements since the inception of FINSAC I, as well as those areas where further improvements should be sought.

2.27 Selected areas where the Ghanaian financial sector has experienced ***improvements*** following the implementation of FINSAC I include notably:

(i) The resolution of banking distress and restoration of financial soundness in the banking system, as a result of the bank restructuring program initiated in 1989. The improvements in the situation of the

state-owned banks (see para 2.17) since 1990 have also been experienced by the Ghanaian banking system overall. Whereas in 1988 seven of the nine banks operating in Ghana were insolvent, at present all but one (COOP Bank, taken over by BOG and in the process of being merged with a stronger bank) of the 14 banks in the system are operating profitably and in compliance with prevailing prudential regulations. The table in 6 shows that for the 3-year period, these banks as a group recorded an average annual profit (before tax) of ₵22.2 billion, representing 3.4% of average total assets and 27.5% of equity. Operating efficiency is reflected in the ratio of operating expenses to average total assets, and these have registered a modest decline from 4.3% in 1990 to 4.1% for the first nine months of 1993. More importantly, improved quality of their combined loan portfolio is reflected in the ratio of non-performing loans to total portfolio, which declined from 60.6% in 1990 to 40.6% in 1991, 32.8% in 1992 and further to 28.5% as of September 1993.

(ii) ***The broadening and diversification of the financial system.*** In 1988, the banking system comprised nine commercial and development banks providing a limited range of conventional banking services (e.g., deposits and loans). By 1992, with the entry into the market of three new banks of a merchant/investment type (Ecobank, Continental Acceptances, Merchant Bank of Ghana), the banking system was able to provide a broader range of financial services including corporate finance, underwriting syndication and advisory assistance. The Ghana Stock Exchange (established in 1990 with support by FINSAC I), in spite of its present modest scale of operations, is providing an infrastructure necessary for the future development of the capital market. The overall level of competitiveness within the system, however, remains low, with the three largest banks (GCB, SSB and Barclays) playing the role of market leaders.

(iii) The enhanced capacity of Bank of Ghana in supervising the banking system, as a result of the new regulatory framework and prudential regulations introduced by the August 8, 1989 Banking Act, as well as the measures undertaken to strengthen the Bank Supervision Department.

2.28 On the other hand, there remains areas in which the performance of the Ghanaian financial sector stands in ***need of further improvements***, including those listed below:

(i) The Bank of Ghana continues to fulfill a dual role of operating both in open market operation to smooth seasonal flows but also to fund the Government's deficit need through the issuance of short term bills. The Central Bank should only be performing the former role of smoothing seasonal flows.

(ii) There is an increasing need to introduce a broadly based competitive structure in the banking sector. This can best be achieved by the

Government aggressively speeding up its divestiture and privatization process of its interests in the Government owned banks.

(iii) The financial liberalization measures (e.g., interest rate decontrol, removal of exchange controls) initiated since 1989 have not been followed by a financial deepening of the Ghanaian economy. The ratio of M2 to GDP has remained flat from 1989 through 1992. The macroeconomic and other factors accounting for such a situation appear to warrant an in-depth analysis.

(iv) The financial system's performance in mobilizing savings remains inadequate. Private sector deposits with the banking system increased from ₵103 billion at end-1989 to ₵241 billion at end-1992 (G) represents an average annual growth of 8% in real terms after adjusting for inflation. The ratio of private sector deposits to GDP at end-1992 was 3.5%. Gross domestic savings, already low at 7.9% of GDP in 1991, fell further to 2% in 1992. These ratios are very low even when compared with other sub-Saharan countries.

(v) Credit to the private sector by the banking system, after stagnating at the approximate level of ₵80 billion during the 3-year period 1989-1991, expanded rapidly, by 56% in 1992 to ₵138.5 billion at end-1992, and further by 42% (52.5% on an annual basis) in the first nine months of 1993, to ₵186 billion. This still represents a low ratio of 2% to GDP, and there is a need for the banking system to sustain the recent credit growth so as to adequately meet the financing needs of the public.

c. **Sustainability**

2.29 The sustainability of the reforms and actions undertaken under FINSAC I derives, amongst other things, from the fact that the reform program was not conceived of as a one-shot undertaking. Rather, its reform program was designed as the first phase of a continuing sectoral adjustment process. In line with that thinking, some three years after its inception (in 1988) and following its successful implementation, FINSAC I was followed by the subsequent FINSAC II approved by IDA in December 1991. Apart from introducing additional sector reforms (e.g., privatization of restructured banks, non-bank financial institutions; improvements in monetary control), FINSAC II included the specific objective of helping Ghana ***consolidate*** those reforms already initiated under the preceding FINSAC I. Thus, the bank restructuring program started under FINSAC I continues to receive IDA's support under FINSAC II toward the forthcoming privatization of most of the restructured parastatal banks. In regard to the recovery of non-performing assets, the preparatory and legal work toward establishing NPART started under FINSAC I, but NPART actually started its operations under FINSAC II. The extensive institution - building and training programs (e.g., Institute of Chartered Accountants, Ghana Institute of Bankers) initiated under FINSAC I continue to this day to receive support under FINSAC II. This continuum between these two successive operations goes a long way in ensuring the sustainability of reforms and actions undertaken under the initial program. Apart from the foregoing, the sustainability of reforms is enhanced by the Government's continuing strong commitment to the reform process. To further ensure sustainability, it would be advisable for IDA and other Donors to

be prepared to continue providing some technical assistance (e.g., logistical support, training) on a gradually diminishing scale over the next few years to selected program implementation agencies (e.g., BOG, ICAG, GSE, Ghana Institute of Bankers).

