CHAPTER THREE: TRADE AND FDI

3.1 Basic Statistical Trends
The external sector has always been the key to Ghana’s economic performance. Good economic performance as in the late 1950s and early 1960s was associated with good trade performance while poor economic performance as in the late 1960s and 1970s was associated with a severe contraction of the external sector.

The Balance of Trade was generally positive in the early years of Ghana’s existence - i.e., late 1950s and early 1960s. There were ample reserves to finance whatever current account deficits were run. Strains began to show in the mid to late 1960s as the country used up its reserves to finance Nkrumah’s ambitious development programme. These problems generally continued into the 1970s and the governments of the day with the exception of Busia’s government (1969-1972) responded by placing a lot of restrictions on imports. These restrictions enabled Ghana to run trade surpluses although the current account remained in a deficit. One result of the restrictions was a severe fall in the importance of the trade sector so that by 1983 exports had fallen to 4% of GDP from 21% in 1970.

There was a fundamental change in economic policy with the introduction of the Economic Recovery Programme (ERP) in 1983. A more liberal, market oriented and therefore more outward oriented policy was introduced. As a result many of the trade restrictions were relaxed. This has led to an expansion of imports and exports with imports outstripping exports in subsequent years. Thus we observe trade and current account deficits for the rest of the 1980s into the 1990s. Because of the policy shift Ghana was also able to attract more official loans, which however led to a rise in debt levels.7

Ghana entered the 1990s with some seven years of structural adjustment behind her. The necessary static efficiency gains emanating from the policy had been achieved and capacity utilisation had improved. What were needed were more dynamic and sustainable gains coming from forward-looking investment decisions and the attainment of a more flexible entrepreneurial response. Policy was therefore increasingly directed towards the strengthening of the private sector and the creation of a conducive environment to achieve such ends.

The deficits on merchandise trade continued into the 1990s. In 1992 gold overtook cocoa as the most important single export. This was on account of heavy investment in gold mining because of the liberalised environment and also favourable prices for gold in the late 1980s and early 1990s. In 1992 gold exports amounted to $343 million, up from $304 million in 1991 as compared to cocoa which contributed $302 million in 1992 down from $346 million in 1991.

7 Policies and performance until the early 1990s have been well documented in Killick, 1978; Jebuni et al. 1994; Oduro, 2000. This study will thus concentrate on the 1990s.
Although current account deficits were experienced throughout the period enough inflows especially in the form of aid came in to fill the gaps. Sometimes though, these were late in coming and thus created budgetary problems.\(^8\) In 1999 and 2000 Ghana experienced a severe deterioration in her terms of trade. The average price of crude oil increased from $10.90 in January 1999 to $24 per barrel in December 1999. The average cocoa price fell from $1434 per tonne in 1999 to $1092 in 2000. Gold had a longer period of decline having fallen from $386 per fine ounce in 1997 to $280 in 2000. To make matters worse the price of timber also fell from $401.7 per cubic metre in 1999 to $351.3 in 2000. Export volume increases, however, mitigated these price declines but the value of exports fell from $2005.5 million in 1999 to $1936 million in 2000 and then to $1867.1 million in 2001.

### Table 3.1: BALANCE OF PAYMENTS (1990 - 2003)

<table>
<thead>
<tr>
<th>Year</th>
<th>Merchandise (In millions of $)</th>
<th>Services (net) Transfers</th>
<th>Capital Flows (net)</th>
<th>Overall Bal.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Export (fob)</td>
<td>Import (fob)</td>
<td>Private</td>
<td>Official</td>
</tr>
<tr>
<td>1990</td>
<td>896.8</td>
<td>-1205.0</td>
<td>-325.4</td>
<td>201.9</td>
</tr>
<tr>
<td>1991</td>
<td>997.7</td>
<td>-1318.7</td>
<td>-352.5</td>
<td>219.5</td>
</tr>
<tr>
<td>1992</td>
<td>986.3</td>
<td>-1456.5</td>
<td>-376.2</td>
<td>254.9</td>
</tr>
<tr>
<td>1993</td>
<td>1063.6</td>
<td>-1728.0</td>
<td>-412.1</td>
<td>261.2</td>
</tr>
<tr>
<td>1994</td>
<td>1237.7</td>
<td>-1579.9</td>
<td>-383.5</td>
<td>271.0</td>
</tr>
<tr>
<td>1995</td>
<td>1431.2</td>
<td>-1687.8</td>
<td>-410.3</td>
<td>263.2</td>
</tr>
<tr>
<td>1996</td>
<td>1570.1</td>
<td>-1937.0</td>
<td>-438.6</td>
<td>276.1</td>
</tr>
<tr>
<td>1997</td>
<td>1489.9</td>
<td>-2128.2</td>
<td>-471.4</td>
<td>400.3</td>
</tr>
<tr>
<td>1998</td>
<td>1813.2</td>
<td>-2346.0</td>
<td>-501.0</td>
<td>453.8</td>
</tr>
<tr>
<td>1999</td>
<td>2012.1</td>
<td>-3228.1</td>
<td>-330.0</td>
<td>472.0</td>
</tr>
<tr>
<td>2000</td>
<td>1936.2</td>
<td>-2766.7</td>
<td>-187.0</td>
<td>499.0</td>
</tr>
<tr>
<td>2001</td>
<td>1884.0</td>
<td>-2830.9</td>
<td>-169.8</td>
<td>689.8</td>
</tr>
<tr>
<td>2002</td>
<td>2015.2</td>
<td>-2707.0</td>
<td>-240.3</td>
<td>472.0</td>
</tr>
<tr>
<td>2003*</td>
<td>2297.2</td>
<td>-2969.4</td>
<td>-371.0</td>
<td>850.5</td>
</tr>
</tbody>
</table>

Source: Bank of Ghana

Throughout the 1990s there was a steady depreciation of the cedi. However the negative shocks experienced at the end of the decade accelerated this process and the cedi-dollar rate rose from ₋2647.32 per dollar to ₋5321.68 per dollar. The consequent increase in the price of imports resulted in a cut in demand for them, which led to a 20% fall in their value. Since the exchange rate is a price any change in it results in potential losses and gains for different actors in the economy. In a well functioning flexible economy, a depreciation would lead to favourable opportunities for exporters and producers of import competing goods who will quickly take advantage of it by increasing production. This action acts as a counter to further depreciation and helps keep the currency stable thus helping to minimise official action to prevent a bigger fall. The steady depreciation that has been experienced over the period is on account of the narrow export base, the lack of substitutes for most vital imports and the general lack of flexibility of entrepreneurial response.

