Ghana: Microfinance Investment Environment Profile

Amit Jha
Neeraj Negi
Rekha Warriar

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Methodology

The central objective of this report is to contribute to the information available to investors interested in the microfinance sector by creating a framework for assessing the country-specific investment risk in microfinance and secondly, by identifying incentives and disincentives for MFIs to disclosing information important to investors.

A team comprising three students spent 12 weeks in Princeton reviewing existing literature on the microfinance sector and one week in Ghana. The fieldwork component consisted of interviewing key institutions in the microfinance sector: MFIs, microfinance associations, relevant government agencies, Savings and Loan Companies, Rural Banks, NGOs, Networks and Associations of MFIs. The teams also made site visits to MFI branch offices to observe client meetings and loan collection procedures.

Abbreviations and Acronyms

ADB	Agriculture Development Bank
ARB	Association of Rural Banks
BOG	Bank of Ghana
CIA	Central Intelligence Agency
CU	Credit Union
CUA	Ghana Co-operative Credit Union Association
CGAP	Consultative Group to Assist the Poorest
DP	Development Partners
FFH	Freedom From Hunger
GCSCA	Ghana Cooperative Susu Collectors Association
GDP	Gross Domestic Product
GHAMFIN	Ghana Microfinance Institutions Network
GNI	Gross National Income
GSE	Ghana Stock Exchange
GTZ	German Agency for Technical Cooperation
HDR	Human Development Report
HIPC	Heavily Indebted Poor Countries
IDA	International Development Association
IFAD	International Fund for Agriculture Development
IMF	International Monetary Fund
MF	Microfinance
MFI	Micro Finance Institutions
NAMFIC	National Microfinance Center
NBFI	Non Banking Financial Institution
NDC	National Democratic Congress
NGOs	Non Governmental Organizations
NPP	National Patriotic Party
PPP	Purchasing Power Parity
RB	Rural Banks
RCB	Rural and Community Banks
RFSP	Rural Financial Services Project
ROSCAS	Rotating Savings and Credit Associations
S&L	Savings & Loans Company
SAT	Sanapi Aba Trust
SEC	Securities and Exchange Commission
SSNIT	Social Security and National Insurance Trust
US	United States
VAT	Value Added Tax
WB	World Bank
WOCCU	World Council of Credit Unions

Country Profile

Political Climate

Ghana is a tropical country located in West Africa. It is bounded by Côte d'Ivoire to the west, Burkina Faso to the north, Togo to the east, and the Gulf of Guinea (Atlantic Ocean) to the south. The country is an exception in the region enjoying relative political stability and peace under democratic governments. Ghana has emerged as a regional leader as evidenced by its presiding over ECOWAS (Economic Community of West African States), peace initiatives in Côte d' Ivoire and Liberia and as the location of the proposed common central bank for the West African Monetary Union.

The present government led by John Kufuor of the National Patriotic Party (NPP) was reelected in December 2004, defeating the John Atta Mills led National Democratic Congress (NDC). Mr. Mills, the leader of NDC, who was earlier defeated by President Kufuor in the 2000 elections, had raised allegations of corruption against the present regime. The government led by President Kufuor is generally perceived to be steadier and cleaner than the past governments led by the NDC. Continuation of NPP in power implies continuity and stability in government policy orientation at least in the medium term.

Northern Ghana, in comparison to the rest of the country, is economically backward and prone to ethnic violence. The ethnic conflict between Andani and Abudu clans last surfaced in this area in March 2002. In the aftermath, the Minister for Northern Region and Interior Minister were forced to resign from office. The government also imposed the state of emergency in Yendi and deployed a rapid response team of soldiers to prevent further violence. The state of emergency was finally lifted in August 2004.

Social Climate

Ghana's population is estimated to be 21 million. About two thirds (63.93%) of it resides in the rural areas (see Table 1). Its capital city is Accra, which has a population of about 3 million. Other important cities include Kumasi, Tema and Sekondi-Takoradi. Ghana's population is concentrated along the southern coast; the northern part of the country is sparsely populated.

Ethnically, Ghana is divided into small groups speaking more than 50 indigenous languages and dialects. Christians comprise 63%, Muslims 16% and people practicing indigenous beliefs 21% of the total population. About 75% of Ghanaian population, 83% of males and 67% of females, is literate. Prior to its independence in 1957, Ghana was a British colony. As a result of the colonial legacy, English is the official language of the country.

The income disparity is moderate with a Gini Coefficient of 0.396. However, 39.5% of the population lives below the national poverty line (HDR 2003). In absolute terms, 44.8 % of the population lives below a dollar a day while 78.5% of the population lives below two dollars a day (HDR, 2003). According to Census of Ghana (2000) about 48% of the country's population is of working age of 15 to 64 years; of these 82% have

some gainful employment. The number of potential clients for the formal Microfinance institutions is estimated to be 3 million.

Table 1: Select Social Indicators

	1999	2002	2003
Population[a]			
Population, total (thousands)	18,912	19,908	20,426
Rural population (% total population)	63.93%	63.26%	n/a
Population density, rural (population per sq km)	n/a	n/a	n/a
Poverty and Inequality [b]			
% Population under $2 a day PPP	78.5%	n/a	n/a
Poverty gap at $2 a day (%)	40.8%	n/a	n/a
% Population under $1 a day PPP	44.8%	n/a	n/a
Poverty gap at $1 a day (%)	17.3%	n/a	n/a
GINI index	0.396	n/a	n/a
Employment			
Economically active population [b] (% total population)	74.7%	n/a	n/a
Unemployment [d]	n/a	8.2.	n/a

Source: [a] The MIX Market: http://www.mixmarket.org/
[b] World Development Indicators 2004
[c] LABORSTA Internet: http://laborsta.ilo.org/
[d] Census of Ghana, 2000

Economic Climate

Ghana has a diverse and rich resource base. It has rich deposits of gold, diamonds, manganese ore and bauxite. Gold, timber, and cocoa production are major sources of foreign exchange. Agriculture, which employs 60% of the country's workforce, comprises 35% of the country's GDP. Industry and services employ 15% and 25% of the workforce and comprise 25% and 39% of the GDP, respectively. Although the Census of Ghana (2000) pegs the unemployment rate at about 8.2% other estimates indicate the unemployment rate to be about 20%.

Presently, the GDP of Ghana is about 7.7 billion US dollars (World Bank estimates, 2004). Although the GNI per capital, using Atlas method, is only US $ 320, as per the PPP measure the per capita income is much higher at US $ 2200 (CIA, 2003). Receipts from the gold sector and a bumper cocoa crop should help sustain GDP growth in 2004. The annual rate of growth is expected to be 5.2% in 2004 and 5.0% in 2005 (IMF 2004). In 2004 the budget deficit was about 3.4 % of GDP. Year on Year annual inflation, which had increased to 41.9% in March 2001, has eased to 12.9% in 2004 (BOG).

