

Paul A Acquah: Evaluating the banking system in Ghana

Keynote address by Dr Paul A Acquah, Governor of the Bank of Ghana, at the Fifth Banking Awards Ceremony, Accra, 6 May 2006.

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Mr. Chairman,
Honourable Ministers of State,
Executives of Corporate Initiative Ghana,
Captains of Industry,
Distinguished Guests,
Ladies and Gentlemen,

1. Thank you very much for the invitation to be the Guest of Honour and Keynote Speaker for this edition of the Ghana Banking Awards event. My understanding is that this is the fifth in the series of banking awards and judging by the array of personalities assembled, it would be right to say that this event has come of age and would remain an expected event on the annual corporate calendar.

2. Mr. Chairman, today's event is truly important and very much welcome. First of all it is purely a private sector initiative, largely driven by consumers of the products and services of the banking industry, and designed not only to recognize excellent banking service delivery but also to foster competition among banking service providers. Secondly, I know that this event has over the years urged banks on to invest in their capacity to deliver superior services either to keep their leadership position(s) or to attain such leadership in the various areas. Thirdly, the event can be seen as a forum where market participants, the consumers of banking services, cast their votes openly with regard to their perceptions and assessments of the quality of the services they receive from individual component banks that constitute the financial system. This type of consumer assessment is of special interest also to the central bank, as the regulator responsible for maintaining the stability and soundness of the industry, and confidence in the financial system as a whole.

3. The public has a legitimate and fundamental interest in an efficient, sound, liquid and well-functioning banking system, that is well-regulated within a stable macroeconomic environment. A banking system that is effective in mobilizing resources and channeling them into productive investments and in support of growth.

4. Mr. Chairman, as with most developing countries that have pursued economic and structural reforms, Ghana has been undergoing a process of financial sector restructuring and transformation as an integral part of a comprehensive strategy for some time.

It is fair to say that we have moved from the history of severe distress and dysfunction in the banking system, illiquidity and insolvency, interest rate controls and credit rationing to a market-based regime. As part of the process, policies and measures were directed at improving the regulatory framework and strengthening bank supervision to ensure increased efficiency and profitability of banks. A policy environment of volatile and generally high

1. inflation, large exchange rate swings, and negative real interest rates over extended periods resulted in an unsustainable portfolio of non-performing assets on the books of many commercial banks that had to be cleaned out.

2. Heavy domestic borrowing by government to finance deficits and a growing domestic debt burden crowded out private sector finance. Faced with an ample supply of relatively low-risk, high return government paper, banks and other financial institutions have had little incentive to engage in – or develop the capacity for – lending and equity finance for the private sector. The debt-interest rate and price dynamics of the past has fostered a short-term perspective among both savers and lending institutions. And one consequence has been very limited access by small and medium-sized enterprises to credit.

3. Mr. Chairman, in the current regime of macroeconomic stability, banks are in a position to efficiently play their primary role as financial intermediaries in the economic growth process, channeling funds from savers to borrowers for investment. Today, macroeconomic stability is being increasingly taken for granted and it is no wonder therefore that the focus of the debate in recent times has shifted to how

to accelerate growth and create employment. At the centre of that debate is a critical role for banks and other financial intermediaries, and the need for a vibrant domestic capital market.

4. Effective intermediation requires that banks mobilize all available financial resources and deploy them in income-generating economic activities. Banks must expand credit to the productive private sector to support international trade, including sub-regional trade. Although there has been some increase in real credit in the last few years, small and medium-scale enterprises still have considerable difficulty accessing credit.

5. Mr. Chairman, since the theme of this award ceremony is efficiency and competitiveness in the banking industry, let me now turn my attention to initiatives that we have pursued in that regard. Some of these initiatives include the movement to universal banking, the adoption of an open licensing system, and the modernization of the payments system, including establishing a central securities depository and the passage of supportive laws.

6. Universal banking, which involves the removal of restrictions on banking activity, was introduced to allow banks to choose the type of banking services they would like to offer in line with their capital, risk appetite and business orientation. It removes for instance, the monopoly that was given to commercial banks in the area of retail banking. It creates room for diversification of the range of financial services that a bank can provide. It allows merchant banks for example to compete for retail deposits. This process would lead to branch network expansion, increasing banking penetration, and also competition for deposits at the retail level.

Universal banking also comes with a higher capital requirement, 70 billion cedis, and this will ensure that banks are sufficiently capitalized to take on additional risk. Banks are also free to take on all aspects of banking, retail,

1. corporate, etc, or they can choose to specialize in a particular segment. Universal banking would therefore make our banks stronger, capital wise and therefore capable of undertaking intermediation at a higher level.