\(^8\)See for instance budget of 1994
3.2 Comparative Advantage, International Competitiveness, Trade and Economic Growth

According to the Heckscher-Ohlin theory a country has a comparative advantage in producing those goods that use intensively the factors it has in abundance. The theory goes on to demonstrate that when countries concentrate on producing those goods in which they have a comparative advantage and exchange them for goods in which other countries have the advantage all countries involved in this kind of exchange will gain. For developing countries trade offers several advantages. Trade can enable a country to achieve rapid economic growth by enabling the country to acquire the vital inputs such as technology to aid in the development process. Through trade the country gets access to expanded markets, which enable full utilisation of local resources. Competition brought on by trade forces local firms to be more efficient and thus more productive. All this aids in the growth process. Ghana can be said to have a comparative advantage in those agricultural goods that thrive in its unique climate. Cocoa, coffee, oil palm, maize, cassava, and yam represent crops that Ghana has advantage in. The presence of minerals confers on Ghana comparative advantage over countries where this is non-existent. Looking at factor endowment, Ghana can be said to be well endowed in low cost labour skills and thus comparative advantage in products requiring this type of labour such as agro based processing, light manufacturing and provision of services like data processing.

Table 3.2: Exports in Millions of dollars

<table>
<thead>
<tr>
<th>YEAR</th>
<th>Gold % Cont.</th>
<th>Cocoa % Cont.</th>
<th>Mineral % Cont.</th>
<th>Timber % Cont.</th>
<th>Non-Trad. % Cont.</th>
<th>% Cont.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>201.7</td>
<td>360.6</td>
<td>242.4</td>
<td>118</td>
<td>62.9</td>
<td>69.0</td>
</tr>
<tr>
<td>1991</td>
<td>304.4</td>
<td>348.7</td>
<td>351.9</td>
<td>124.2</td>
<td>62.6</td>
<td>62.2</td>
</tr>
<tr>
<td>1992</td>
<td>343.4</td>
<td>302.5</td>
<td>388.6</td>
<td>113.9</td>
<td>68.4</td>
<td>6.9</td>
</tr>
<tr>
<td>1993</td>
<td>433.9</td>
<td>284.4</td>
<td>473.5</td>
<td>147.4</td>
<td>71.7</td>
<td>6.7</td>
</tr>
<tr>
<td>1994</td>
<td>548.7</td>
<td>320.2</td>
<td>588.2</td>
<td>165.4</td>
<td>119.3</td>
<td>9.4</td>
</tr>
<tr>
<td>1995</td>
<td>647.3</td>
<td>389.5</td>
<td>678.8</td>
<td>190.6</td>
<td>159.7</td>
<td>11.2</td>
</tr>
<tr>
<td>1996</td>
<td>612.4</td>
<td>551.8</td>
<td>641.3</td>
<td>146.9</td>
<td>276.2</td>
<td>17.6</td>
</tr>
<tr>
<td>1997</td>
<td>579.2</td>
<td>470</td>
<td>613</td>
<td>172</td>
<td>329.1</td>
<td>21.1</td>
</tr>
<tr>
<td>1998</td>
<td>687.8</td>
<td>620.4</td>
<td>717.9</td>
<td>171</td>
<td>401.7</td>
<td>22.2</td>
</tr>
<tr>
<td>1999</td>
<td>710.8</td>
<td>552.3</td>
<td>749.1</td>
<td>174</td>
<td>404.4</td>
<td>20.1</td>
</tr>
<tr>
<td>2000</td>
<td>702.0</td>
<td>437.1</td>
<td>755.9</td>
<td>175.2</td>
<td>400.7</td>
<td>20.7</td>
</tr>
<tr>
<td>2001</td>
<td>617.8</td>
<td>381.1</td>
<td>691.4</td>
<td>169.3</td>
<td>459.6</td>
<td>24.4</td>
</tr>
<tr>
<td>2002</td>
<td>689.1</td>
<td>463.4</td>
<td>756.5</td>
<td>182.7</td>
<td>504.3</td>
<td>25.0</td>
</tr>
<tr>
<td>2003*</td>
<td>710.8</td>
<td>30.9</td>
<td>802.2</td>
<td>893.6</td>
<td>588.9</td>
<td>25.6</td>
</tr>
</tbody>
</table>

Source: Ghana Statistical Service

However comparative advantage in these fields is only potential. Much work is always needed to translate this potential advantage to actual advantage. A certain environment is needed to facilitate economic activities. These include –

- a well functioning trade infrastructure consisting of roads, warehousing, port facilities and other transport related infrastructure
- reliable supply of utilities such as electricity, water and telecommunications
- a hardworking and disciplined labour force operating in a flexible labour
market which ensures fairness to both employers and employees

- transparency and honesty on the part of public officials
- an environment in which information flows freely to enable economic agents to make appropriate decisions

Unfortunately the environment in Ghana at the moment is far from these ideal conditions. A World Bank study on international competitiveness in Ghana showed that transport costs are generally higher than international and even some regional rates (World Bank, 2001). Poor investment in the rail network over the years has led to its virtual collapse. At the moment only a part of the network is functioning. The capacity of this functioning part, i.e., Kumasi to Takoradi has fallen and transporting bulk items such as bauxite have become problematic.\(^9\)

Although telecommunications services have expanded greatly in recent years service remains poor with inter-connection between fixed line and mobile providers remaining poor (see Jebuni and Laryea, forthcoming). There have been numerous reports of corruption in the judicial service\(^{10}\) and Ghana’s record on corruption as evidenced by the latest Transparency International Report though better than most African countries evaluated remains poor.\(^{11}\)

Other problems identified by the World Bank study include lack of a ‘cold chain’ – that is, a series of mobile chillers, refrigerated trucks and cold storage facilities to reduce the spoilage time between harvest and sale. This is particularly important for horticulture, an area with a lot of potential for Ghana.