## 6. IDA Performance

2.30 IDA's contributions to the success of the reform program have been significant. Its extensive financial sector review preceding the preparation of the operation led to a meaningful policy dialogue with Government officials, and provided major conceptual inputs into the Government's Statement of Financial Policy which formed the basis of the agreed reform program supported by FINSAC I. IDA's performance during project implementation was fully satisfactory. The dialogue on financial sector issues continued during implementation of the Credit as part of IDA's supervision work, particularly in relation to the fulfillment of the conditions for second and third tranche releases - IDA staff and consultants made substantive contributions inter alia, toward the formulation of the General Framework document outlining the main guidelines and modalities for bank restructuring, as well as the design of NPART and operating policies, the Government agency in charge of non-performing assets recovery. IDA's supervision work for this Credit has been intensive, amounting to 111 staff weeks for the period up December, 1992. This worked out to a supervision coefficient of 22 staff weeks per year, which reflects the fact that IDA gave due consideration to the complexity, and the commensurate supervision requirements, of the program. Furthermore, the secondment of one IDA staff, with relevant sector and field experience, to Bank of Ghana during the 1988-91 period, was of considerable assistance in improving the Borrower's implementation capacity. Finally, IDA's support of and close involvement in the reform program enhanced the latter's credibility vis-a-vis external donors, thus enabling the successful mobilization of co-financing consisting of a loan of US$94 million equivalent from the Japanese Government and a grant of US$12 million equivalent from Switzerland.

## 7. Borrower's Performance

2.31 The success of FINSAC I is attributable in no small measure to the Government's steadfast commitment to the reform program, in particular to the priority objective of resolving the banking distress situation prevailing in 1988 and restoring the sound operation of the banking system. The performance of all project implementation entities has been satisfactory, in particular that of Bank of Ghana which has been excellent. Bank of Ghana, with support from IDA-seconded staff (para 2.30) played an important role in coordinating and monitoring the implementation of all program activities, until the establishment, in 1992, of the FINSAP Implementation Secretariat. The delay which occurred in the fulfillment of the second tranche release conditions, which took 17 months following effectiveness (para. 2.11), and which subsequently required an extension of the original closing date from September 30, 1990 to December 31, 1992, is attributable not to slackening of efforts, but rather to the Government's thorough and systematic approach to implementing reforms, apart from the multiplicity of these release conditions. The nominal delay was also attributable to an over-optimistic initial estimate of the pace of implementation and disbursements. All audit reports have been received timely and have been found satisfactory.

## 8. Lessons Learned

2.32 Financial sector reforms stand a better chance of successful implementation if they are initiated in the aftermath (and within the broader context) of an overall structural adjustment programs. That is so because, by then, certain requisite macroeconomic conditions (such as an appropriate exchange rate regime; and the reduction in fiscal imbalance) have already been achieved, thus enabling the financial sector to operate in a relatively distortion-free environment. The implementation of FINSAC I, initiated in 1988, benefitted from the exchange rate and fiscal reforms previously introduced under the Economic Recovery Program started in 1983 and supported by SACI in 1987.

2.33 Intensive economic and sector work, including agreement, in principle, with the Government on a broad action program of sector reforms preceding appraisal, helped expedite the processing cycle of FINSAC I without sacrificing quality. The time interval between the Initiating Memorandum and Board approval was less than four months, that between appraisal and effectiveness, less than six months.

2.34 The choice of disbursing the Credit in three tranches (instead of the more usual two tranches), for a relatively complex and time-consuming reform program such as FINSAC I (and for financial sector adjustment operations generally), probably helped improve implementation by intensifying the policy dialogue between the Government and the Bank on key sectoral issues during discussions preceding the tranche releases.

2.35 Drawing a lesson from the difficulty of assessing the impact of FINSAC I on the overall financial sector (para 2.26), it would have been desirable for the Government and the Bank to agree on a set of pre-established, monitorable indicators of financial sector performance. Such indicators could include: ratio of financial savings to GDP; savings deposits with banks; private sector savings; evolution of credit to private sector; amount of open market transactions by the Central Bank; securities transactions; ratio of non-performing loans to total outstanding portfolios of banking system. These indicators, which should not be construed as targets, would be useful for the purpose of periodically and systematically monitoring the performance of the financial sector and banking system overall (during program implementation), and not just that of specific program components.

2.36 The systematic (as opposed to the case-by-case) approach to bank restructuring (through the adoption of a comprehensive and system-wide framework for restructuring) has contributed to the generally successful outcome of the restructuring, as evidenced by the fact that six out of the seven distressed, state-owned banks have recovered their financial viability. In retrospect, however, it would have been advisable for the Bank to press the Government at an early stage for a more forceful rationalization (i.e., a reduction in the number) of these banks, through mergers or liquidations. As things stand now, their number (seven) is likely to be reduced to five, with the proposed merger of SSB/NSCB and that of COOP Bank with another (still undetermined) bank. A greater reduction in the number of state-owned banks (say to three or four) would have been even more desirable since it would further lessen the Government's direct role in the operation of the banking system. Subsequent privatization would also be easier to achieve for a smaller number of banks given the limitations of the market.

2.37 The specific modality chosen under FINSAC I for recovery of non-performing assets, namely the establishment of a specialized Government agency to take over and realize

such assets, is an interesting one and, in the case of Ghana, has proven moderately successful in terms of the amounts actually recovered. However, there are alternative modalities (e.g., keeping non-performing assets with the originating banks and entrusting these banks with the responsibility for recovering them) that have been applied in other countries. A Bank-wide cross-country comparative review of the relative effectiveness of the alternative methods might yield operationally relevant lessons.

2.38 Implementation experience of FINSAC I points out the important role of technical assistance. The most useful components were: (i) consultancy assistance in drafting guidelines for bank restructuring and the modus operandi for NPART, the loan recovery agency; (ii) secondment of experts to both managerial and advisory positions in restructured banks; (iii) capacity building in banks of Ghana, particularly for strengthening banking supervision; and (iv) assistance toward the establishment and start-up of Ghana Stock Exchange.

