ANNUAL DINNER OF THE CHARTERED INSTITUTE OF BANKERS (GHANA)

ADDRESS BY

DR. ERNEST ADDISON,

GOVERNOR, BANK OF GHANA

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The President of the Chartered Institute of Bankers,

Chief Executive Officer of the Institute of Bankers,

Fellows of the Institute,

Members of the Banking Fraternity,

Distinguished Guests,

Ladies and Gentlemen

Introduction

1. Good evening to you all. It is an honour and a great pleasure to be here tonight. Not to forget, it is also my first time in my role as Governor of the Bank of Ghana to address this annual event which brings the finest banking professionals and other stakeholders in the financial industry. Certainly, this joyous occasion should provide us the opportunity to de-stress from our very busy schedules and a rather challenging year for the banking industry.

2. We do have sumptuous meals to eat tonight, and while doing that, I will crave your indulgence over the next few minutes to discuss two key issues deemed critical for the central bank's vision of building stronger and resilient banks in the economy. These are building a stronger economy for robust and resilient banks and strenghtening the corporate governance structures of our institutions within the broader financial sector plan.

3. We have started seeing some recovery in the economy after a period of slow growth attributed to challenging domestic and external conditions, with a sharply deteriorated fiscal position due to weak revenue mobilisation and unconstrained spending in the round up to the elections. The large fiscal imbalance impacted on the current account balance leading to a significant deterioration.

4. By the end of 2016, the macroeconomic risks in the economy with inadequate international reserves, a volatile exchange rate, high inflation and rapid accumulation of public debt was a source of concern. These developments were compounded by the energy crisis and disruptions in oil production. The weak economy and problem in the energy sector affected the banking industry with high non performing loans. The environment of high inflation and high depreciation eroded the capital base of banks in real terms and coupled with the impact of the required provisioning due to non performing loans, led to a need for several banks needing to rebuild their capital buffers. The decline in the real capital base of banks when macroeconomic environment is weak provides ample reason why macroeconomic stability must be of utmost priority for building a strong and sustainable banking sector.

5. Ladies and gentlemen, this is exactly what the first order of business of the new government sought to do. The macroeconomic framework of the 2017 budget was anchored on unwinding the large economic imbalances to restore stability. These included bold policy initiatives aimed at fiscal consolidation focusing on tightening expenditure controls and plugging revenue leakages as well as re-profiling short-term debt into long-term instruments to create some fiscal space. These were complemented by monetary policy management strategies to lower inflation and ensure exchange rate stability.

6. The results are clear for all to see: In the year to date, these policies have started gaining roots—inflation has fallen from 15.4 percent at the end of 2016 to 11.6 in October 2017. As a result, the policy rate has been lowered by about 550 basis points with commercial bank lending rates also coming down by some 150 basis, although banks are expected to do better. In addition, there has been relative stability on the foreign exchange market with the cedi depreciating against the US dollar by 4.6 percent since the beginning of the year compared to the same period average of about 17 percent depreciation over the last three years. In addition, economic growth is gradually rebounding supported by significant

improvements in electricity supply, higher crude oil production and some government initiatives targeted at boosting agriculture and manufacturing activities. In the second quarter of 2017, real GDP growth was estimated 9.0 percent as compared with 1.1 percent same period of 2016 and projected to reach 7.9 percent by end 2017.

7. There is no doubt that the current policy debate is about how to move from stability to accelerated growth and employment generation. This is the new paradigm shift we are targeting. However, Madam President, there is no doubt about the fact that macroeconomic stability must remain the necessary condition to facilitate the growth and development objective. For instance, reduction in inflation helps to reduce uncertainty, and helps economic agents to extract information from relative prices. This leads to more investment and efficient resource allocation and higher growth.

8. Ladies and Gentlemen, strong financial institutions operating in a stable macroeconomic environment are the bedrock of financial stability. Such financial institutions typically have a strong capital base well aligned to their risk profile; with a high quality portfolios of assets, high accounting standards, and robust balance sheets; and they have a culture of timely disclosure of information and submit to the discipline of the market. Such institutions are less vulnerable to external shocks and are therefore a source of resilience for an economy.