Furthermore a slow moving bureaucracy which creates delays in registering companies and difficulties when going through customs procedures have been identified. Lack of easy access to land for productive purposes has also been particularly problematic over the years. All these problems impose huge costs on companies. Many firms also report that information from government representatives participating in international trade meetings is disappointing (World Bank, 2001).

All these problems serve to increase transactions cost and thus reduce Ghana’s competitiveness. Thus one cannot only consider resource endowment when looking at comparative advantage and competitiveness but also the complementary environment, which translates a potential comparative advantage into an actual one. On this score Ghana can be said to have a lot of unfulfilled potential. Moreover it should be noted that Ghana produces and exports a myriad of goods in which she has preferential market access to the EU market. These include tuna and

\(^9\)Some efforts at rehabilitation are being made at present. Three foreign firms have submitted bids to rehabilitate the network (Daily Graphic of April 2004).

\(^{10}\)For instance the 1997 Auditor-General’s Report concluded that Ghana’s Judiciary was steeped in corruption. Also in an editorial of ...the Ghanaian Chronicle stated that “it is an open secret that some tribunal chairman collect bribes from accused persons and even at times from plaintiffs.”

\(^{11}\)In the latest survey Ghana scored 3.9 out of a possible 10.
palm oil. For tuna Ghana currently enjoys duty free access while Asian exports are subject to a 24% duty. These preferential access provisions are however not permanent and are actually under threat in the new global trade environment under the World Trade Organisation (WTO). Also Ghana has to comply with a growing number of EU regulations on environment and food safety standards.

One factor that is very important for competitiveness is the real exchange rate. This is the nominal exchange rate adjusted for inflation between Ghana and her trading partners. This measure is more relevant for price competitiveness since it reflects the affordability of Ghana’s products as compared with those of her trading partners. Table 3.3 shows that for much of the 1990s there was a real appreciation of the cedi as the nominal exchange rate did not depreciate sufficiently to counteract the increase in inflation. This was on account of the Bank of Ghana’s use of the exchange rate as a nominal anchor against inflation, i.e., intervening to keep the nominal rate constant in order to keep inflation low rather than seeing the exchange rate as a tool that affects competitiveness (CEPA 1997, 1998).

This could partly account for the widening trade deficit over the period. The massive nominal depreciation that occurred in 2000 moved the real exchange rate more than sufficiently to maintain competitiveness. That is, there was a real depreciation. Since the beginning of this decade, the real exchange rate has been slightly undervalued (Table 3.3). Many have argued that the use of the exchange rate as a nominal anchor against inflation is wrong since it undermines the competitiveness of Ghana’s economy (CEPA, 1998).

### 3.3 Import and Export Composition

The composition of imports and exports generally reflect Ghana’s comparative advantage. Imports over the years have consisted of industrial goods such as construction machinery, and services such as insurance and freight. These products use factors that are relatively scarce in Ghana – capital and skilled labour. A lot of technology is also embodied in these imports. Over the years the composition of these imports has not changed much. In the years following independence Ghana’s import substitution strategy enabled some substitution for imports to be achieved. But many of these industries were highly dependent on imported inputs and with a deteriorating foreign exchange position over the years these industries have struggled and very little further progress was achieved. With the coming into force of the trade liberalisation policy cheap imports from the Asian countries have meant that the range of imports have rather expanded as have the absolute value of total imports. Between 1990 and 2001 exports of merchandise increased from $896.8 million to $1867 million – an increase of 108% while there was a much larger increase in imports by 146% – i.e. from $1205 million to $2968 million. One particular fact worth mentioning is the growth of poultry imports. There was a substantial increase in the second half of the 1990s from 2,314 metric tonnes in 1992 to 10,766 in 1999.
Protests from the poultry industry in 2003 caused the government to impose additional taxes on imported poultry but these were withdrawn almost immediately.\textsuperscript{12}

The main exports over the year have remained cocoa, timber, gold and other minerals. These also reflect Ghana’s endowment in natural resources. During the 1990s the government made a lot of efforts to widen this narrow base of exports. Changes have come very slowly and the percentage of non-traditional exports increased steadily albeit from a narrow base. Between 1988 and 2001 there was a ten-fold increase in the value of non-traditional exports and the number of items exported expanded from 166 to 260. Its proportion to the total value of merchandise exports jumped from 6.7% in 1988 to 25% in 2001. Ghana therefore appears to be slowly diversifying its export base. The impressive thing about the trend is that most of these items are processed and semi-processed goods. In 1988 the number of agricultural non-traditional exports was 65 with a total value of $27.1 million representing a percentage of 63.9.

\begin{table}[H]
\centering
\begin{tabular}{|c|c|c|}
\hline
Year & Exchange Rate & Real Effective Exchange Rate 1995=100 \\
\hline
1980 & 2.75 & 652.13 \\
1981 & 2.75 & 1437.21 \\
1982 & 2.75 & 1795.48 \\
1983 & 30.00 & 1209.48 \\
1984 & 50.00 & 469.36 \\
1985 & 59.99 & 339.23 \\
1986 & 90.01 & 194.98 \\
1987 & 176.06 & 151.65 \\
1988 & 229.89 & 145.88 \\
1989 & 303.03 & 136.92 \\
1990 & 344.83 & 136.30 \\
1991 & 390.63 & 139.36 \\
1992 & 520.83 & 123.11 \\
1993 & 819.67 & 108.10 \\
1994 & 1052.63 & 86.89 \\
1995 & 1449.28 & 100.00 \\
1996 & 1754.39 & 108.99 \\
1997 & 2272.73 & 115.51 \\
1998 & 2325.58 & 124.94 \\
1999 & 3535.14 & 125.56 \\
2000 & 7047.65 & 80.98 \\
2001 & 7321.94 & 81.50 \\
2002 & 8438.82 & 80.98 \\
\hline
\end{tabular}
\caption{Exchange Rate Trends (c/$)}
\end{table}

Source: IMF’s International Financial Statistics (various years)

\textsuperscript{12}According to critics of the withdrawal the government bowed to pressure from the IMF and World Bank but both these institutions and the government have denied this.
By contrast processed and semi-processed items were 82 representing a value of $15.2 million giving a contribution of 35.9% by 1999 there had been a substantial change in these proportions - the number of agricultural products had increased slightly to 72 with a value of $77.8 million representing 20.9% of non-traditional exports. By contrast the number of semi-processed and processed goods had expanded to 178 with a value of $313.3 million representing 77.5%. Non-traditional processed and semi-processed products include items such as wood products, aluminium products and prepared foods.