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## II. PROJECT REVIEW FROM BORROWER'S PERSPECTIVE

1. **Background**: As part of the economic recovery programme, the major objectives of which were to (a) shift relative prices in favour of production, particularly for exports and efficient import substitution; (b) restore fiscal and monetary discipline; (c) initiate the restoration of the country's social and economic infrastructure; and (d) to encourage private investment, the Government of Ghana saw the need to strengthen the financial sector. It was realized that the financial sector was handicapped by significant institutional weaknesses and Ghana needed an efficient and dynamic financial sector that would both mobilize domestic resources and allocate them efficiently to different sectors of the economy.

The Government, therefore, with the IDA, initiated strategies on the financial sector in 1985 and in 1988 the First Financial Sector Adjustment Credit I (FINSAC I) was given to Ghana. The Government, therefore, developed a comprehensive and far-reaching action programme with the main aim to:

(i) enhance the soundness of banking institutions through reforms of the regulatory framework and the restructuring of distressed financial institutions;

(ii) improve deposit mobilization and efficiency in credit allocation; and

(iii) develop the money and capital markets.

The Main Achievements of the Programme are:

(a) Liberalization of the financial (banking) environment: This has been achieved with the removal of ceiling on interest rates and bank charges and the abolishing of all sectoral credit targets.

(b) Formulation of improved legal and regulatory framework: The new banking law has been promulgated and has been effective so far.

(c) Securing improved banking supervision function: The department has been strengthened and is now able to fulfill its functions under the banking law to ensure a disciplined banking environment.

(d) Implementation of a comprehensive bank restructuring programme: Six out of seven state-owned banks were restructured initially and have improved considerably since then. The seventh, Ghana COOP Bank has just been restructured financially following earlier efforts on management and institutional restructuring. (December, 1993)

(e) Recovery of non-performing assets: Total recovery has been adequate. Total recovery expected by 1995 is c18 billion. Total recovery from 1991 to 1993 is 9.9 billion; which is 92.43% of the actual recovery target of c10.7 billion.

(f) Development of money and capital market: A modest start was made with the establishment of Consolidated Discount House. Later, Securities Discount Company Ltd. was also established. The Ghana Stock Exchange was also established in September 1990 and even though the volume of shares traded has been relatively low, recent developments in the economy indicate that the capital market will soon experience a vigorous take-off and a buoyant growth.

(g) Formulation of the corporate restructuring programme: There was a study under the programme which identified potentially viable enterprises and non-viable enterprises.

(h) Strengthening the accounting and auditing profession: Assistance to the Institute of Chartered Accounts (ICAG) included the provision of two consultants to the ICAG who have helped in strengthening the institutional set up and related activities that affect the effectiveness of the ICAG.

(i) Improving training: Strengthening of the Institute of Chartered Accountants and provision of training to staff of the Bank of Ghana and other beneficiary institutions formed part of the activities under this heading.

## 2. PROJECT DESCRIPTION AND IMPLEMENTATION

The Financial Sector Adjustment Credit I was provided by the World Bank in an original amount equivalent to US$100 million but was subsequently increased to US$106.6 million to support the financial sector adjustment programme in particular and the Economic Recovery Programme in general. The loan components are:

| | | | |
|---|---|---|---|
| Part A: | Imports/Balance of Payment Support | - | US$95 million |
| Part B: | Technical Assistance | - | US$11.6 million |

The first tranche of the loan was released when the loan became effective in August 1988. The second tranche was released 17 months after that. It was expected to be released 9 months after the first tranche release. The third tranche was released 6 months after the second tranche - three months earlier than anticipated. Technical assistance was obtained for the recruitment of consultants for the various banks and financial institutions.

Items procured under the facility were done according to World Bank regulations. The technical assistance disbursement was extended to December, 1992.

## 3. LOAN DISBURSEMENT

| | 1988 ($) | 1989 ($) | 1990 ($) | 1991 ($) | 1992 ($) |
|---|---|---|---|---|---|
| Part A: Imports | | | | | |
| Part B: Technical Assistance | - | 383,000 | 1,325,000 | 2,881,000 | 3,088,000 |

## 4. LESSONS LEARNED

The implementation of FINSAC I, initiated in 1988, benefitted from the exchange rate and fiscal reforms introduced under the economic recovery programme started in 1983. This supports the view that implementation of comprehensive macro-economic policy initiatives helps to induce mutually re-enforcing interactions across sectors and provides the basis for successful sectoral projects.

- The benefit of detailed pre-implementation planning. In this case it is necessary to recall that there was a tripartite (Ghana Govt/Edesa Consultant/IDA) planning session before the implementation of the Banking Restructuring Programme. The detailed planning of activities proved beneficial in implementation.

- The systematic approach, involving well defined phasing of the various bank structuring activities also contributed to the successful outcome of the restructuring programme. The banking restructuring programme initially focussed on damage control issues, then followed by formulation and implementation of short-term turn-around plans which were also followed by preparation of rolling corporate plans. The step-by-step restructuring also recognized the need to tackle management restructuring first, then institutional restructuring before undertaking financial restructuring.

- The method used for the recovery of non-performing assets by the establishment of the NPART, a specialized unit with time-bound life, has been quite successful. It is also instructive.

- Technical assistance has been a very useful component of the programme and has been an effective tool for setting up of NPART, recruitment of experts for the banks and supporting capacity building in the Bank of Ghana. Assistance was also given for the establishment of the Ghana Stock Exchange.

Manpower constraints frustrated the rate of implementation in certain areas and underscored the need to ensure adequacy and sufficiency of manpower requirements and institutional set up before agreeing on project targets.