9. Madam President, this year has been quite challenging and as supervisors, we have been working assiduously to implement measures that would change the recent narrative associated with the banking sector as fragile and poorly supervised. In so doing, we have identified weak corporate governance practices as one of the underlying causes for the challenges facing the sector.

10. Corporate governance plays an important role in promoting a sound financial system—contributing significantly to improving overall performance, not only profits but more importantly reputation of banks and credibility of the entire financial sector. Good corporate governance mechanisms revolve around the basic tenets of **fairness, transparency and accountability**. Good corporate governance is critical to the proper functioning of the banking sector and the economy as a whole.

11. Ladies and Gentlemen, banking is a business and a good business at that but one that demands integrity and unquestioned reputation. Let me repeat a story once shared by a former Governor of the Bank to this fraternity. The Goldsmiths, who originated banking, saw a business opportunity after realizing that people who deposited gold with them only withdrew a fraction at a time, while others placed more deposits. They then deduced the possibility of profit making by lending out a proportion of the gold deposits and hoping that all the gold would not be recalled at the same time.

12. But, the goldsmiths were not experts in the theory of probability. Hence, their credbility and reputation became the most priced asset. They became acutely aware that if at any given time the public lost confidence in their ability to safeguard the deposits, a run on them would bring certain calamity. Over time the business of banking has grown in complexity but the basic tenets of credibility and reputation has fundamentally remained the same. Your own Institute, the Chartered Institute of Bankers Ghana has as its motto, Honesty and Integrity.

13. All over the world, the history of banking crisis indicates that without the public's assurance of well-capitalized, liquid and sound banks, the intergrity of the financial system, just like the Goldsmith, would be at risk. The system would be unstable, prone to a run, resulting in closures and financial distress for depositors. This will spillover to economic challenges and weaken growth prospects in the long run.

14. Globally, there are several examples of corporate governance failures in the financial sector which had adverse economic consequences. Indeed, the global economy is still recovering from the contagion effects of the US financial crises, which occurred about a decade ago.

15. In our own history, the banking sector has witnessed its fair share of corporate scandals and bank failures. Looking back to the 1980s, the Ghanaian economy experienced one of its worst performances which spilled over to the banking sector. Signs of financial distress emerged as public confidence in the financial sector waned, aggravated by a demonetization programme, and negative real interest rates on bank deposits. The loan books of banks became severely impaired and eroding the capital base of the affected banks.

16. Over time, the economic difficulties coupled with poor corporate governance structures resulted in the eventual collapse of four banks and restructuring of others. These failures prompted the need for extensive policy measures and reforms to strengthen the legal and regulatory frameworks. Several laws were enacted to enhance business practices and risk management systems in the banking industry. As time progressed, other pieces of legislature were enacted in response to the changing dynamics and in line with international standards.

17. Ladies and gentlemen, in recounting this history, I am seeking to draw attention to the adage that 'history repeats itself'. Despite the improved regulatory environment and supervisory frameworks, we have witnessed the resolution of two banks this year. While no systemic challenges to the financial sector arose from the resolution, it is useful to understand the underlying factors and reposition the sector to avoid the same mistakes in the years ahead.

18. Let me be upfront and say that though the failure of the two banks was due to significant capital deficiencies, the underlying reason was poor corporate governance practices within these institutions. In this instance, we saw the dominant role of shareholders who exerted undue influence on management of the banks, leading to poor lending practices. This was also reinforced by weak risk management systems and poor oversight responsibility by the boards of directors. Some of the examples of recklessness that led to the failure of the two banks include:

- **Co-mingling of the banks' activities with their related holding companies**. For instance, one bank was paying royalties for the brand name, even at the a that the bank's financial performance was abysmal and could not pay dividends. Interestingly, the royalties were approved by four (4) out of seven (7) members of the Board without the consent of the other significant minority shareholders including an International Financial Institution. As a result, the international institution placed a notice on its website abrogating all relationships with the Bank and this led to most of the foreign lenders cutting off their credit lines to the Bank and recalling their credits thereby creating serious liquidity squeeze to the bank.