3.4 FDI Flows: Sources, Activities, Ownership, Joint Ventures

Generally investment is financed through saving and if a country can save enough it should be able to meet its investment needs. When saving is too low to finance investment needs foreign saving has to come in the form of investment flows.

<table>
<thead>
<tr>
<th>Table 3.4 Evolution of Non-Traditional Exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>-------</td>
</tr>
<tr>
<td>Value</td>
</tr>
<tr>
<td>Agric.</td>
</tr>
<tr>
<td>Processed</td>
</tr>
<tr>
<td>Handicraft</td>
</tr>
</tbody>
</table>

Source: Ghana Export Promotion Council

Between 1980 and 1999 Ghanaian saving rate averaged 6% of GDP while domestic investment averaged 13.9% (World Bank, African Development Indicators 2002 CD-ROM). The shortfall is made up by inflows from abroad. With the launching of the ERP in 1983 Ghana became a large recipient of Overseas Development Assistance (ODA). ODA inflows constituted over 50% of capital formation compared with the Sub-Saharan African average of 34%. Often ODA inflows were linked to some FDI projects.

After the stabilisation phase of the ERP government began to pay more attention to structural problems and getting investment to flow in. Thus a new mining law was enacted in 1986 to encourage investment in natural resources. FDI flows which had fallen drastically to single digits in the early 1980s remained extremely low for most of the rest of the 1980s. The low levels might have been due to a wait-and-see attitude by potential foreign investors as there was a lot of uncertainty as to how committed the government was to reform. There was a modest increase in 1989 as confidence grew slowly and government started the privatisation process. There was a steady increase in subsequent years as the privatisation process took off and more inflows came.

The significant increase in investment inflows to $233 million in 1994 was on account of the partial sale of AGC to the South African mining company Lomin. Following this, six other companies including Accra Brewery and Standard Chartered Bank had the government offloading its majority shares in them, and again in 1996 sold its 30% of the shares of Ghana Telecom to Telekom Malaysia. After 1996 the flows declined again. By then the government had divested full or partial stakes in the largest banks, mining, manufacturing and service companies. It had difficulty in finding strategic partners for the remaining firms. Benefits of privatisation were being questioned and
the Ghanaian government was having a dispute with AGC, which had implications for investor confidence. The main problem though was the decline in economic activity starting with the energy shortage of 1997/98. There was a recovery in 1999 and 2000 though flows fell again in 2001 and 2001.

In spite of these improvements, however, the performance is low compared to that of similar African countries. According to a 1999/2000 survey by the United Nations Conference on Trade and Development (UNCTAD) Ghana ranks sixth among African countries in terms of attractiveness of the investment climate. In terms of inflows however Ghana ranked only 21st. This poses a big challenge for the government and other stakeholders.

Investors have been mainly attracted to the natural resource sector. The greatest proportion goes into mining. The fact that the government retains a 10% free share does not appear to have deterred investors. In the energy sector VRA has encouraged investment from independent power producers. Companies involved in projects to expand capacity include GE Hydro, CMS, and Marathon Power all of which are US companies. In the manufacturing sector investment has mainly concentrated in resource based processing and exports. Leading investments include the Pioneer Food Cannery, partially owned by Heinz US and engaged in the processing and canning of tuna, and West Africa Mills which processes cocoa and is owned by a German firm. Other notable investments include Guinness Ghana limited – Ireland, Ghana Agro Food Company – Germany, Coca-Cola – US, Accra Brewery – South Africa, Cadbury’s of UK and Nestlé of Switzerland.

Services have attracted a smaller volume of investment than the other sectors. Most of these have been attracted into the banking sector, with two merchant banks and a commercial bank attracting strategic foreign investors in 1991. There are now some 17 foreign banks and a number of leasing companies, two Savings and Loans companies, and two discount houses.

Traditionally most investments come from Europe especially from Britain. This is on account of colonial ties. Since the ERP, investors from other regions have been playing a bigger role. South African investors are now major participants in the mining sector and also the brewing and retail sectors. Asian investors however now account for the largest investments. Malaysia Telekom has a 30% stake in Ghana Telecom and other Malaysian companies are involved in television and film, infrastructure and the provision of services for the free trade zone. While the UK still has the largest number of projects, it ranks only fourth by investment value after Malaysia, the US and Switzerland. There are also a large number of foreign investors from India, Lebanon, and Syria who serve the domestic and tourist markets through general trading, import-export and in the hospitality sector.

Between 1994 and December 2002 the Ghana Investment Promotion Centre (GIPC) registered 1189 FDI projects. Of these 410 projects are in the services sector, 387 in manufacturing, 165 in tourism, 111 in building and construction and 116 in the agricultural sector.
427 projects are wholly foreign owned while 966 are joint foreign-Ghanaian owned. Foreign capital invested in these projects amount to $1.5 billion. 139 projects come from Great Britain, 116 from India, 110 from China. Also the US has 94, Lebanon has 84, Germany has 83, South Korea has 53 and Italy has 50.

While the importance of Britain reflects the colonial relationship it is noteworthy that developing countries such as India and China are also important. Two African countries, Nigeria and South Africa also have a substantial presence with 37 and 26 projects respectively. The bulk of the projects are in Greater Accra with 79.2% followed by Ashanti with only 7.1%. There is obviously a need for Ghana to ensure through a tweaking of the incentive structure a better distribution of projects.