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# FINANCIAL SECTOR ADJUSTMENT CREDIT I
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## III. STATISTICAL INFORMATION

### 1. Related Bank Loans & Credits

| *TITLE* | *DATE (FY)* | *AMOUNT (US$ million)* |
|---|---|---|
| ERP & ERP SFacility | 1984 | 76.0 |
| RIC & RIC AFacility | 1985 | 87.0 |
| ISAC & ISAC AFacility | 1986 | 53.3 |
| EdSAC | 1987 | 34.5 |
| SACI & SACI AFacility | 1987 & 1988 | 115.0 & 15.0 |
| FINSAC I & Supplement | 1988 & 1989 | 100.0 & 6.6 |
| SAC II & Supplements | 1989, 1990 & 1991 | 1201.0, 5.7 & 8.3 |
| EdSAC II | 1990 | 50.0 |
| SAIII & Supplements | 1991 & 1992 | 120.0 |
| FINSAC II | 1992 | 100 |
| AGSAC | 1992 | |
| PEED | 1993 | 80 |
| | | 41 |

### 2. Credit Data

| | *CUMULATIVE ESTIMATED AND ACTUAL DISBURSEMENTS (US$ million)* | | | | |
|---|---|---|---|---|---|
| | *1988* | *1989* | *1990* | *1991* | *1992* |
| Initial Estimate | | 36.0 | 89.9 | 106.6 | |
| Actual | | 43.2 | 48.8 | 100.5 | 106.6 |
| Actual as % of Estimate | | | | | |

## 3. Credit Processing Timetable

| | *Original Date* | *Actual Date* |
|---|---|---|
| Initiating Memorandum | 02/10/88 | 02/10/88 |
| Appraisal | 02/22/88 - 03/03/88 | 02/22/88 - 03/0488 |
| Negotiations | May 1988 | May 1988 |
| Letter of Financial Development Policy | March 1988 | March 1988 |
| Board Approval | May 31, 1988 | May 31, 1988 |
| Loan Signing | June 14, 1988 | June 14, 1988 |
| Effectiveness | August 1988 | August 11, 1988 |
| Second Tranche Release | March 1989 | June 1990 |
| Third Tranche Release | December 1989 | December 1990 |
| Closing | September 30, 1990 | December 31, 1992 |

## 4. Mission Data

| | *Date* | *No. of Weeks* | *No. of Persons* | *Staff Weeks* | *Date of Report* |
|---|---|---|---|---|---|
| Appraisal I | Feb. 22 - Mar 4 | 3 | 3 | 9 | Mar 21, 1988 |
| Supervision I | Feb 11 - Mar 3 | 4 | 4 | 16 | Mar 3, 1989 |
| Supervision II | May 19 - 23 | 1 | 2 | 2 | Jun 29, 1989 |
| Supervision III | Sep 30 - Oct 13 | 4 | 3 | 12 | Oct 27 1989 |
| Supervision IV | Feb 12 - 28 | 3 | 1 | 3 | May 7, 1990 |
| Supervision V | Jun 25 - Jul 13 | 4 | 8 | 32 | Aug 20, 1990 |
| Supervision VI | Nov 7 - 26 | 5 | 3 | 15 | Dec 6, 1990 |
| Supervision VII | Jun 15 - Jul 7 | 4 | 3 | 12 | Jul 30, 1992 |
| Supervision VIII | Aug 13 - 18 | 1 | 4 | 4 | Aug 19, 1992 |
| Supervision IX | Oct 8 - 20 | 2 | 3 | 6 | Nov 5, 1992 |
| Supervision X | Sep 29 - Oct 8 | 2 | 1 | 2 | PCR pending |

**REPUBLIC OF GHANA**
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**POLICY MATRIX**

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| **I. Measures to Enhance Soundness of Banking Institutions** | |
| **A. Prudential Regulations** | |
| 1. (i) Establish a minimum capital adequacy ratio for prudential purposes; (ii) increase minimum amount of paid-up capital to establish a bank (to be revised from time-to-time by BOG); (iii) apply capital adequacy provisions to development finance institutions engaged in commercial banking; (iv) limit dividends by banks that do not meet capital adequacy guidelines; and (v) empower BoG to mandate greater capital for prudential purposes for individual banks on case-by-case basis. | **1-5**: Legal Instrument (L.I. 1389) satisfactory to IDA passed in December 1988, covering inter alia minimum capital, capital adequacy ratio, development banking lending limits and auditing requirements (long-form audit). Enforcement of its disposition has started under close monitoring by the central bank (Bank of Ghana (BOG).<br><br>Draft of new Banking Law superseding the Banking Act 1970 (Act 339) and the Banking and Financial Institutions Decrees, 1979 (AFRCD 17) under review by IDA. The new law, embodying the dispositions introduced under L.I. 1389, was approved by the PNDC on August 8, 1989. |
| 2. Require development finance institutions, where engaged in commercial banking, to provide for statutory reserves of at lease the levels required of commercial banks. | |
| 3. Place limits on secured as well as unsecured loans to any single borrower (individual or enterprise). Place stricter limits on secured as well as unsecured loan to companies in which a bank's director has an interest exceeding a certain percentage. | |
| 4. Review and increase penalties for violation of banking regulations. | |

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| 5. Require audited reports on banks submitted to BOG to be in long form format in accordance with other BOG guidelines, based substantially on international standards. | |
| 6. BOG to require banks to classify their portfolios according to criteria for substandard, doubtful and loss assets (to be reported on a periodic basis, together with the specific provisions established). These standards to be developed with the assistance of an international accounting firm. Implementation of the full range of remedial actions to await the appointment of two technical advisors in bank supervision. | New accounting and auditing standards for banks were prepared by mid-1988 with support of an international auditing firm, reviewed by IDA and subsequently incorporated in L.I. 1389. |
| 7. Introduce improved reporting requirement from banks to the BOG, off-site analytical capabilities and indicators, as well as logistical support. | New, improved reporting standards satisfactory to IDA were introduced in 1989. Compliance by banks since have been generally satisfactory. |
| 8. Support establishment of a credit clearing house for banks. | The credit clearing house (to be renamed interbank credit data bank) initially expected to start operating by end-1989, is now to be operational in 1994, following a delay on account of the Ghana Bankers Association. |
| **B. Banking Supervision** | |
| 1. Enforce, through guidelines and monitoring action, internal controls and in-house audits of banks. | Has been in effect since 1989 as part of the restructuring of state-owned banks. |
| 2. (i) Issue mandatory minimum terms of reference expanding scope of external audits of banks and (ii) hold periodic discussions between BOG and the auditors. | New audit requirements enacted under L.I, 1389. The new standards have been enforced for all banks as of calendar year 1988, under BOG's close supervision. Compliance is generally satisfactory. |
| 3. Strengthen examination methodology and skills. Review staffing needs of BoG's Examination Department, incentives and staff training, and set up a permanent training program for examiners. | A new supervision manual has been introduced since 1990. |

