Policy Brief - Ghana's Proposed Development Bank Must Work

Introduction

The **Research and Consultancy Centre (RCC)** of UPSA has instituted the **UPSA ECONOMIC DIALOGUE SERIES in partnership with Citi TV/FM,** a platform to contribute meaningfully to Ghana's economic policy discourse. This policy brief is the second in the series for 2021 in respect of offering a credible and thought-leading platform to engage with experts in the development finance and the banking fields on **establishing the Development Bank of Ghana (DBG)**. The purpose of this policy brief examines Ghana's peculiar credit situation, by contextualising the global and other country-specific development banks with the view to offering policy recommendations that may enhance the successful establishment and operation of the proposed Development Bank of Ghana. The DBG, as outlined in the 2021 Budget Statement and Economic Policy presented to the Parliament of Ghana on the 12th of March, 2021, is one of the core pillars of Ghana CARES Obaatanpa programme. This policy brief highlights the fundamental constraints in Ghana's financial system that the proposed DBG seeks to address, and offers expert view on its successful implementation.

1. Background

Generally, Development Banks are financial institutions whose main task is to finance and promote developmental projects by providing medium and long-term funds at low interest rates to the private sector to operate in conjunction with other financial institutions. It is on this basis that the government intends to establish a Development Bank of Ghana for it to address the issues. The establishment of the proposed Development Bank of Ghana, is projected to address systematic failures in the credit market including lack of medium- and long-term credit, and lack of adequate funding to the productive sectors of the economy. Thus, the DBG is expected to support the drive to steady recovery in the manufacturing and the industrial sectors, especially, in the post Covid-19 recovery process.

In the view of the RCC, this development financing model can provide financial support to the underserved Small and Medium Enterprises (SMEs) and other strategic sectors, and priority areas of the country. This will help to achieve sustainable growth of the economy, and thereby assure a more equitable distribution of the benefits of progress and a better quality of life for the citizenry. It is also viewed as the government's effort to support, encourage and catalyse expansion through public and private investment in physical development, redevelopment of business and industry. Such a bank is positioned in the global perspective of development banks.

2. Global Perspectives of Development Banks

The number of development banks around the globe has increaseed rapidly since the 1950s. These have been encouraged by the International Bank for Reconstruction and Development, International Development Association (a member of the World Bank Group) and their affiliates. Historically, development banks have been important instrument of governments to promote economic growth by providing credit and a wide range of advisory and capacity building programmes to household, small and medium enterprises and even large private corporations whose financial needs are not sufficiently served by private commercial banks or local capital markets. During the last financial crisis (2007-2009), some development banks in Latin America, Asia, Africa and Europe assumed a countercyclical role by scaling up their lending operations when private banks experienced temporary difficulties in granting credit to the private sector.

While there have been regional development banks such as the European Investment Bank, Asian Infrastructure Investment Bank and the new Development Bank established by the BRICS countries (Brazil, Russia, India, China, and South Africa) to contribute further to a more balanced public-private mix in development finance, individual countries have also established development banks. There are country-level specific banks including China, Germany, India, and South Korea. Thus, the proposal of the Government of Ghana to establish the DBG is taking a cue from the examples of other countries, like Germany, to ease credit constraints and channel funds to productive sectors of the economy.

3. Ghanaian Specific Setting

Agricultural Development Bank and National Investment Bank were established in the early 1960s as national development banks. In the pure sense of a development bank, the existing development banks have suffered mission creep and have over the years metamorphosed into deposit-taking commercial and retail banks, derailing them from their development banking status. Consequently, these banks have not been able to deliver and adequately support the country's development processes.

The DBG is to help overcome the shortage of medium- and long-term loans since nearly 85% of current bank loans are for periods of less than 5 years. The challenge is for the DBG to correct the existing fundamentals which have hindered availability of long-term private sector credit. Currently, long-term finance is not esily accessible for firms of all sizes in Ghana, especially SMEs. The problem is felt acutely in the agriculture and manufacturing sectors which receive a much smaller share of credit from the financial sector compared to their share in GDP and employment.