Table 2: Select Economic Indicators

	1999	2000	2001	2002	2003
Monetary					
Inflation rate (annual average)	12.41	25.19	32.91	14.82	26.67
Lending rate (Dec)	n/a	n/a	n/a	38.5	32.75

Treasury bill rate (30 days, Dec)	31.48	38.00	26.99	26.62	18.66
Output and Income					
GDP (current US$; thousands)	7,709,759	4,977,580	5,309,200	6,159,567	7,700,000 [d]
Real GDP growth [b] (Annual %)	1.92%	2.35%	2.43%	2.75%	1.9%
Budget balance [b] (% of GDP)	n/a	n/a	-4.5	-5.9	- 3.5
GNI per capita, Atlas method (current US$)	330	380	290	270	320
Exchange Rates and Foreign Investment					
Exchange rate (Cedi per US$; end of period)[c]	3,538.06	6,809.50	6,895.77	8351.90	8,852.3
Total foreign debt[b] (% of GDP)	109.9%	169.8%	131.5%	107.2%	91.4%
Foreign direct investment, net inflows (% of GDP)	3.33%	3.16%	1.68%	0.81%	n/a

Source: The MIX Market: http://www.mixmarket.org/; [a] The World Bank Group; [b] International Country Risk Guide (ICRG); [c] Bank of Ghana; [d] Estimated by World Bank.

Despite being well endowed with natural resources, Ghana's economy remains heavily dependent on international financial and technical assistance. Ghana opted for debt relief under the Heavily Indebted Poor Country (HIPC) program in 2002. Ghana qualified under the fiscal criterion and the debt relief was calculated to bring the NPV of debt-to-government revenue ratio down to the HIPC threshold of 250 percent. Total debt relief under the enhanced HIPC Initiative from all of Ghana's creditors amounts to US$3.5 billion in nominal terms and US$2.2 billion in the NPV terms. Following debt relief under the HIPC initiative, Ghana's general government debt-to-GDP ratio is expected to fall to about 90% by the end of 2004. At the same time, gross public sector external debt is expected to fall to 147% of current account receipts (Source: Standard and Poor).

The present government has been committed to stricter monetary and fiscal policy, accelerated privatization, improvement of social services and poverty alleviation. This policy orientation is likely to continue in future. Standard & Poor's Ratings Services[1] has accorded a 'B+' long-term and 'B' short-term foreign and local currency sovereign ratings to Ghana (Nov, 2004). Fitch has also given Ghana a 'B' rating for long and short term exposures and has assessed the economy outlook to be positive.

Despite the weak financial situation of the government and low level of economic development, the outlook for Ghana is stable because of political environment, improving external liquidity and manageable levels of net public external debt and debt service payments.

[1] http://www2.standardandpoors.com/servlet/Satellite?pagename=sp/Page/HomePg

Overview of Microfinance Sector

Policy Support to Microfinance

Since more than three-fourth of the population of Ghana lives under two dollars a day, micro finance is probably the most appropriate way to provide financial services to a majority of Ghana's population. It's, therefore, not surprising that present government perceives microfinance to be central to achieving the greater goal of poverty alleviation. Through microfinance the government aims to provide poor entrepreneurs, especially those in the informal sector, with greater access to customized financial services. First systematic effort to restructure the rural banking sector was with initiation of the International Development Association (IDA) financed Rural Finance Project which continued from 1989 to 1995. This project, which was implemented by the Bank of Ghana, initiated institutional reforms in the rural banking sector and provided a line of credit to the eligible rural banks.

In 2000, the poverty focus of the new regime led to initiation of the subsidized credit programs for poor. Such programs created distortions in the microfinance market and had the effect of stifling the growth of this sector. Due to opposition from the MFIs, GHAMFIN, and donor agencies such as World Bank and GTZ, the government now consciously avoids distorting the market.

Presently, the Rural Financial Services Project (RFSP), which has an estimated outlay of US $ 22.96 million and spans from 2001 to 2006, is being implemented by the BOG[2]. The project aims at providing a coherent framework for rural economic transformation and growth. It aims to broaden and deepen financial intermediation in the rural areas through effective linkages between the formal rural and micro-financial institutions and informal entities operating in the rural areas. The project has following objectives:

- Capacity Building of the Informal Financial Sector. This component aims to strengthen operational linkages between informal and semi-formal micro-finance institutions and the formal network of rural and community banks to enable them to expand services to a large number of rural clients.
- Capacity Building of Rural and Community Banks through restructuring weak rural banks and strengthening their operational effectiveness; strengthening their internal control systems including provision of new information technologies, logistics and training of key staff; and, developing an overall development plan for all categories of staff including Board of Directors.
- Establishment of the ARB Apex Bank for the rural banking system to harness economies of scale needed by the rural banks to become competitive.
- Strengthening the institutional and policy framework for improved oversight of the rural finance sector. To achieve this, key logistics (including training) will be provided by the program to BOG to better equip it for effective supervision of the Apex Bank and the rural banks. The Ministry of Finance is also being supported to ensure continuity in the on-going rural microfinance initiatives.

[2] http://www.BOG.gov.gh/rpapers/rfdoc.htm

As part of the ongoing financial sector reforms, Ghana is developing a National Strategic Framework to remove impediments to improving delivery of financial services to the micro and small enterprises. The framework aims at fostering a fully integrated financial sector supported by a reliable regulatory system and that offers a broad range of financial products and services to the micro and small enterprises, especially those in the informal sectors, on a sustainable basis. The objective is to establish a decentralized and sustainable micro-finance system, prudentially regulated with close linkages with the formal financial sector, and an effective outreach to the poor.

The government has recently constituted the National Microfinance Centre (NAMFIC), to facilitate administration of government and donor credit funds, and to coordinate the efforts of microfinance practitioners and stakeholders. Through this, on one hand, state wants to avoid market distortions due to subsidy and, on the other, wants to increase the availability of funds to this sector. Government is strengthening GHAMFIN to provide financial and managerial capacity building services to MFI networks and service providers. Although NAMFIC is yet to become operational, such measures indicate that government's commitment to the development of this sector will continue.

Institutions Providing Micro Finance Services

Ghana's financial system can be broadly divided into three categories- formal, semi-formal and informal. The formal institutions are incorporated under the Companies Code 1963 and licensed by the Bank of Ghana (BOG) under the Banking Law, 1989, or the Financial Institutions (Non- Banking) Law, 1993. Commercial banks and rural banks are incorporated under Banking Law, while the Savings and Loans companies and Credit Unions are incorporated under the Non Banking Financial Institution (NBFI) law. The Credit Unions, however, are not regulated by the BOG, but by the Credit Union Association (CUA) which acts as a self regulatory apex body.