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| 4. Establish computerized system for prudential returns for banks and analyze the financial situation of banks based on a set of performance indicators. Provide feedback to bankers. | Software for the processing of the related returns, including an early warning system, has been developed (based on the new reporting standards) system in 1989 became fully operational by December 31, 1989, following acquisition of required hardware in October 1989. |
| 5. Draw up and implement an annual inspection plan, including full and targeted examination (each bank to be visited at least once a year). | In 1992, Bank Supervision Department of BOG carried out on-site inspections of all banks, on the basis of a pre-established annual inspection plan. This was to be repeated in 1993 and thereafter. |
| 6. Repeat external audits of banks with assistance of international auditors. | Done for state-owned restructured banks. |
| **C. Accounting and Auditing** | |
| 1. Institute of Chartered Accountants (ICA) has agreed to be the focal point for efforts to upgrade and strengthen the accounting profession in Ghana. | A review of training needs and other measures for improving the accounting profession was carried out with ODA financing. The report's recommendations, including an action plan for strengthening ICAG, has been implemented since 1990. |
| **II. Banking Restructuring** | |
| 1. Carry out full diagnostic studies by international auditing firms. | Completed by 1989. |
| 2. Implement safeguard measures to prevent further deterioration. | Directives issued by BOG in February 1989, which also has been closely monitoring compliance by banks undergoing restructuring. |
| 3. Recruitment of an advisor on banking restructuring. | Restructuring advisory team started work in January 1989 under Swiss grant. |
| 4. Formulation of framework and timetable satisfactory to IDA specifying the modalities for the restructuring of banks, in particular (i) measures for dealing with banks portfolio of non-performing loans, including loans to state-owned enterprises, and (ii) rescheduling/conversion of Government's loans to banks. | General Framework document approved by Government in July 1989. Implementation modalities included (i) enabling for NPART and the Special Tribunal; (ii) operational guidelines for NPART: and (iii) transitional measures to arrest deterioration and achieve a return to profitability of restructured banks. |

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| 5. Agreement with IDA on specific proposals and targets for a reduction of banks' non-performing portfolio (including off-balance sheet items). | The cleaning up of banks' portfolios through replacement of non-performing assets by Government bonds and/or other offsetting operations was achieved by 1991-92 for six of the seven restructured banks, except for COOP Bank. |
| 6. Finalization of specific restructuring plans acceptable to IDA for commercial and development banks. | Restructuring plans for six of the seven distressed banks were completed by end-1990, reviewed by IDA and implemented since. The one exception related to COOP Bank. |
| 7. Undertake study on needs for corporate sector restructuring. | The Time-phase study on corporate restructuring was completed by external consultants in May 1990. It was subsequently followed in 1991-92 by an updating study, by local consultants. A number of consultants' recommendations were acted upon under a separate IDA investment prospect (PEED). |
| 8. Carry out study on exchange risk protection. | It was subsequently jointly decided by Government and IDA to abandon this study, which no longer appeared relevant following the abolition of exchange controls. |
| **III. Deposit Mobilization and Credit Allocation** | |
| **A. Deposit Mobilization** | |
| 1. Review provisions in laws and regulations relating to disclosure of information. | |
| 2. Allow banks to set scale of charges; undertake survey of charges on a semi-annual basis and publish results. | Deregulation of banking charges completed by October 1990. |
| 3. Amend regulations to permit banks to vary working days and business hours of branches. | No such regulations existing in Banking Act of August 9, 1989. |
| 4. Review system for collecting and clearing cheques. | Status unknown. |
| 5. Allow banks to set own interest differential on demand, savings and time deposits. | Deregulation of banking deposit rates achieved by February 1988. |

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| 6. Design and introduce package of measures to attract emigrants remittances. | Completed. |
| **B. Credit Allocation** | |
| 1. Allow banks to set their own interest rates on loans. | Deregulation of banking lending rates achieved by February 1988. |
| 2. Discontinue sectoral credit targets. | Last sectoral credit target, for agriculture, was removed in November 1990. |
| 3. Establish mechanisms and criteria for determining use of special line of credit and other special schemes to be used only in special circumstances | Status uncertain. There appears to be no need for action as the only lines of credit in Ghana are from the Bank Group (for SMEs, Export Development, etc.). |
| 4. Review efficacy of Credit Guarantee Scheme. | This scheme has been dormant and is now inoperative, thus obviating the need for its review. It is being addressed under the PEED project. |
| **C. Efficiency of Banking Operations** | |
| 1. Prepare and circulate standard set of average efficiency measures for banks. | BOG has been collecting, computing and analyzing relevant operating ratios for banks (operating cost, profitability, interest margin, etc.) for comparison purposes. |
| **IV. Money and Capital Markets** | |
| **A. Money Market** | |
| 1. Determine modus operandi for Consolidated Discount House (CDH). Establish nature and extent of liquidity support by BOG. Identify prudential reporting and monitoring requirement of BOG. Define operational limits through acceptance by CDH and BOG of a CDH Statement of Operational Policies, to be developed with Technical Assistance. | Consultant report on strengthening CDH, financed by ODA-UK, completed by April 1990 and implemented. |
| **B. Capital Market** | |
| 1. Conduct study of (i) investors, (ii) corporate issuers and (iii) secondary trading to determine demand. | **1-4**: Study undertaken by IFC in 1989. Its findings confirmed desirability to proceed with caution in developing regulatory and institutional (i.e., Stock Exchange) framework since volume of business was expected to be thin in early years. |