FDI has had a big effect on trade in the 1990s. The great success achieved with non-traditional exports has been linked with FDI. According to the World Bank exports from locally based foreign firms accounted for 75% of the increase in earnings recorded over the 1995 and 1999 period and represented about 34% of the value of non-traditional exports in 1999. These include furniture manufacturing, canned, chilled and frozen fish products to European markets, and clothing to the US. The development of the Free Trade Zone has also helped to improve export-oriented FDI. By the end of 2000, 32 manufacturing firms were operating under free zone status exporting a total of $251 million accounting for 13% of total exports (Source??). The most evident example of the effects of FDI on trade is in gold mining, which has experienced an increase in gold production of 500% between 1990 and 2000.

Other wide-ranging effects of FDI include technological improvements that have occurred in the gold sector and the telecommunications sector as well as the enhancement of infrastructure within these sectors.

### 3.5 Trade Policy and Regulation

The broad policy objective as expressed by the government throughout the 1990s was to maintain the flexible exchange rate regimes that had been established in the late 1980s. Though flexible the idea was also to ensure that it is stable hence a policy of building up reserves was also pursued so that targeted interventions could be made to ensure this stability. Liberal trade policies were also to be pursued to ensure that imported inputs could come in easily to facilitate industrial production.

Having an exchange rate that is freely determined by market forces and thus is neither undervalued nor overvalued is considered to be consistent with an outward oriented policy. As a result one overriding goal of policy throughout the 1990s was a major push to add to the range of exports produced - i.e., to expand the range of non-traditional exports.

A policy of maintaining flexibility but also ensuring stability might be contradictory if not carefully pursued. The essence of ensuring flexibility is to allow the free interplay of market forces so that the exchange rate will provide correct signals to what is happening on the ground for economic agents to act on. Too much enthusiasm for stability can have the unintended effect of distorting the signals that economic agents need. What is needed in pursuing such a policy is a careful reading of the factors that
are putting pressure on the currency at any particular time in order to distinguish the fundamental ones from the merely speculative. Intervention is only necessary when the pressure has nothing to do with fundamental, long term movements in economic forces.

As already mentioned what is more important for the goal of maintaining competitiveness is the real exchange rate rather than the nominal exchange rate. Thus the ultimate goal is to maintain stability in the real exchange rate, which might not necessarily mean a stable nominal rate. When the big shocks of 1999 and 2000 hit the nominal exchange rate depreciated rapidly. Such a fall in the value of the currency has always been problematic for government, and there was pressure on the government to resort to the sort of restrictive measures that were adopted in the 1970s, but apart from raising tariffs on some goods this direction was not seriously pursued.

Great efforts were made in the 1990s to expand the production of non-traditional exports. Prominent among efforts made was the Trade and Investment Programme (TIP) sponsored by the United States Agency for International Development (USAID). This Programme lasted from 1993 to 1997 and focussed on the creation of an enabling environment and the provision of institutional support for exporters. The TIP put in place the Trade and Investment Management Unit which comprised all Ministries and other organisations whose activities relate to export development. Some achievements made included the removal of foreign exchange control measures that required non-traditional exporters to surrender most of their foreign exchange earnings to the monetary authorities and the removal of restrictions on what can be exported.

Another programme introduced was the Private Enterprise and Export Development Programme (PEED) which was designed to provide export financing in foreign exchange or in cedis to Ghanaian non-traditional exporters. Other incentives provided included the waiver of duty for exporters who used imported inputs.

During the 1990s the Ghana Export Promotion Council (GEPC) could be described more of a promotional agency than a regulatory one. In line with this a Product Development Division was created within the council to help identify new products and producers, organize exporters into production associations and provide information to entrepreneurs in the field. Education programmes were also organised for exporters and export facilitators throughout the period as well. Additionally, solo exhibitions in selected ECOWAS countries were organised to promote exports into the sub-region.

In October 2000 the US government passed the African Growth and Opportunity Act (AGOA) which designated 34 Sub-Saharan African countries as beneficiaries of special trade preferences. The purpose of AGOA as stated by the Act was to strengthen US relations with African countries and to encourage African countries to pursue political and economic reforms and achieve higher economic growth. To take advantage of AGOA the Ministry of Trade and Industry (MOTI) in 2001 established the AGOA National Committee to advice on the visa system and customs procedures, marketing, and publicity of export products.
In 2001 a President’s Special Initiatives on Accelerated Export Development was launched. The aim of the Initiative was to target areas which were deemed to have potential. In pursuance of this, support was given for the setting up of a private company, The Ayensu Starch Factory, to process the output of out-grower cassava farms into high grade industrial starch for export. Similar support is being given to the textiles and garments sector to take advantage of AGOA. Other areas designated for support include palm oil and salt.

To provide support for distressed but potentially viable enterprises an Export Development and Investment Fund (EDIF) was launched in 1998. This was to be used as a guarantee scheme to leverage financing available from the banks. The industries targeted for support were textiles and garments, wood and wood processing, food and food processing and packaging. The EDIF law was enacted in 2000 and operations of the fund started in July 2001. Money was to come from 10% of divestiture proceeds and a levy on dutiable values of all non-petroleum products imported for commercial purposes.

To facilitate the operation of a free market economy through a liberalized trade sector a Restrictive Business Practices (RBP) Law was passed in 1993 in order to check unethical business practices. The law was to ensure a conducive environment for the conduct of business in Ghana. The Private Enterprise Foundation (PEF) was also established to consolidate and strengthen private sector associations in the country.

While the primary efforts of policy have been to promote the export of non-traditional exports with positive results being achieved, much focus remained on traditional sectors. For cocoa the main objectives of current policies are to raise cocoa production from 400,000 tonnes to 500,000 tonnes by 2004/2005 and to 700,000 by 2009. Other objectives included the maintenance of Ghana’s distinctive position as the supplier of the finest and most consistent quality cocoa and in addition retain the traditional premium obtained by Ghana’s cocoa on world markets. Measures taken include the privatisation of distribution of inputs to farmers, and the provision of credit to purchase inputs following the removal of subsidies on inputs. Since 2001 government has intensified its mass spraying of cocoa farms.