Table 3: Key Financial Service Providers

Organization Type	Number	Total clients served	No. of depositors	Total deposit base mill. $	Ave deposit per client	No. of borrowers	Total loan portfolio million $	Ave balance per client
Commercial Banks	17	n/a	n/a	1,300	n/a	n/a	900	n/a
Rural Banks	117	1,200,000	1,200,000	126	105 [a]	150000	47	313 [a]
Savings and Loan[s]	10	240,000	200000	n/a	n/a	40000	10	250
Credit Unions	253	144,898	144,898	31	214	n/a	21	n/a
NGOs	50	56,000	___	___	___	56000	4	70
Susu Collectors & Clubs	4032	1,200,000	1,200,000	11	9	n/a	n/a	n/a

Source: Bank of Ghana; Ghamfin; GCSCA; annual reports of the S&L Companies. [a] Calculated from Andah & Steel, 2004; [b] Including the present loan portfolio of Sinapi Aba Trust.

Although all formal institutions have some involvement in microfinance, only the rural banks and S&Ls can claim substantial involvement. The Semi formal sector comprises Credit Unions and NGOs. The Credit Unions cater to the financial needs of its members, who are generally from the salaried class. NGOs, on the other hand, focus primarily on the disadvantaged sections. The informal sector comprises *Susu* collectors, traders, money lenders, ROSCAS, etc. They, along with the NGOs, are providing microfinance services to the poorer sections.

Formal Sector

Commercial Banks

The commercial banking sector comprises 9 commercial banks, 5 merchant banks and 3 development banks. With a domestic deposit base of about US $ 1.3 billion they are the most important players in the financial market (BOG, 2004). Only 38% of the total assets of the Commercial Banks are in form of loans; banks prefer investing in liquid and low risk government securities that now constitute about 25% of their total assets (BOG, 2004). In addition, state owned enterprises also attract a substantial part of the lending from the commercial banking sector. This has the effect of crowding out the financial resources available to private sector. Although, the banking penetration ratio of one bank branch per 54,000 people is relatively high, the commercial banks reach only 5% of the total households due to their strong urban bias. For example 35% of the commercial bank branches are in Greater Accra even though it represents less than 13% of Ghana's population (Buchs and Mathisen, 2003)[3]. Even within the urban areas most potential microfinance clients are not able to access their services due to high deposit requirements.

Among the commercial banking institutions, Agriculture Development Bank (ADB), which is one of the three development banks in Ghana, is playing an important role in providing financial services to the agriculture sector. The Agricultural Development Bank - ADB - was set up by an Act of Parliament (Act 286) in 1965 to promote and modernize the agricultural sector through appropriate but profitable financial intermediation[4]. Due to its financial problems, which resulted in a negative net worth, ADB was restructured in 1992. Presently, The Government of Ghana owns 51.83% shares while the BOG owns 48.17% shares of ADB. After restructuring, although financial profitability of ADB has improved, it has remained subsidy-dependent. Its development banking services available for small scale operators include credit for production, processing and marketing of agriculture products; cocoa financing; maintenance of agriculture farms and adoption of improved technologies; and, agro-allied services related to input and equipment supply, and transportation. An individual can open a savings account with the ADB with a minimum deposit that could be as low as US $ 11. Presently the loan portfolio of ADB is about US $ 100 million of which about half is dedicated to the agriculture sector and a quarter is with small holders. A substantial portion (30%) of the ADB's assets is in form of government securities.

[3] http://www.isser.org/Banking%20in%20Ghana.pdf
[4] http://www.agricbank.com/about_adb.asp

Rural and Community Banks

The Rural and Community Banks (RCBs) are owned by members of the rural community through equity and are licensed to provide financial intermediation in the rural areas. The rural banks started their operations in 1976 with an aim to mobilize savings and provide credit facilities in rural areas that were not being serviced by the commercial banks. These banks expanded rapidly in 1980s. A major reason for expansion was government's introduction of special checks instead of cash payment to cocoa farmers. Poor financial management, weak supervision and natural calamities led to deterioration of the financial viability of rural banks; for example, in 1992 the Banking Supervision department of BOG considered only 23 (19%) of the 123 RCBs to be functioning satisfactorily (Steel & Andah, 2003). In 1999, 23 distressed RCBs were closed down and the depositors compensated by the Bank of Ghana. This sent a strong signal to the RCBs to improve their financial position or face closure. As a result the number of RCBs performing satisfactorily increased from 46% in 1999 to 76% in 2001 (Steel & Andah, 2003).

Presently, 117 RCBs are functioning in Ghana. The total combined assets of RCBs are about US $ 165 million of which about 23 million (14.2%) is shareholders capital. On average RCB has about 8500 clients (Kowubaa, 2000). The total deposit base of the RCBs is US $ 126 million, the loan portfolio about US $ 47 million, and the investments in Treasury Bills and Govt. Bonds about US $ 72 million (BOG, 2004). The average loan cycle for micro entrepreneurs is 4-6 months and rate of interest is 40% simple. Some of them have adopted community assessment of loans.

In 1994, BOG had disallowed RCB participation in Clearing. RCBs' dependence on commercial banks for clearing, treasury functions and currency supply put them at serious disadvantage and resulted in loss of credibility and customers. This has been mitigated by the setting up of the ARB Apex Rural Bank (under the Rural Financial Services Project being implemented since 2002) which now handles clearing, specie management and capacity building for the RCBs.

Savings and Loan Companies

Presently, 10 Savings and Loan companies are operational in Ghana. According to our estimates, based on figures for 5 S&Ls, the S&Ls together have more than 200,000 depositors and over 40,000 borrowers. The loan portfolio of the S&Ls is about US $ 10 million.

The advent of S&Ls in the financial sector is fairly recent; the first S&L license was issued Women's World Banking Ghana (WWBG) in 1994, which was earlier an NGO working on microfinance. Sinapi Aba Trust[5], which obtained a License to operate as an S&L in 2004, has presently has about 20000 borrowers and an outstanding loan portfolio of US $ 2.9 million. First Allied S&L, which like Sinapi Aba Trust is based in

[5] Although Sinapi Aba Trust has got a license to operate a S&L, which has now started operating, the trust has still not transferred all of its microfinance portfolio to the S&L. Thus, at present both the structures coexist. Although, we have included Sinapi Aba Trust in this section, it could have very well been included in the section on NGOs.

Kumasi, presently has 80,000 depositors with total deposits of US $ 6.2 million and 7411 borrowers with US $ 2.4 million loan portfolio. Sikaman S&L[6] with 1,800 borrowers and US $ 1.6 million loan portfolio and Citi S&L with more than 5000 borrowers and a loan portfolio of US $ 1.7 million are other major players. WWBG has a relatively small loan portfolio of US $ 0.2 million. However, with a borrower base of 2442 and outstanding loan per client of US $ 82, it has been able to focus more on poorer sections.