| *ISSUES/ACTIONS* | *IMPLEMENTATION* |
|---|---|
| 2. Review experience in other countries, possibly with IFC assistance, and make decision on applicability in Ghana. | Capital and debt market evaluation being continued under PEED project. |
| 3. Discuss available incentives, review likely effects and implement. | |
| 4. Develop with technical assistance, a suitable regulatory framework depending upon outcome of study (IV.B.I.) | |
| 5. Give financial and logistical support to ICA to review and upgrade auditing standards for corporate sector. | ICAG received financial and logistical support under FINSAC I, which enabled it to start work toward developing uniform set of accounting and auditing standards for corporate sector. This work is being supported under FINSAC II. |
| 6. Amend Social Security Decree Regulation to allow some of social funds generated to be invested in long-term securities of credit-worthy finance institutions and companies. | Previous regulations restricting investments by Social Security National Investment Trust (SSNIT) to Government-issued securities were rescinded by mid-1990. |

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## Financial Statements of Seven Restructured Banks
(Amounts in ₵million)

| *BALANCE SHEET* | *31-12-91* | *31-12-92* | *30-09-93* |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and short-term funds | 81,789 | 120,459 | 86,257 |
| Investments/FINSAP bonds | 181,005 | 192,174 | 230,184 |
| Advances | 40,976 | 57,291 | 85,436 |
| Other asset accounts | 29,311 | 76,820 | 73,796 |
| | 333,081 | 446,744 | 477,673 |
| Trade investments | 611 | 241 | 2,888 |
| Fixed assets | 8,013 | 12,336 | 13,302 |
| **TOTAL ASSETS** | 341,706 | 459,321 | 493,883 |
| **LIABILITIES** | | | |
| Deposits/current accounts | 173,890 | 246,990 | 271,643 |
| Creditors and accruals | 104,796 | 127,637 | 120,054 |
| | 278,686 | 374,627 | 391,697 |
| Borrowings | 11,095 | 15,788 | 13,734 |
| **TOTAL LIABILITIES** | 389,781 | 390,415 | 495,431 |
| **SHAREHOLDERS FUNDS** | | | |
| Stated capital | 10,306 | 11,306 | 11,682 |
| Reserves | 26,283 | 37,589 | 58,948 |
| Retained earnings | 15,335 | 20,011 | 17,804 |
| **TOTAL LIABILITIES AND SHAREHOLDERS FUNDS** | 51,924 | 68,906 | 88,863 |
| **PROFIT & LOSS STATEMENT** | | | |
| Interest income | 39,743 | 39,352 | 48,350 |
| Interest expense | 11,401 | 14,095 | 16,216 |
| **NET INTEREST INCOME** | | | |
| Commission and fees | 6,725 | 9,710 | 9,390 |
| Other operating income | 3,711 | 5,909 | 594 |
| **TOTAL OPERATING INCOME** | 38,778 | 40,876 | 42,134 |
| Operating expenses | 15,157 | 21,652 | 20,289 |
| **OPERATING PROFIT** | 23,621 | 19,224 | 21,829 |
| Charge for doubtful debts | 13,790 | 10,678 | 2,485 |
| **NET OPERATING PROFIT** | 9,831 | 8,546 | 19,343 |
| Other income | 149 | 277 | 684 |
| Exceptional items | (108) | 1,607 | 2,229 |
| **PROFIT BEFORE TAX** | 9,872 | 10,430 | 22,257 |
| Taxation | 5,961 | 2,466 | 5,393 |
| **PROFIT AFTER TAX** | 3,911 | 7,964 | 16,864 |

| *BALANCE SHEET* | *31-12-91* | *31-12-92* | *30-09-93* |
|---|---|---|---|
| **RATIO ANALYSIS** | | | |
| Operating expenses: Total operating income | 39.1% | 53.0% | 48.2% |
| Operating expenses: Average assets | 4,9% | 5.4% | 4.7% |
| Total operating income: Average assets | 12.4% | 10.2% | 11.8% |
| Operating profit: Average assets | 7.6% | 4.8% | 5.4% |
| Profit before tax: Average assets | 3.2% | 2.6% | 6.2% |
| Profit after tax: Average assets | 1.3% | 2.0% | 4.7% |
| P.A.T.: Average shareholders' funds | 8.4% | 13.2% | 28.5% |

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## Loan Portfolio Classification of Restructured Banks
(Amounts in ₵million)

| *(Year-End)* | *1988* | *1989* | *1990* | *1991* | *1992* | *09/30/ 1993* |
|---|---|---|---|---|---|---|
| A. Total Portfolio Outstanding | 65,168 | 86,503 | 72,553 | 78,098 | 114,507 | 131,801 |
| B. Performing Loans | 27,658 | 23,851 | 28,412 | 46,380 | 77,121 | 94,139 |
| C. Non-Performing Loans (C = A - B) | 37,510 | 62,652 | 44,141 | 31,718 | 37,386 | 37,662 |
| D. Percentage of Non-Performing Loans (D = C/A) | 57.7% | 72.5% | 60.6% | 40.6% | 32.8% | 28.5% |

**Notes:** (1) Non-Performing Loans are those classified in the following three categories: sub-standard, doubtful and loss, in accordance with Bank of Ghana guidelines.

(2) The aggregate data on this table relate to 6 of 7 restructured banks: GCB, SSB, NSCB, NIB, ADB and BHC. The data relating to the COOP Bank are not available.