A big problem has been the percentage of the proceeds paid to farmers. One of the policy objectives of the structural adjustment programme was to raise this percentage. From levels of around 20% in the early 1980s there was a gradual increase to about 46% in 1992. This proportion however fell in the mid-1990s as producer price increases were not transferred to farmers. Over the past two years the aim of policy has been to raise this percentage to 70%. Currently it is 68%. The operations of Ghana Cocoa Board (COCOBOD) were also streamlined in order to reduce overheads and to intensify research on diseases and pest controls.

Gold production has increased since the ERP began because of the more favourable investment climate created, which allowed investment in the sector to expand. The broad policy objectives for the mining sector have been:

- incentives to increase and sustain investment in the sector,
- avoidance of degradation of the environment, and
- ensuring that people in the sector benefit from exploitation of the mineral resources.
More specific incentives relate to encouraging foreign investment and these are discussed in the section on FDI policy.

For timber, a new Forest and Wildlife policy was adopted in 1994 under which the government initiated a series of control measures including a ban on the export of logs, the designation of resource areas and the concept of “annual allowable cut”. A Timber Resource Management Act was also passed in 1998 to improve the allocation system of logging permits and to control illegal chainsaw operators. The Act also provided for a more efficient and transparent allocation process based on a new contract scheme – the Timber Utilization Contract (TUCs). Under the system firms bid for contracts to log particular sections of the forest. Each contract has a duration of 40 years and is renewable as long as the contractor manages its designated logging area according to specified criteria. Implementation however still suffers from malpractices (UNCTAD, 2003). Other policy initiatives include encouraging the use of lesser known species and the placement of levies on exports to support reafforestation.

A big problem for the government over the years has been the increased competition faced by local industry, who hitherto had operated behind stringent protective walls. Having been set up in a policy environment promoting import substitution they have become more like dinosaurs in an environment encouraging free competition from the outside world. Over the years the government has tried to give some support to these industries or at least try not to further erode their competitiveness. Thus in 1994 when the import sales tax was rationalised by narrowing the gap between duty rates similar rates were set for domestic sales taxes. On the import side the policy of trade liberalisation continued and restrictions on imports were further eased.

The dilemma facing the government in dealing with local manufacturing concerns can be summed up in this statement by the Minister of Finance in the 1994 budget: “Many domestic industries have high import and capital intensities and relatively low domestic value added. As a result anything short of the outright banning of competing imports will continue to be seen by them as providing inadequate protection.” One might argue though that part of the reason making domestic industry uncompetitive is the poor nature of the domestic infrastructure and the general business environment which increases transaction and other costs. Further improvement in this direction therefore might minimise the need to use trade restrictions to support the sector.

3.6 FDI Policy and Regulations
From the time of independence when the Nkrumah government viewed foreign investment with suspicion, because it perceived this kind of investment as exploitative, there has been a radical change in attitude by the various governments since 1983. Policies encouraging foreign investment were pursued first with the Investment Code of 1985. This Investment Code which was revised in 1991 covered all areas of investment with the exception of petroleum and mineral investment, which are regulated by the Ghana National Petroleum Corporation and the Minerals Commission respectively. The Investment Code consolidated all relevant legislation affecting investment and was the first manifestation of the new thinking on investment.
A new investment code superseding all earlier ones was enacted in 1994. Under this code investment by foreign concerns which had already been liberalized earlier was further liberalized. At the time of its enactment it was praised as the best in Africa (UNCTAD, 2003). Under this new code the Ghana Investment Promotion Centre was established with the express aim of encouraging and promoting investment in the Ghanaian economy. It eliminated the need for prior approval, eased the establishment of companies and provided incentives and guarantees to investors.

Incentives provided included:

- the depreciation of the capital allowance of 75% of capital expenditure incurred in the year of investment and in subsequent years,
- the free transferability of profits and dividends,
- foreign exchange retention accounts through which all foreign payments including dividends can be made,
- exemption from payment of customs duties on machinery and plant for the establishment of mines and further relief for selected items for on-going mining companies, and
- the establishment of well-defined rules for dispute settlement.

Under the Act only the following types of businesses were reserved exclusively for Ghanaians - the sale of anything whatsoever in a market, petty trading, hawking or selling from a kiosk at any place, operation of taxi and car hire services operating less than ten vehicles, pool betting business, beauty saloons and barber shops. With the exception of these, foreigners could operate any enterprise in the country.

In the case of a joint enterprise with a Ghanaian partner, the non-Ghanaian shall invest no less that $10,000 of the capital. Where it is wholly owned by a non-Ghanaian the investment of foreign capital shall be not less than $50,000. In the case of enterprises engaged in only the purchasing and selling of goods the investment of foreign capital shall be at least $300,000. Although these figures are low compared to developing countries, it must be stated here that most developing countries have abolished such requirements. In fishing, non-Ghanaians could hold no more than 50% of the stake while this figure is 40% in the insurance industry. Also foreign ownership of a publicly listed company on the stock exchange could be no more than 75%.

The minimum capital requirements however do not apply to portfolio investment or an enterprise set up solely for export trading. Generous repatriation of investment income was also provided for in this act. Thus no restrictions whatsoever were placed on the repatriation of this income provided obligations such as taxes have been met. Guarantees were also provided against expropriation by government, and where the government deems it in the national interest to expropriate any concern, a fair and adequate compensation and a right of access to the High Court were provided for. Any dispute not amicably settled may be submitted to international arbitration.