There is considerable diversity in the methods used by the S&Ls to address the needs of their respective market niche. Sinapi Aba Trust and First Allied S&L use group based lending methodology. Sinapi Aba starts by constituting a 'Trust Bank,' which has 15 to 40 members. If the repayment record of the group members is good, they graduate to form solidarity groups that have a smaller size – 5 to 15 members – but have a higher credit limit. Along side Sinapi Aba targets credit worthy individuals through its schemes for individuals based on guarantees. First Allied S&L, in addition to adopting the group lending methodology, has also tied up with the local consumer goods outlets and Travel Agencies to give to give consumer loans. Citi S&L, on the other hand, uses *Susu* Clubs or any other economic association for their group loan product, with joint group guarantee. It has also targeted *Susu* collectors as its main depositors. Sikaman S&L, which started its operations in 2002, has been able to break even within two years of its operation by adopting the global best practices in microfinance.

Semi Formal Sector

NGOs and Credit Unions are legally registered under the Companies Code and the Department of Co-operatives, but BOG does not regulate or supervise them. The NGOs are active in capacity building of the communities and a variety of microfinance activities including financing. The Credit Unions are technically under the BOG but the actual regulation is done by the self regulatory association- Ghana Co-operative Credit Union Association.

Credit Unions

Credit Unions are thrift societies offering savings and loan facilities exclusively to members (Steel & Andah, 2004). Although the first credit union was constituted in Jirapa, northwestern Ghana, in 1955, CUs were brought under legislation in 1968 (Kwadwo, 2001). By 2004, there were 254 CUs with 144,898 members a deposit base of US $ 31 million, an average deposit size of US $ 214 per member, and a total loan portfolio of US $ 21 million. About 70% of the CUs are essentially salary earners co-operatives. In early 2004, the savings interest rate was 16% while loans attracted an average interest rate of 19.5%.

Generally, members of the CUs make predetermined periodic deposits into their accounts and may borrow more than their savings balance. Most CUs require borrowers to provide security, in addition to being in good standing with their deposits. The quality of the services that the members receive from the CU is generally poor. They face increasing competition from the commercial banks, which are able to provide better

[6] Sikaman changed its name to Procredit in Nov 2004.

automated services and higher returns on savings. To be competitive Credit Unions need to be more cost efficient and need to enhance the range of services they provide.

NGOs

According to GHAMFIN about 50 NGOs are presently providing microfinance services to poor. Almost all of these, along side providing microfinance services, also work as multi-purpose and welfare oriented institutions. They play an important role in providing financial services to the poor people especially those in the northern part of the country where presence of Commercial Banks, Rural Banks, and S&Ls is very thin. The client base of most of the NGOs is very small – in 2003 only four NGOs exceeded a client base of 3000 and their total client base was about 56000.

GHAMFIN conducted a survey of 43 NGOs in 2002. The survey shows that on an average[7] the NGOs providing Microfinance services have been operational for 5 years, and have 12 personnel including 4 loan officers. On average[8] they have 1109 active borrowers of which 83% are women, and an outstanding balance per creditor of US $ 70. Thus, the outstanding loan balance per creditor is lower than for other MFIs such as S&Ls and rural banks, underscoring their ability to cater to the needs of the poorest clients.

Most NGOs that operate as MFIs, along side microfinance services also provide a range of services such as education on nutrition, family planning and AIDS, and capacity building of the poor beneficiaries in financial accounting and planning. Freedom from Hunger, Ghana, has been collaborating with some RCBs and has successfully introduced the 'credit with education[9]' model of lending which is showing good loan recovery. However, most NGOs are presently dependent on grants for their sustenance. Based on their current performance almost all the NGOs were financially and operationally unsustainable institutions. Some financial NGOs are receiving deposits and on lending through banks which results in low accountability.

In general, group based micro- lending, mainly to women groups, have shown high rates of recovery generally ranging between 98 to 100%. Most of the loans are invested by the beneficiaries in economic activities such as fishing, trading, processing palm oil, and processing of cassava into *'gari'*. Grain Banking is another innovative and popular experiment in Ghana. This involves providing grain storage facilities to farmers to enable them to hold onto the produce to receive better prices. The grain bank loans them seeds, fertilizers etc. besides providing market information on prices and market conditions. This initiative is being supported by GTZ.

[7] Based on 27 responses
[8] Based on 27 responses
[9] The general objective of this project is to enable poor women in rural areas of Ghana to increase their incomes and savings and to motive them to undertake nutritionally beneficial behavioral changes to improve their household food security, nutrition, and health status.

Informal Sector

A significant part of the micro-finance activities are presently being performed by the informal sector, which comprises *Susu* Collectors, money lenders, traders, ROSCAS, friends and relatives.

Susu Collectors

A *Susu* collector is a person who collects savings, generally on a daily basis, from his clients. At the end of the month he returns the total accumulated savings of his client after deducting a day's collection as his compensation. These collectors visit shops, work places, market stalls and homes each day to collect funds towards a savings plan. The collection from a client could be as low as 20 cents per day – average 60 cents per day – implying that the group that *Susu* collectors cater to are those that may not be eligible to open formal savings accounts with commercial banks despite the high amount of savings accumulation over time.

Although duration of collection and periodicity may differ, the principle on which this system works remains the same. *Susu* collectors retain some part of the saving as compensation for services rendered and pay no interest to the clients. *Susu* collectors may give occasional loans to their clients before the end of the deposit period, or could make loans to them for a period longer than the deposit period based on their assessment of the credit worthiness of their clients and the extent to which they have capital or deposits available for lending. The *Susu* collectors are generally from the same community as their clients and often their family has been in this vocation for generations. As a result, they enjoy the trust of their clients.

A survey conducted by the Ghana Cooperative *Susu* Collectors Association (GCSCA) found that in year 2002 there were 4032 *Susu* collectors, of which 882 were active members of the Association. On average a *Susu* collector serves more than 300 clients; thus, they may be serving a total of about 1.2 million clients.

In order to enhance their efficiency, *Susu* collectors often institute *Susu* clubs wherein vendors and micro-enterprise operators meet at a designated place and on specified time to deposit savings. This arrangement allows *Susu* collectors to collect savings from a much larger number of clients without spending much time.

The GCSCA was established in 1994 to act as an umbrella organization to regional *Susu* collectors' societies. The objective behind its formation was to self regulate the activities of the *Susu* collectors and to instill best practices in them, to facilitate greater consumer confidence and deposit mobilization. Even though *Susu* collectors mobilize savings, the central bank has refrained from regulating them.

The institution of GCSCA is expected to facilitate formalization of the *Susu* system in future. It is also likely to integrate the *Susu* collectors with the mainstream banking institutions. This in turn will reduce the risk involved for the depositors.

Some rural banks such as First Allied have tried adopting the *Susu* collector model for mobilizing savings and giving loans. There efforts have not met with much

success as the bank employees were not able to gain the level of confidence and intimacy that the *Susu* collector enjoy with the rural poor.