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## Aggregate Balance Sheet Statements of All Banks, 1988-1992
(Amounts in ₵million)

| *ASSETS* | *1988* | *1989* | *1990* | *1991* | *1992* |
|---|---|---|---|---|---|
| Cash & Short-term Funds | 106,805 | 140,986 | 213,954 | 256,186 | 272,339 |
| Cash in hand | 6,724 | 10,415 | 12,207 | 23,344 | 51,836 |
| Balances with bank of Ghana | 22,516 | 28,832 | 33,034 | 43,770 | 59,659 |
| Balances with banks | 33,443 | 35,588 | 64,578 | 72,283 | 58,496 |
| Money at short notice | 43,623 | 66,187 | 104,085 | 116,832 | 104,347 |
| Investments | 30,727 | 66,648 | 148,123 | 210,873 | 250,006 |
| Government Securities | 9,162 | 17,665 | 38,153 | 129,583 | 98,426 |
| Bank of Ghana Bills | 957 | 4,749 | 10,818 | 8,153 | 19,888 |
| Treasury Bills | 260 | 0 | 6,555 | 2,990 | 240 |
| Term placements | 10,227 | 34,165 | 51,245 | 45,326 | 76,185 |
| Bills discounted | 10,042 | 9,919 | 22,489 | 20,738 | 47,281 |
| Other Bills | 49 | 150 | 8,863 | 4,083 | 8,184 |
| Loans and Overdrafts (net) | 58,193 | 41,918 | 57,355 | 78,472 | 135,245 |
| Loans | 46,951 | 53,915 | 55,770 | 55,670 | 63,702 |
| Overdrafts | 42,027 | 44,146 | 46,926 | 63,365 | 114,888 |
| Provisions for debts | (35,785) | (56,143) | (46,341) | (40,562) | (42,790) |
| Other Assets | 40,289 | 50,485 | 54,608 | 64,870 | 93,857 |
| Investments in subsidiaries (net) | 2,726 | 9,208 | 2,678 | 8,379 | 3,044 |
| Shares | 1,433 | 1,180 | 1,255 | 1,606 | 2,575 |
| Loans | 4,156 | 10,872 | 2,177 | 2,501 | 2,158 |
| Provisions | (2,861) | (2,778) | (754) | (780) | (1,688) |
| Fixed Assets | 11,117 | 12,682 | 12,811 | 15,042 | 21,318 |
| Total Assets | 244,359 | 321,942 | 489,531 | 628,819 | 775,809 |
| **Liabilities** | | | | | |
| Deposits | 158,976 | 243,373 | 320,298 | 430,639 | 495,462 |
| Savings Accounts | 32,450 | 43,685 | 105,294 | 193,846 | 144,841 |
| Current Accounts | 98,790 | 164,980 | 168,777 | 181,946 | 288,891 |
| Time Deposits** | 27,720 | 34,758 | 46,227 | 48,245 | 73,699 |
| | 0 | 0 | 0 | 6,902 | 8,031 |
| Creditors and Accruals | 73,607 | 71,439 | 110,439 | 24,179 | 180,439 |
| Borrowings | 18,687 | 21,841 | 5,660 | 10,336 | 14,937 |
| Local | 4,896 | 7,327 | 2,204 | 5,315 | 7,627 |
| Foreign | 13,792 | 14,814 | 2,881 | 5,021 | 7,310 |
| Total Liabilities | 251,270 | 336,753 | 436,889 | 565,454 | 690,638 |
| Stated Capital | 3,442 | 4,585 | 18,529 | 15,685 | 19,206 |
| Capital Surplus | 3,062 | 3,886 | 3,685 | 3,872 | 4,826 |
| Exchange Reserve | 5,091 | 9,755 | 17,990 | 23,795 | 33,183 |
| | | | | | 1,523 |
| Income Surplus | (19,505) | (32,498) | 12,988 | 20,013 | 26,134 |
| Shareholders' Funds | (6,910) | (14,812) | 53,192 | 63,366 | 84,971 |
| Liabilities & Shareholders' Funds | 244,359 | 321,942 | 489,531 | 628,819 | 775,809 |
| Contingent Liabilities | 59,508 | 69,903 | 57,808 | 30,813 | N.A. |

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## Aggregate Income Statements of All Banks
(₵million)