The DBG is premised on the principle of serving as a wholesale and non-deposit taking bank. Such a bank holds potential capacity to receive support from both bilateral and multilateral institutions such as World Bank. Once the DBG is established, it will work to increase support for key sectors such as agribusiness and manufacturing companies by offering long-term wholesale financing, credit guarantees and other services for them, and by making it more efficient and less risky for private financiers to lend to SMEs.

The establishment of the DBG under the Ghana CARES 'Obaatanpa' Programme is expected to provide credit support to businesses. The aim is to increase access to long-term finance and boost job creation for enterprises in key sectors including agribusinesses and manufacturing. Ghana's quest for a national development finance institution to provide critical financing for economic development is now urgent. Thus, there is the need to critically implement the DBG well to achieve its objectives. It is on this basis that we offer the following recommendations.

4. The Way to Go - Better Ways of Establishing and Implementing the New Development Bank of Ghana

With the experience of Development Banks in other countries including those of Japan, South Korea, Singapore, Brazil and Germany, Ghana's Development Bank holds promise as Ghana can learn from the experience of those banks. Viewed in this way, **the Research and Consultancy Centre of UPSA offer the following recommendations in respect of establishing and operating the DBG:**

Before the Establishment of the DBG:

i. The initial funding source of the DBG is a clear case for concern. The DBG should be well-capitalized before it takes off.

ii. There is need for sensitization and education of the citizens and MSMEs about the DBG and its functions. This will ensure adequate knowledge and access of the credit system to be offered.

iii. There may be the need to retrain the participating bank and non-banking financial institutions on the modalities and operations of the DBG, particularly on the new focal areas that the financial institutions have hitherto not operated in.

iv. There is a need for government to ensure that there is wide stakeholder involvement in the setting up process. Recruitment of staff of the DBG should be competitive and based on merit.

Operations of the DBG:

a) Generally, the cost of borrowing (interest rate) should be checked and implemented according to plan and the laid down procedures for accessing credit from the DBG.

b) There should be a focus on the real sectors which have much linkages to facilitate job creation and fast track economic transformation. The DBG should have clear focal areas. If for instance foreign Development Banks such as the German Development Bank (KfW) focuses on only 3 areas (agriculture, sustainable economic development and governance) in Ghana, Ghana's DBG cannot be an exception and priority sectors of agribusiness and manufactures need to be emphasized.

c) Due diligence on borrowers as well as proper documentation and background information of businesses should be made before loans are approved to reduce bad loans. There should be effort to avoid loans to government and political cronies.

d) Independence from the government in the day to day running of the bank's operations is a key successful implementation strategy.

e) There should be transparency of loan policies, accountability of management and independent audit system.

f) In the past, a number of commercial and national development banks had poor risk management systems which led to much lower loan recovery rate. This situation needs to be guarded against.

Supervision and Management of the DBG:

a. It is obvious that other banking activities have diluted the previous specialized banks established to cater for financing needs of agriculture and manufacturing sectors. For the DBG to succeed, there is the need for management of the DBG to ensure that the bank concentrates on its core mandate.

b. The regulatory and supervisory role allocated to the Bank of Ghana through the Development Finance Institution Act 2020 (Act 1032) should not be compromised in any way.

c. The DBG, Bank of Ghana and other regulatory institutions should ensure no arbitrage, where those financial institutions who get access to the capital offered by the DBG do not divert the low interest rate credit to other financial institutions to offer those low interest funds at a relatively higher interest rate to other businesses.

d. The selection of management of the DBG should be competent professionals with no political influence in the appointments. Related to this is that, there should be no political interference with the governance and operations of the DBG.

e. Sound corporate governance practices are key implementation considerations, and focus has to be on results.

5. Conclusion

The DBG is projected to boost economic growth, reduce poverty and improve the lives of the poor. With the involvement of the international development banks, the DBG is likely to ensure use of professionals and application of best practices. The strategic focus of the National Development Bank should be to keep the compass on providing access to long-term finance in the key sectors of agriculture and manufacturing. By offering long-term wholesale financing, credit guarantees and other services, the Development Bank will help increase overall lending to priority sectors. This, notwithstanding the expected benefits, there is the need to uphold the suggested recommendations so that the DBG can push higher the frontier of the production possibilities of the financial system in Ghana.

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