Moneylenders

Moneylenders provide credit to their clients generally in lieu of collateral preferably in the form of physical assets such as buildings, farmland and undeveloped land. Loans to employees may be secured against their salary; verbal guarantees from family heads, friends and relatives may also be accepted as security. Moneylenders were the first form of microfinance to be officially licensed in Ghana – the government issued Moneylenders' Ordinances in 1940 and in 1957. Although in past money lenders had a significant presence in microfinance, this has substantially declined over the past couple of decades. According to one account while there were 33 licensed moneylenders in Accra in 1972, by 1988 this number had declined to 4. These days most money lenders operate informally and are involved in the vocation as a part time activity.

Traders

Traders play a significant role in providing rural finance. These traders, who generally work as intermediaries between producers such as farmers and fishermen, and urban markets, provide credit in form of inputs or an advance against a future agreement on purchase of the crop. The implicit interest rate is often as high as 50%.

Regulatory Framework

Bank of Ghana

BOG, the central bank of Ghana, regulates the banking and non-banking financial sub-sectors. The legal framework governing the central bank were revised vide the Bank of Ghana Act, 2002, giving enhanced autonomy to BOG in framing monetary policy, regulation and supervision of banking and non banking financial institutions.[10] The Banking Law, 1989 which governs all banking companies in Ghana is under revision and a new Act is expected to be enacted shortly. The Financial Institutions (Non Banking) Law, 1993 and the rules framed under the Act are applicable to Savings and Loan Companies. Currently there is no formal deposit insurance in Ghana, though the Government and BoG have generally compensated small depositors of rural banks when they failed or were shut down. Ghana has so far not established a separate framework to cater to the regulatory requirements of the Micro-finance sector.

BOG has prescribed minimum start up capital requirements for various types of regulated financial institutions[11]. The current requirements for institutions that can offer microfinance services are:

[10] http://www.BOG.gov.gh

[11] W.E.F, Feb 3, 2003

- Local commercial Banks must have a minimum capital of 70 billion Cedis[12] of which 60% should be from resident Ghanaians.
- Foreign Banks must have a capital of 70 billion Cedis with a minimum of 60% being subscribed in convertible currency.
- A Development Bank is required to have a capital of 70 billion Cedis.
- Rural Banks are required to have a capital of 500 million Cedis of which corporate bodies should own at least 50% and individuals 20%.
- Savings and Loan companies should have a capital base of 15 billion Cedis, and if it is a foreign S&L then 60% of the capital should be in form of a convertible currency.

The liquidity requirements for banks and other deposit taking commercial institutions are laid down by BOG. They need to maintain a primary reserve in form of cash and deposits with BOG and a secondary reserve in form of investments in government securities and Treasury Bills. Up to 2002 the liquidity requirements for the rural banks was as high as 62%, to enable them to benefit from the high yields on sovereign securities and improve their financials. This has subsequently been brought down to the current level of 8% in form of primary reserves plus 5% deposit with ARB Apex and a 30% secondary reserve. Thus, rural banks currently need to have 43% of their assets in form of liquid assets.

Banks and NBFIs are subjected to capital adequacy requirements. The current requirements stipulate that a bank's capital should be at least 6% of its risky assets. For a deposit taking NBFI it should be at least 10% of its risky assets. The primary or Tier one capital (equity and free reserves) should constitute at least 50% of the total capital adequacy requirement. Subordinated debt component in the secondary capital should not exceed 50% of the total secondary or tier two capital. The capital adequacy requirements in the country are well below the Ist Basle Accord prescriptions.

BOG has laid down exposure norms for banks as per best practices in banking. The current stipulations on group and individual exposure etc. are listed below:

- To any one group or individual not more than 25% of the net worth of the institution;
- Unsecured Credit should not be more than 10% of net worth of the institution;
- Loans to Director and employee credits have a ceiling;
- Investment in immovable property other than for own business is not permitted

Banking and FI regulations lay down provisioning requirements and rules for minimum disclosure. Audit guidelines and forma for Long Form Audit Report to be submitted by the auditors have been prescribed. Banks are required to submit their Balance sheet and Profit and Loss Accounts to BOG within three months from the date of closing (31st December). Accounts are also required to be published in a leading daily newspaper. BOG supervises the institutions under its jurisdiction through offsite returns and onsite inspections. The frequency of inspections is annual.

[12] ($1 = Cedis 9000 (approx))

Other Regulators

ARB Apex Rural Bank

Currently the Apex Bank looks after the clearing and settlement needs, specie and treasury management needs of the rural banks. It is also responsible for training rural bank officials, improving the MIS system of rural banks and for developing a standard reporting system. The Apex Bank may eventually emerge as a sub regulator/ supervisor of the rural banking system under the purview of the BOG.

Credit Union Association

The Credit Union Association (CUA) serves as a self-regulatory apex body for the credit unions. The Department of Cooperatives has laid down eligibility norms for full registration of a new credit union. CUA applies prudential norms that are similar to the operating and financial standards of the World Council of Credit Unions (WOCCU). BOG has desisted from extending its regulatory jurisdiction authorized by the 1993 NBFI Law to the Credit Unions. A new Credit Union law is proposed, which is expected to streamline the delegation of specific supervisory functions to CUA. CUA will then report to a Supervisory Board with BOG rather than to the Department of Cooperatives as at present. CUA enforces its regulations by downgrading status of CUs who default in meeting its requirements.

Ghana Cooperative Susu Collectors Association

The Ghana Co-operative *Susu* Collectors Association (GCSCA) imposes a number of regulatory barriers to entry as well as providing services to its members. A prospective member must be recommended by a zonal executive, provide two sworn guarantors, deposit 1 million Cedis into a security fund, save 5,000 Cedis a month, take a medical examination, and undergo a three month training with an existing member. Other measures intended to improve the confidence of the public in doing business with members of GCSCA include wearing uniform colors, paying off clients' deposits from the security fund in case of the death or disappearance of a collector, and assisting in arbitration of disputes. GCSCA monitors performance of the industry by collecting quarterly data from its zonal societies on the number of clients, amounts mobilized, problems encountered, and assistance given.

GHAMFIN

Ghana Microfinance Institutions Network evolved from a research program sponsored by the World Bank designed to strengthen micro-finance institutions and to contribute to a mechanism for supporting sustainable grass root institutions that provide financial services to the poor. Ghamfin's main objective is to support and facilitate processes that help in addressing the constraints faced by its members. These constraints have been identified by various studies of the Ghanaian microfinance sector, and include lack of access to on-lending funds, poor MFI staff skills, inappropriate financial technologies and inadequate operational strategies, poor MIS, absence of performance standards, codes of conduct, conflict resolution mechanisms and so on. These constraints

affect Ghana, since the microfinance sector in this country is still young. Hence, the capacity-building of Ghanaian MFIs presents a major task, high on Ghamfin's agenda. Ghamfin's specific objectives are accordingly:

- To establish performance indicators for the self-regulation of MFIs in Ghana ;
- To develop an information bureau on the microfinance industry in Ghana;
- To organize seminars and workshops to share best practices among members;
- To provide access to continuous training for MFIs;
- To enhance financial integration between the formal, semiformal and informal sectors; and,
- To collaborate with the Government, donors and other regional networks to overcome common problems facing MFIs and to seek funds for research and development.