2. Along with universal banking, the central bank has also adopted an open but selective licensing policy, which allows the entry of new banks. The addition of new banks will encourage faster modernization of banking operations and efficiency of the financial system, the better to support the growth and diversification of the financial service industry. Competition should positively affect the tariffs banks charge for their products and services, lower lending rates in line with credit risks, and make credit accessible to all sectors in the economy. We continue to promote rural banking to improve financial intermediation in the rural areas of the country where banking penetration is still low.

3. Mr. Chairman, we are aware that while the entry of new banks would increase competition, excessive numbers within the system could dilute the franchise value of banks and increase instability. Entry therefore has to be selective, well-managed, and paced over time and clear exit rules and prudential supervision vigorously enforced to safeguard systemic stability.

4. Mr. Chairman, the Bank of Ghana has also undertaken a number of reforms of the payment system, including the passage of a Payments Systems Act in 2003 and the introduction of the Real Time Gross settlement System, which has created an environment for safe, sound, secure and timely payments. While the clearing cycle for paper instruments has improved tremendously, the central bank would soon switch to the Codeline Clearing and Cheque Truncation System together with an Automated Clearing House in line with current trends in cheque processing technology. We are also pursuing a policy to be supported by Ghana's Millenium Challenge Account, of integrating all 120 rural banks into the national payments system through a Wide Area Network and supported by a rural bank computerization and capacity-building program.

5. The Bank has also spearheaded the establishment of the Central Securities Depository (CSD) for electronic documentation of all securities, which ensures virtually instantaneous security of title. It is expected that listings on the Stock Exchange would migrate to the CSD. As banks increasingly engage in universal banking, capital market activities would become important and the integration of the banking and capital market operations would be facilitated by these payment and depository systems.

Mr. Chairman, it is clear that the central bank has been putting in place the payments system infrastructure that would facilitate a competitive, efficient banking sector. And the banks on their part have been introducing new services and modernizing their systems. We notice, however, that competition is not well reflected in the pricing of banks' services and there is a general feeling of

market participants that banks are over-pricing risks in the economy judged by real interest rate spreads; this may be as a result of information asymmetry. Yet corporate banking responsibility requires that banks deliver

1. efficient services at competitive rates. In view of this, we are working to put in place another piece of infrastructure, the Credit Reporting Bill to underpin the establishment of Credit reference bureaux. The draft bill should be passed into law this year. It should facilitate credit risk assessment and foster a culture of repayment of loans.

2. Mr. Chairman, as we honour banks for excellence, let me at the risk of dampening some of the exuberance on display, by noting that the consumer complaints unit at the Bank of Ghana has received and dealt with a number of complaints by customers of banks. These complaints normally border on unfair banking practices and include; high interest charges on loans and overdrafts, high bank charges on transactions, non-payment of interest on savings accounts, delays in crediting interest on treasury bills, and high initial deposit and minimum operating balances. I hope that the recipients of the various awards are not that much guilty of such practices.

3. Mr. Chairman, global developments in regulation and supervision of banking is shifting to a focus on risk and the holding of commensurate level of capital. Basel II, the new capital framework to be implemented in 2007 by the advanced countries, is a risk-based framework.

4. For our banking system to remain competitive, the players must understand the risks they undertake and be able to measure and manage them profitably. In line with that we are re-orienting our supervisory focus away from just compliance with norms to a system of risk-based supervision. This will involve re-orienting our approach towards implementing a risk-based supervision process. In this framework our supervisory effort will be directed towards how well banks assess their risks and how actively they are managing these risks and their capital, thereby minimizing systemic problems for the entire banking system.

5. Mr. Chairman, as you may be aware, the end of this year is the deadline for all banks to become compliant with the mandatory capital level for a universal banking license. Over the years some progress has been made in banks re-aligning their capital with that minimum, but a number of banks are yet to get there. It is my hope that these banks would explore all the options, including mergers and listing on the exchange to raise the additional capital for re-licensing. Attaining an enhanced level of capital is crucial for competition in the banking industry, both locally and sub-regionally.

6. Mr. Chairman, the theme for this evening's event 'An Efficient Banking Sector for Competitive Advantage in the Sub-Region' is indeed very appropriate. The Ghanaian banking system must aim to re-position itself to support the strategy of moving to middle-income status and to compete in the wider global sub-regional and even global market. The central bank will continue to support the financial services sector through appropriate policy initiatives and legal framework. In this regard, the new foreign exchange bill as well as the anti-money laundering bill, which would be passed into law this year, should serve to underpin the competitive edge of Ghanaian banks and the financial system in an increasingly competitive global environment.

1. Mr. Chairman, in conclusion, the initiative of banking awards to encourage competition and efficiency in the banking industry is a worthy one. I hope that the banks that have won awards today would be spurred on to further excellence. I also hope that other banks would take a cue from this and work harder in the ensuing years, so that they also can become award winners. And the industry as a whole will continue to enjoy the growing confidence of all stakeholders.

2. Mr. Chairman, Ladies and Gentlemen, I thank you all for the invitation to be part of this event and for your attention.

Thank you.