In mining a new mining code was enacted in 1983. Under this code government retains a 10% free share in any mining venture with the option of acquiring an additional 20%, which confers on it a managerial share.
To further encourage investment into the country the Ghana Free Zones Board was set up in August 1995 under the Free Zone Act of 1995. Companies that operate under this act enjoy the following privileges:

- total exemption from payment of direct, indirect duties and levies on all inputs for production and sale of export products manufactured in the free zone, including VAT. This applies to plant and equipment, raw materials and intermediate goods;
- total exemption of income tax on profits for the first 10 years. Upon expiration of the 10-year holiday, the enterprise is only liable to a tax not exceeding 8% as long as it operates in the free zone. In return the enterprise must export at least 70% of its products while the rest can be sold on the Ghanaian market.
- a hundred percent foreign ownership was allowed.
- there is relief from double taxation for foreign investors and employees.

The free zones were demarcated as follows;

- 680 acres of land for the development of the Tema Export Processing Zone which has been leased out to Business Focus Group of Malaysia and it plans to bring in several electronics firms
- 2,200 acres of land at Sekondi
- the sea ports of Tema and Takoradi and also Kotoka International Airport
- Fumesua near Kumasi which has the added advantage of being developed into an inland free port – the first in West Africa

As of 2000, 78 firms had registered to operate in the zone of which 52 were operational employing some 6000 people.

To support the initiatives adopted to attract investment into the country, the Ghana Trade and Investment Gateway project was launched in 1999. The project is to help modernise equipment and raise the human capacity base of the Customs, Excise and Preventive Service (CEPS), Ghana Ports and Harbour Authority, Ghana Investment Promotion Centre, Ghana Immigration Service and the Ghana Free Zones Board for the prompt handling and the provision of offsite infrastructure for the export processing zone enclave.

The object of the Gateway Project is to attract a critical mass of export-oriented firms to kick-start export-led growth as well as facilitate trade. This involves the creation of an enabling environment to facilitate the increased level of private investment, reduce the cost of doing business as well as providing the necessary infrastructure services as well as the provision of off-site infrastructure for on-site facilities.

While Ghana has made a lot of progress since the ERP in attracting foreign investment a lot of work still needs to be done. Ghana’s investment code of 1994
which stood out at the time of its enactment among African countries has now been superseded by others. While a survey carried out by UNCTAD confirmed the attractiveness of Ghana’s Free Zone as a one-stop regulatory authority which reduces the time consuming process of dealing with multiple agencies investors identified certain shortcomings in the same survey (UNCTAD, 2003). These include the provision of technology, education, access to credit and fiscal incentives. Fiscal incentives include delays in paying duty drawback and VAT refunds on imported inputs. Access to land is also a serious problem that was identified in the survey.

Even though the new mining law is a vast improvement over what existed before it has been criticised for having low investor after tax return. A recent financial modelling of Ghana’s fiscal regime in comparison with that of five leading mining countries shows its fiscal take to be the highest and most onerous on the investor. The fiscal take is the net present value of state take from taxes, royalty and concessionary state equity. One significant weakness of the investment climate in the country is that firms that do not operate in the Free Zone lack “a one-stop shop” for registering their business. Numerous agencies are involved in the registration process and valuable time is wasted.

3.7 External Debt
In 2001 Ghana decided to take advantage of the Enhanced Heavily-Indebted Poor Country Initiative (HIPC) launched by the IMF. This was an admission that Ghana’s debt situation had become unsustainable based on the IMF and World Bank definitions. While Ghana had its first debt crisis in the 1960s debt levels fell in the 1970s as very little new debt was contracted. The oil crisis of 1979 again brought the problem to the fore and after the ERP of 1983 there was a substantial increase in debt levels as the levels of concessionary loans increased substantially.

Under ERPII, Ghana had some assistance with debt rescheduling through the Extended Fund Facility and the Structural Adjustment Facility. Under an even more favourable Extended Structural Adjustment Facility (ESAF) in 1988, Ghana received an IMF loan on softer terms amounting to SDR 506 million but this did not prevent a net repayment to the IMF between 1987 and 1992.

Debt levels continued to increase steadily in the 1990s. However the structure of debt has become more favourable. The proportion of long-term debt has steadily increased over the years so that in 2001 it was 88% of total debt compared with 62% in 1990. The level of short term debt was low in the early 1990s but then increased substantially in 1993. This proportion, which increased from 1.54% in 1990 to 4.7% in 2001, however remains low. The absolute levels of medium term debt though have decreased over the years. In 1990 it was over 20 times the level of short-term debt but by 2001 it was only one and a half times as much. Its proportion has also fallen considerably to 7.5% in 2001 from 36% in 1990.

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13The modelling was carried out by Transborder Advisory Service, a private consulting firm with special expertise on mining policy issues. Countries studied were Chile, Indonesia, Peru, Papua-New Guinea, and Tanzania.
The Debt Service Ratio which has been fluctuating between 1990 and 1997 dropped considerably in 1998 and has continued to drop since then. Payments made reflect the structure of the debt so that long term debt payments have seen an increase. One unfavourable statistic though is the Total Debt/GDP ratio. This has been increasing since 1990. It increased substantially in 1993 to 82.65% and then bumped up again substantially to 121.1% in 2000. One sad fact about the debt problem has been that debt rescheduling under more favourable conditions has been taking place since 1987 with the IMF Extended Fund Facility and the Structural Adjustment Facility but this relief was being used to service earlier loans rather than being invested.

A World Bank report on Trends in Developing Countries in 1993 classified Ghana’s level of indebtedness as severe. Ghana has successfully followed a policy of relying on concessionary borrowing rather than on commercial loan. This has not helped in terms of the sustainability of the debt.

The Highly Indebted Poor Country (HIPC) Initiative was introduced in 1996 due to a combination of three factors:
- pressure from NGOs led by Jubilee 2000 for debt relief,
- implementation of the Brady Plan that provided debt relief for middle income countries, and
- a number of low income countries were not servicing their debt anyway.

To be eligible for debt relief under HIPC a country must qualify for concessional assistance under the IMF and World Bank. In addition it must face an unsustainable debt service even after application of traditional debt relief mechanisms. Under the original HIPC initiative the critical values for sustainability were;
- a net present value of public and publicly guaranteed debt equivalent to 200-250% of exports,
- external debt service to export ratio of 20-25%, and
- a net present value of debt to fiscal revenue ratio of 280% This applied to countries that had a ratio of exports to GDP of 40% and revenue to GDP ratio of 20%.