GHAMFIN is establishing performance indicators and putting in place reporting structures for the members in line with CGAP[13] and MIX standards. GHAMFIN organizes seminars, workshops and conferences aimed at sharing experiences and evolving best practices in the industry. It works very closely with the Government, donors, regional networks, and service providers. GHAMFIN is likely to emerge as a self regulatory organization with reporting and disclosure requirements for its members ranging from *Susu* collectors to the rural banks. In the brief span, GHAMFIN has emerged a key facilitator in the Ghanaian microfinance sector.

Investment Climate

Ghana welcomes foreign investments. All sectors are open to foreign investment with special focus on cotton and textiles, agri-processing, floriculture etc. The Ghana Investment Promotion Center Act (1994) and formalities to be completed for investments, where applicable, are available with Ghana Investment Promotion Centre[14]. Investments into regulated financial sector are subject to the requirements of the Bank of Ghana[15]. Exchange Control regulations for repatriation of capital are available on the website of Bank of Ghana.

The Ghana Stock Exchange (GSE) was established in 1989 and began trading in corporate equities, bonds and government securities in 1990. The Securities Regulatory Commission was established in 1998 to oversee and regulate the bourse. It was later named as the Securities and Exchange Commission (SEC). The GSE had 24 listed companies and a market capitalization of US$ 740m at end-2002. Liquidity has remained extremely low; the volumes traded averaging only around 2% of total market capitalization. Most retail investors are passive and public awareness of the GSE is relatively low. Some of the rural banks expressed intentions of getting themselves listed on the Stock Exchange eventually to tap capital markets. The requirement of a continuous run of profits for 3 years before listing is one of the factors preventing them from being

[13] The Consultative Group to Assist the Poor

[14] http://www.gipc.org.gh/IPA_Information.asp?hdnGroupID=3&hdnLevelID=3

[15] http://www.BOG.gov.gh/notices/others/loans.htm

listed. With improved performance and finances, some of them could be tapping the markets in the near future.

Ghana reportedly receives more than $ 2 billion annually in personal remittances. It is estimated that about 60% of the domestic savings are outside the formal banking system as people divert their savings into the informal systems. Bringing these funds into the formal banking pool will enable better distribution of credit. The minimum capital requirements for formal MFIs prescribed by the BOG are considered too high by market participants, considering the current volume of business transacted by these entities. Thus, high capital requirements are a barrier to entry in the formal banking sector.

Reporting and Information Sharing

BOG has the legal authority to regulate, supervise and direct the banking and credit system and to and to license, regulate, promote and supervise non-banking financial institutions. Various regulatory returns including monthly statement of assets and liabilities and loan portfolio quality monitoring have been prescribed and are being monitored by the BOG. The BOG rules for non banking financial institutions (NBFI-BOG Rules, 2000) require these institutions too review micro and small (business) loans on a monthly basis and stipulates provisioning norms for delinquency (Section E, Rule 21). In addition, the NBFIs are also required to submit audited financial reports on a calendar year basis within 4 months of the end of the year (Section F, Rule 29). Although, these reports are being submitted by the NBFIs in the required formats, for many NBFIs gathering this information is an additional burden. Often these reports are not very accurate and are submitted late. Moreover, since these reports focus on compliance with the prudential regulations, they are not useful for taking managerial decisions. Thus, it is apparent that most NBFIs have a poor MIS system due to which they often do not have information useful for management decisions. Nonetheless, some S&Ls' such as Sinapi Aba and Sikaman have highly sophisticated MIS system through which they have been able to monitor and assess their performance regularly. Other regulatory organizations have developed their own reporting requirements. The current level of information availability is inadequate.

Since a major source of funding for the NGOs working in microfinance is from donor agencies, most of them collect and maintain only that information which is required by their respective donors. Use of this information for management control is rare.

In recent years, GHAMFIN has been instrumental in facilitating improvement in MIS systems of the MFIs. Established in 1996 by a group of MFIs, GHAMFIN has been working towards building capacities in the MFIs and is trying to help them strengthen their MIS and help them monitor and benchmark their performance. It is collaborating with CGAP and MIX-exchange to facilitate MFIs in monitoring and reporting their performance. This has started yielding results; many MFI feel that this has helped them improve their performance. Though the current state of information availability is unsatisfactory, the situation is poised to improve considerably with various initiatives outlined above and GHAMFIN's pivotal role.

Investment Opportunities

According to official assessments of the government of Ghana, over 50% of microfinance demands of the existing MFI clients are not met due to limited access to on lending funds. Further, of the total demand for microfinance loans less than 10% demand is presently being met by the formal and semi formal MFIs; presently the MF services in Ghana reach about 300,000 people against a potential of three million active and bankable poor[16]. Others either have no access to microfinance services or depend upon the informal sector to meet their needs. Thus, formal and semi formal sector is not able to provide most potential clients access to microfinance services.

Generally speaking, Microfinance Institutions (MFIs) in Ghana have a limited reach, operate in a restricted geographical zone, are financially weak, have poor MIS, and most are yet to attain operational sustainability, although several have the potential to be self-sufficient. The attractive features of the Ghanaian microfinance sectors include relative political stability, public security, presence of a cadre of educated professionals and stable policy environment. However, since the absolute number of population living below two dollars a day is only about 16 million the over all size of the market is small. Further, many areas of the country, especially the northern belt are sparsely populated making it difficult to service the needs of the un-banked population of that area.

Although many MFIs, especially the rural banks and Saving & Loan Companies (S&Ls), are presently in need of mobilizing funds to grow and are attracted to the lower interest rates on loans from the international market, they are reluctant to expose themselves to the currency risks. The Cedi, the Ghanaian currency, has in past been very unstable. This increases the currency risk for the microfinance institutions if the transaction is to be conducted in hard currencies such as US dollar or Euro and alternatively for foreign investors if transaction is in Cedis. Thus, small size of the market and the currency risks may be two major deterrents for the international investors. An intermediate structure in the organization of the MF sector to hedge against currency risk and refinance individual MFIs might go a long way in directing investment to the performing MFIs.

[16] Estimate by NAMFIC in conversation with the team

Risk Factors

Political Risk

The country is enjoying political stability under a democratically elected government and seems poised to remain stable overall. After reelection, the current president has a mandate for four more years. This bodes well as the present government is widely perceived as having performed well on the economic front and has accorded lot of attention to the microfinance sector. Thus, we may expect a favorable and stable political climate in future for the microfinance sector. Potential political strife and localized ethnic conflicts, however, cannot be ruled out.