| *(Year-End)* | *1988* | *1989* | *1990* | *1991* | *1992* |
|---|---|---|---|---|---|
| Interest Income | 25,287 | 25,255 | 45,036 | 71,653 | 72,143 |
| Short-term funds | 4,292 | 5,406 | 12,660 | 22,956 | 18,106 |
| Investments | 4,902 | 5,503 | 15,644 | 28,185 | 31,502 |
| Advances | 16,093 | 14,346 | 16,732 | 20,512 | 22,534 |
| Interest Expense | 13,753 | 16,086 | 19,143 | 26,782 | 28,101 |
| Savings accounts | 6,332 | 5,688 | 11,499 | 17,178 | 14,359 |
| Current accounts | 117 | 359 | 308 | 1,126 | 4,216 |
| Time accounts | 5,541 | 7,593 | 4,801 | 6,462 | 7,175 |
| Borrowings | 1,763 | 2,446 | 1,535 | 2,016 | 2,351 |
| Interest Margin | 11,584 | 9,169 | 25,893 | 44,871 | 44,042 |
| Other Operating Income | 20,199 | 12,246 | 18,722 | 19,952 | 29,091 |
| Commissions and fees | 6,937 | 9,352 | 9,550 | 12,976 | 16,004 |
| Profits on exchange (net) | 12,534 | 2,006 | 2,968 | 4,868 | 10,476 |
| Dividends from investments | 56 | 263 | 477 | 816 | 1,381 |
| Other | 672 | 625 | 727 | 1,293 | 1,230 |
| Gross Earnings Margin | 31,733 | 21,415 | 39,615 | 64,824 | 73,133 |
| Operating Costs | 21,170 | 18,274 | 21,238 | 32,270 | 36,096 |
| Staff costs | 12,095 | 12,114 | 12,865 | 17,302 | 23,865 |
| Occupancy costs | 1,363 | 1,452 | 1,702 | 2,647 | 2,952 |
| Other operating costs | 7,713 | 4,708 | 6,671 | 12,321 | 9,280 |
| Net Earnings Margin | 10,562 | 3,141 | 18,376 | 32,553 | 37,037 |
| Other Costs (net) | 20,561 | 13,398 | (13,733) | 15,944 | 13,449 |
| Depreciation costs | 2,068 | 1,663 | 2,552 | 1,90 | 2,399 |
| Net provisions for bad debts | 18,689 | 20,283 | 12,432 | 15,757 | 13,182 |
| Other income | 196 | 8,548 | 28,717 | 1,719 | 2,183 |
| Profit (loss) Before Tax | (9,999) | (10,257) | 32,109 | 16,609 | 23,598 |
| Taxes | 2,348 | 1,085 | 5,370 | 10,950 | 9,072 |
| Profit (loss) After Tax | (12,347) | (11,342) | 26,739 | 5,659 | 14,516 |
| Allocation of Profit | | | | | |
| Dividends | 35 | 98 | 545 | 1,411 | |
| Statutory reserves | 154 | 262 | 7,360 | 2,391 | |
| Other reserves | 1 | 0 | 0 | 0 | |
| Income surplus | (12,556) | (11,702) | 1,626 | 1,857 | |
| Adjustments | 20 | 0 | 17,208 | 0 | |

Source: BOG

1988 includes GCB, BBG, SCB, NSCB, NIR, MB, ADB, BHC, SSB, BCC, and GH, COOP. (GCB data covers 18 months because the fiscal year end-1987 is June.)
1989 includes GCB, BBG, SCB, NSCB, NIB, MB, ADB, BHC, SSB, BCC and COOP.
1990 includes GCB, BBG, SCB, NSCB, NIB, MB, ADB, BHC, SSB, BCC, COOP, ECO & CAL. (Data for Ecobank covers 9 months ending December 1990.)
1991-92 includes GCB, BBG, SCB, NSCB, NIB, MB, ADB, BHC, SSB, BCC, COOP, ECO & CAL.

# REPUBLIC OF GHANA
# FINANCIAL SECTOR ADJUSTMENT CREDIT I
# CREDIT 1911-GH

## Selected Data on Financial Intermediation
## (₵million at end of period)

| | *1988* | *1989* | *1990* | *1991* | *1992* | *Sept. 1993* |
|---|---|---|---|---|---|---|
| Money Supply | 139,031 | 185,153 | 216,958 | 227,190 | 360,685 | 374,446 |
| Quasi-Money | 50,155 | 54,918 | 66,284 | 96,591 | 158,658 | 184,137 |
| Broad Money (M2) | 189,186 | 240,071 | 283,242 | 392,671 | 523,604 | 558,583 |
| M2/GDP | 18.0 | 16.9 | 14.0 | 13.0 | 17.0 | |
| Total Assets of Banking System | 231,000 | 322,000 | 490,000 | 629,000 | 776,000 | |
| Equity Capital of Banking System | (6,900) | (14,812) | 53,192 | 63,366 | 84,971 | |
| Credit to Private Sector | 37,408 | 79,361 | 80,201 | 83,084 | 138,516 | 185,966 |
| Private Sector Deposits | 105,970 | 103,012 | 140,118 | 171,737 | 241,099 | |
| Total Deposits | 158,976 | 243,373 | 320,298 | 430,639 | 495,462 | |
| Banks' Fixed Deposit Rates (%) | 19.25-25.50 | 19.25-25.50 | 16.25-25.50 | 21.00-32.00 | 15.50-20.00 | 22.00-24.25 |
| Treasury Bill Rates (%) | 19.00 | 19.00 | 20.00-27.50 | 20.00-32.00 | 18.00-25.00 | 29.50 |
| BOG Discount Rates | | 26.00 | 26.00-30.00 | 20.00-35.00 | 20.00-30.00 | 30.00-35.00 |
| Banks' Lending Rates | 22.50-30.25 | 22.50-30.25 | 22.50-30.25 | 22.50-36.00 | 19.00-29.00 | 25.50-31.50 |
| Banks' Profit (Loss) Before Tax | (9,999) | (10,257) | 32,109 | 16,609 | 23,358 | |
| PBT as % of Total Assets | -11.9 | -3.8 | 7.8 | 3.0 | 3.4 | |
| PBT as % of Equity | -142.8 | -69.3 | 60.3 | 26.3 | 27.5 | |
| Banks' Profit (Loss) After Taxes | (12,347) | (11,342) | 26,739 | 5,659 | 14,516 | |
| Provisions for Bad Debts | 35,785 | 56,143 | 45,341 | 40,582 | 42,790 | |
| Provisions as % of Portfolio | 40.20 | 57.30 | 44.20 | 34.10 | 24.00 | |

| | *1988* | *1989* | *1990* | *1991* | *1992* | *Sept. 1993* |
|---|---|---|---|---|---|---|
| Non-Performing Loans1/ | 37,510 | 62,652 | 44,141 | 31,718 | 37,386 | 37,662 |
| Non-Performing Loans as % of Portfolio2/ | 57.7 | 72.5 | 60.6 | 40.6 | 32.8 | 28.5 |
| Banks' Liquid Reserves as % of Total Deposits | | 53 | 56 | 62 | 68 | 70 |

1/ Data relating to the 6 restructured banks: GCB, SSB, NIB, ADB, NSCB and BHC.

2/ Data relating to the 6 restructured banks: GCB, SSB, NIB, ADB, NSCB and BHC.