The enhanced HIPC initiated in 1999 after considerable criticism of the original one relaxed these requirements to these;
- it lowered the sustainability target for net present value of debt to export ratio from 200-250% to 150%,
- it lowered the sustainability target for net present value of debt to revenue ratio from 280% to 250%, and
- it lowered the threshold for eligibility under fiscal criterion from 40% to 30% for the export to GDP ratio and 20% to 15% for the revenue to GDP ratio.

Ghana became one of the countries that became eligible for consideration for debt relief due to the enhancement of the Initiative. However Ghana’s indicators were not significantly above the critical values. The amount of debt relief that Ghana would have qualified for therefore was not very large (CEPA, 2002). Also Japan had warned that Ghana would no longer be eligible for its loans, although the Japanese’s stance on this has waned since.
Ghana had however begun accessing the Poverty Reduction and Growth Facility which replaced the Enhanced Structural Adjustment Facility in November 1999. This new facility required the preparation of a poverty reduction strategy paper (same as under HIPC) and thus by the time Ghana finally decided to join the HIPC Initiative in 2001, some progress had been made preparing the paper.

An assessment of Ghana’s debt sustainability indicators in February 2002 based on end of December 2000 figures put the net present value of debt to revenue ratio at 570% and the net present value of debt to export ratio at 157% (IDA and IMF, 2000). The amount of debt relief Ghana is expected to receive under the enhanced HIPC was calculated on the basis of the fiscal criterion, as the export to debt ratio was not favourable in terms of the amount of relief. It is estimated that the total debt relief required to bring down the net present value of the ratio of debt to revenue to below the critical value of 250% is $2186m (CEPA, 2002).

**Table 3.5 Debt** (millions of US$)

<table>
<thead>
<tr>
<th>Year</th>
<th>Short-Term</th>
<th>Medium-Term</th>
<th>Long-Term</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>53.83</td>
<td>1254.61</td>
<td>2178.59</td>
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<tr>
<td>1991</td>
<td>29.35</td>
<td>1329.81</td>
<td>2443.70</td>
<td>3802.86</td>
</tr>
<tr>
<td>1992</td>
<td>71.16</td>
<td>1346.44</td>
<td>2731.61</td>
<td>3968.88</td>
</tr>
<tr>
<td>1993</td>
<td>197.17</td>
<td>1252.33</td>
<td>3230.47</td>
<td>4679.97</td>
</tr>
<tr>
<td>1994</td>
<td>267.60</td>
<td>1212.91</td>
<td>3514.66</td>
<td>5022.17</td>
</tr>
<tr>
<td>1995</td>
<td>270.50</td>
<td>976.00</td>
<td>3827.76</td>
<td>5074.26</td>
</tr>
<tr>
<td>1996</td>
<td>286.00</td>
<td>881.70</td>
<td>4179.25</td>
<td>5346.95</td>
</tr>
<tr>
<td>1997</td>
<td>287.00</td>
<td>769.49</td>
<td>4594.91</td>
<td>5651.40</td>
</tr>
<tr>
<td>1998</td>
<td>295.00</td>
<td>646.55</td>
<td>4980.03</td>
<td>5921.58</td>
</tr>
<tr>
<td>1999</td>
<td>295.00</td>
<td>501.03</td>
<td>5071.88</td>
<td>5867.91</td>
</tr>
<tr>
<td>2000</td>
<td>275.00</td>
<td>382.66</td>
<td>5404.34</td>
<td>6062.00</td>
</tr>
<tr>
<td>2001</td>
<td>300.00</td>
<td>471.24</td>
<td>5600.53</td>
<td>6376.77</td>
</tr>
<tr>
<td>2002</td>
<td>360.00</td>
<td>528.30</td>
<td>5697.03</td>
<td>6585.33</td>
</tr>
</tbody>
</table>

Source: Bank of Ghana

The enhanced HIPC relief is expected to reduce debt service payment due by about $215m per year on average between 2002 and 2011.

There is still considerable dissatisfaction with the debt relief process. The debt relief that is provided is regarded by supporters of debt relief such as Jubilee 2000 as limited. There is also some evidence that donor countries are reducing aid flows at the same time as relief is granted (Ranis and Stewart, 2001). Overseas development assistance to Africa fell in per capita terms in the 1990s. For Ghana official aid assistance which stood at $505.04m in 1991, fell drastically and although some recovery took place it has not reached that level since. In 2000 it was $315.86m (CEPA, 2002). As a result of taking advantage of the HIPC Ghana saw debt relief of $249 in 2002 by about 4% of GDP.
3.8 Expected Policy Reforms
Since the launch of the Economic Recovery Programme, Ghana has seen a lot of activity in the trade sector with many policy initiatives taken to buttress the initial programme. The movement has been towards creating a more market oriented economy in which private economic agents acting in their self interest drive the economy. This is reflected in the oft quoted slogan of the private sector being the engine of growth. It is expected that this will continue to be the direction in which the economy will move in a fundamental way. The trade shocks of the late nineties and 2000 created some pressure to go back to the control measures of the seventies but the fact that this was not done indicated that the current direction taken will not be changed easily. A big problem for the economy remains those kinds of industries set up under heavy protective barriers in the 1960s that still need protection. The international environment under the auspices of the World Trade Organisation (WTO) is less friendly to protectionist measures. Also governments are becoming increasingly aware of the welfare costs to consumers of protectionist measures. What this means for Ghana is that less support will be forthcoming for domestic industries whose structure is such that they cannot compete. Also we should expect more initiatives to support sectors in which Ghana can compete with the best there is in the world. We should expect further removal of institutional bottlenecks, streamlining of rules and the creation of better infrastructure.

Furthermore it has been increasingly realised that a stable macro environment is very important for creating a thriving export sector. We should thus expect more fiscal prudence and legislation to make the Bank of Ghana more independent and thus more able to resist government borrowing pressure.

All in all we should expect an economic environment which is more like that of the successful economies of Asia and less like the command economies of the old Soviet Union.