Economic Risk

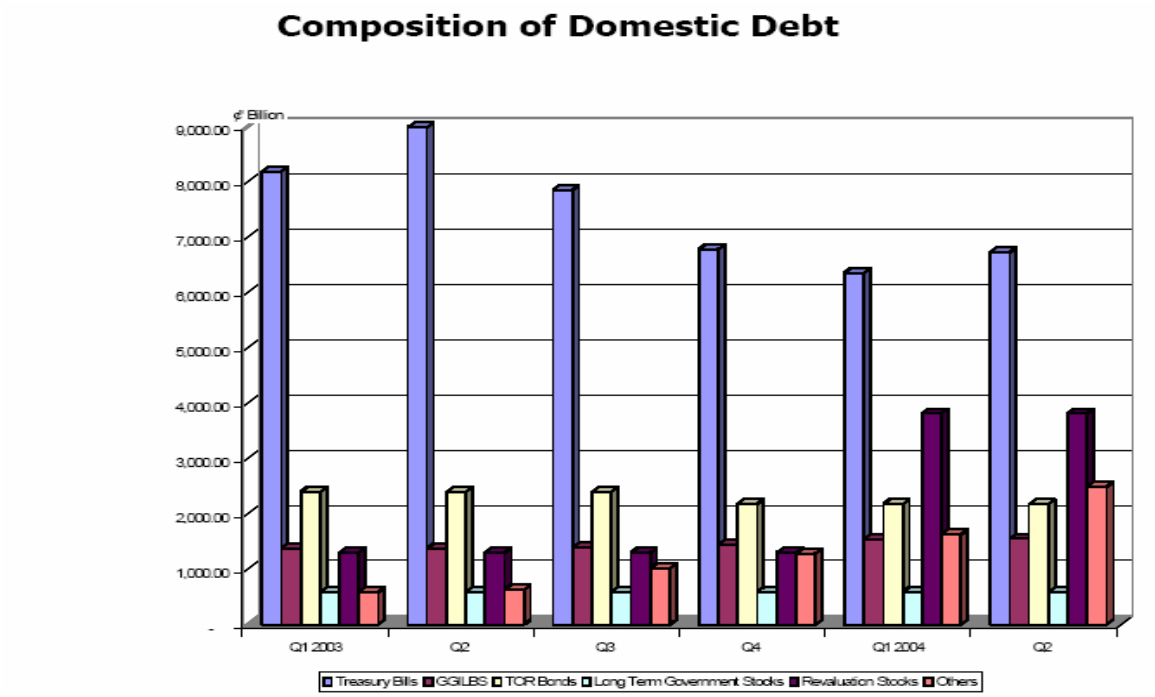
The economy is heavily dependent on cocoa, gold, manganese etc and a few such key commodities. The level of manufacturing activity is low. The fortunes of the economy are therefore strongly linked to the world prices of gold and cocoa especially. The price for gold has been rising in the face of a weakening dollar. Cocoa production touched record levels in 2004 and combined with war in Cote d'Ivoire, a competing producer, Ghana has been able to perform favorably in the export of these two products.

Inflation is hovering around 13% but is considerably lower than the 40% levels of 2001. Inflation is strongly correlated to oil prices and therefore, the risk of inflation reemerging is high. There is increased uncertainty on this front as the government is committed to end the subsidies in the oil sector and move to market pricing by Feb 2005, the impact of which is not predictable at this stage.

Financial Risk[17]

Government securities are perceived to be the best avenue for investment in Ghana's financial markets. The return on the sovereign paper has been higher than the stock market or returns or any other form of investment. As a result, banks and other institutions found it simpler and more profitable to keep their resources deployed in government paper. This is evident from the repeated findings of excess holding of government securities by all categories of financial institutions (well above prescribed levels of statutory reserves). The rates on government paper are being slowly brought down, but most banks still hold considerable portion of their assets in this portfolio. This is true for microfinance institutions also, as many of them prefer to retain much above the statutory requirements in government paper severely curtailing lending to the sector they are expected to serve. The period of maturity of the bills is normally less than a year. There is no long term instrument for investment in the market. It is therefore not surprising that the Treasury Bills dominate the domestic debt market in Ghana (Graph 1).

[17] Parts of this section draw heavily from the Economist Intelligence Unit Country Report 2004



Graph 1 (Source: Bank of Ghana)

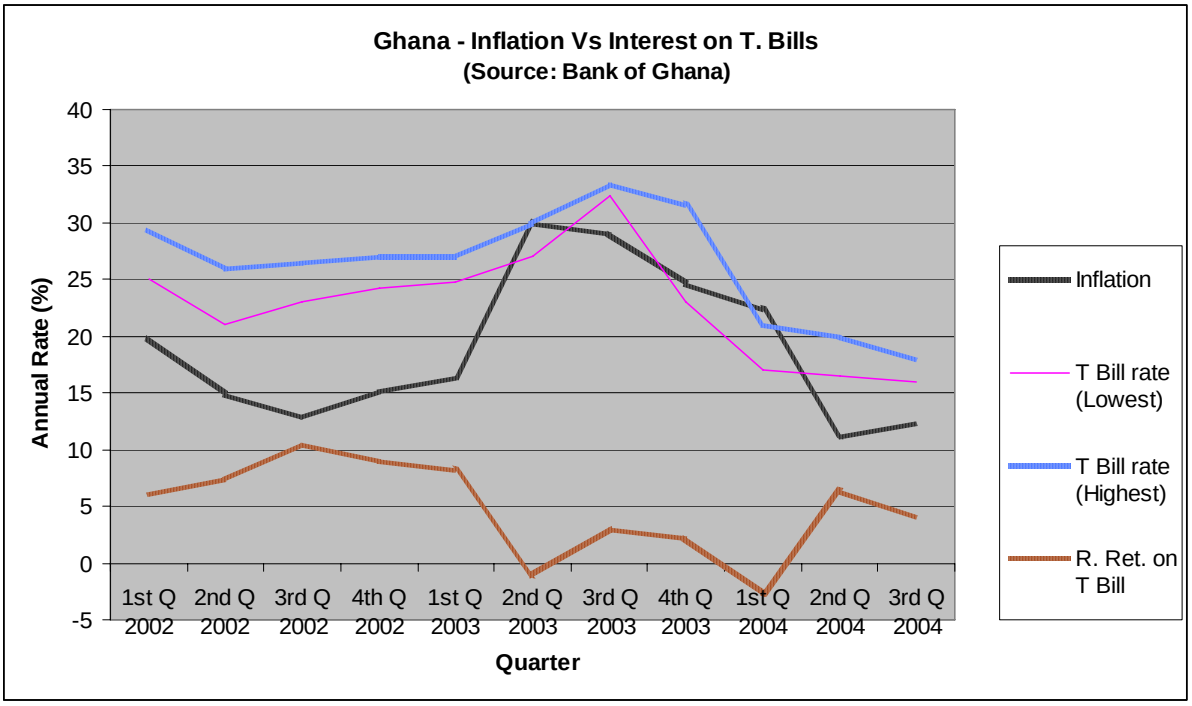
Ghana operates a flexible exchange rate regime. The foreign exchange value of Cedi is thus established independently through the use of an inter-bank market and licensed private Forex Bureaux. Ghana fully accedes to Article IV of the IMF Convention of Free Current Account Convertibility and Transfer.

After having been kept pegged at artificial levels for decades, the Cedi was devalued and floated in stages since 1984. In 1995 the government began to use the exchange rate as a nominal anchor against inflation. This strategy involved considerable intervention in the foreign-exchange market and slowed the nominal depreciation. In 1998 the Cedi was stable in nominal terms, falling by just 4% against the dollar. However, combined with average annual inflation of 20%, this translated into a sharp appreciation of the real exchange rate. In mid-1999 the Cedi began a steep slide, falling from Cedi 2,453 per US$ in May 1999 to 6,293 in August 2000. Although the Cedi's fall against the US dollar slowed in the final quarter of the year (when it depreciated by only 3.7%), during the year as a whole the Cedi depreciated by 52% against the dollar, falling from an annual average 2,647 per US $ in 1999 to 5,322 in 2000. The Cedi depreciated by less than 5% in 2001 owing to tighter monetary and fiscal policies, lower inflationary expectations and a reduction in external debt-service payments. Higher imports by construction and utility companies after the government settled its arrears with them, and a lack of intervention by the central bank caused the Cedi to depreciate by 15% against the US dollar during 2002.

The Cedi has been remarkably stable against the US dollar so far this year. On October 17th, 2004, it stood at 8,730 per US $, down only 3.5% on its end-2002 level. This has been the result of strong inflows of foreign exchange caused by high international prices for gold and cocoa and an increase in expatriate remittances. Additionally, there was some official support from the BOG to defend the exchange rate as a nominal anchor, both in terms of monetary policy and foreign-exchange inflows. Although the Cedi has depreciated against the currencies of other major trading partners, owing to the weakness of the US dollar, the large inflation differential between Ghana

and the US and EU means that in real terms Ghanaian exporters are losing competitiveness.

The country does not have a forward exchange market. Thus no hedge is available to MFIs, who obtain foreign currency funds and need to repay in foreign currency, while resources remain deployed locally in Cedis. In the past, the Agricultural Development Bank has run into trouble due to un-hedged foreign currency exposure.



Graph 2 (based on BOG data)

Over the past three years the annual rate of interest on Treasury Bills has ranged from 16% to 33%, depending upon the duration of the maturity and the expected inflation rate at that point in time. The interest on treasury bills has on average been 4.7% higher than the annual rate of inflation. Out of past 11 quarters, interest on Treasury bills has been higher than the inflation rate in 9 occasions; it's only during periods when inflation was very high, but was expected to lower down, that interest on treasury bills was lower (see Graph 2). Treasury bills, therefore, become a safe avenue for investments for the commercial and rural banks in short to medium term. It is, therefore, not surprising that on average banks park more than 30% of their investments in treasury bills; this has the effect of crowding out the funds available for lending to the small borrowers.

Entry capital requirements are high considering the size of the MFIs and the scope for expansion. Despite the different types of institutions involved in MF, the growth of the sector has been slow. This is partly because of physical infrastructure constraints. Interest rates are high. The ultimate beneficiary gets his loans at rates ranging from 26-40%, which increases default risk.

Organizations Interviewed

1. **Agriculture Development Bank (ADB)**
   Agriculture Development Bank (ADB), which is one of the three development banks in Ghana, is playing an important role in providing financial services to the agriculture sector. The Agricultural Development Bank was set up by an Act of Parliament (Act 286) in 1965 to promote and modernize the agricultural sector through appropriate but profitable financial intermediation.

2. **Association of Rural Banks (ARB) Apex Bank**
   Started in 2001, functions as a mini Central Bank for the rural and community banks and provides them banking and non-banking support services.

3. **Bank of Ghana**
   Central Bank of Ghana.

4. **First Allied S&L**
   First Allied S&L is based in Kumasi and has been operating as a Savings and Loan company for about a decade. It has recently acquired additional capital from Africap to meet the new capitalization norms stipulated by the Bank of Ghana

5. **Freedom from Hunger**
   Freedom from Hunger/Ghana has been operating as an independent NGO and is affiliated with Freedom from Hunger through a strategic alliance agreement that further develops, promotes and supports Credit with Education service in the Republic of Ghana, and potentially elsewhere in Africa**.** Based in Accra, it assists the Rural Banks in the training of staff, implementation of systems, and developing of procedures to deliver Credit with Education**.**

6. **GHAMFIN**
   An informal network of institutions and individuals that operate within Ghana's Microfinance Industry to develop an efficient and sustainable MF industry in Ghana.

7. **Ghana Cooperative Credit Unions Association (CUA) LTD.**
   To work as an association of credit unions to provide them essential services in their establishment and operations and to promote and maintain their financial stability.

8. **Ghana cooperative Susu collectors Association**
   Started in 1994, works as an association of Susu collectors who number more than four thousand and form the strong informal system of saving and lending in Ghana.

9. **German Technical Agency(GTZ)**
   This agency is involved in capacity building and training programs to professionalize the MFIs, develop standards of accounting, book-keeping and reporting as well as build a responsive and business like clientele among the poor.

10. **Kraban Support Foundation**
    It is a financial NGO based in Accra and started in 1997. Works with community based cooperative savings and Credit societies. and lending in Ghana.

11. **National Microfinance Centre (NAMFIC)**
    Established in the office of the President of Ghana to coordinate the development of the MF sector and to give it policy support.

12. **Sinapi Aba Saving & Loan Company**
    Sinapi Aba S & L has recently received license for operating as a savings and loan bank. It is a sister concern of Sinapi Aba Trust and has been created to expand its microfinance program. It has started operations with a branch in Kumasi and is likely to expand its operations soon.

13. **Sinapi Aba Trust**
    Sinapi Aba Trust is a NGO working in Ghana. Its central objective is foster enterprise development among and to increase incomes of the economically disadvantaged sections of the society. It has a well established microfinance program. It has recently established Sinapi Aba S&L to run its microfinance program on commercial principles and to mobilize money through deposits for growth.

14. **Sikaman Savings and Loans company**
    An NBFI base in Accra with a focus on lending to micro and small enterprises. Their micro loans are in the range of approx. $500-1000.

15. **Upper Manya KRO Rural Bank Limited**
    One of the well functioning rural banks which together form the heart of the formal MF sector in Ghana.

16. **World Bank Office, Ghana**
    Coordinates the WB funded programs in the country in different sectors. Ghana and the World Bank are beginning a very important period in their partnership. Between February 2003 and July 2004 (with the preparation of the Ghana Poverty Reduction Strategy), additional World Bank assistance to Ghana reached **US$725 million**, and is growing. Projects in the portfolio range from sectors such as education and health, to power, land administration, water and sanitation. WB is involved in the Rural Financial Services Project.

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