- Also, very **high executive compensation schemes** were being operated by the affected banks which were not commensurate with their operations. The risk and earnings profile of the banks could not support the compensation schemes.

- Non-Executive Directors of the banks compromised their independence and fiduciary duties to serve as checks on Executive Directors. This was because rewards such as business class air tickets were being granted to them annually.

- Interference by Non-Executive Directors in the day-to-day administration of the banks weakened the management oversight function of executive directors. Some non-Executive Directors were also acting as consultants to the same banks with no clear mandate, which gave rise to conflict of interest situations.

- **Non-adherence to credit management principles** and procedures as the banks were heavily exposed to insiders and related parties. There was also no evidence of interest payments on these investments. The investments were therefore impaired, but some members of the Board at the time accepted the responsibility to pay off the said amount through a board resolution.

- Diversion of funds to holding companies and their related parties was wide-spread. In the case of one Bank, placements could not be traced to the bank's records though some customers showed proof of their investments with the Bank.

- Irregular board meeting also accounted for the weaknesses in the board oversight.

- In all of these cases, one thing was clear, and that is, the banks could not delineate themselves from their past practices as finance houses. They followed the same practice of borrowing from high net worth persons at a very high costs without any plans to bring themselves in line with the industry norm.

19. Certainly, it is for these numerous reasons that the central bank is seeking, among others, to enhance corporate governance practices as well as risk assessment frameworks across all banking institutions. This will contribute significantly to improve overall performance as well as the reputation of banks and credibility of the entire financial sector.

20. Some may ask, what were the Banks supervisors doing during all this time with such gross violations going on in the banking sector.

21. Upholding the highest ethical standards and professionalism in the performance of our supervision function cannot escape my watch going forward, and I demand same from you all. We shall employ an appropriate mix of both on-site supervision and off-site surveillance to implement the **Risk Based Supervision Framework**. The Bank's supervision examiners have built capacity on the subject and will assess banks' risk management frameworks for effectiveness, responsiveness and timeliness in dealing with risks, deploying resources and in protecting depositors' funds.

22. As part of the Bank of Ghana's regulatory mandate, we are working on **corporate governance directives** for the banking sector. Among others, these directives will focus on oversight responsibilities of the Board of Directors and bank management, prioritize risk management systems, and ensure independent audit roles, among others. In particular, the guidelines will impose the tenure of Chief Executive Officers and Non-Executive Directors of banks, the size of bank Boards, the retiring age for Directors and disclosure of attendance at Board meetings by Directors in annual accounts.

23. These initiatives are underscored by the fact that banks need **sound corporate governance practices** to build public trust and confidence, as well as operational credibility. Without these, banks stand the chance of eroding public trust and ultimately jeopardizing shareholders investments and depositors' funds and most importantly weakening economy activity.

24. Another guideline which will strengthen corporate governance structures in the banking sector is that on **financial publications**. This has been updated to include detailed corporate governance disclosures by banks and the inclusion of provisions on corporate governance under the Banks and Specialized Deposit taking Institutions Act, 2016 (Act 930). The guide for financial publications seeks to ensure that International Financial Reporting Standards (IFRS) are adopted in the preparation and presentation of financial statements. It also seeks to clarify and provide direction as well as bring uniformity in the financial reporting process across the industry.

25. In addition, the Bank has issued the **Basel Capital Requirement Directive (CRD)** for feedback from the banking industry as part of preparations towards the implementation of the Basel Capital Accord. All these seek to achieve fairness, transparency and accountability, which are core tenets of good corporate governance.

26. These notwithstanding, there is also a role for the financial institutions even as the central bank updates the role corporate governance plays in its approach to supervision. Financial institutions must embrace these efforts with a strong internal governance culture committed to the highest standards of integrity, transparency and proper controls.

2018 and beyond

27. Madam President, in the year ahead, our banks will be **Basel II/III compliant**. As we speak, all banks have the **Capital Requirement Directive** and I implore your active participation in the implementation process.

28. Following the passage of the BSDI Act, 2016 (Act 930), the Bank of Ghana has reviewed existing directives and regulations to align with the Act. This, together with the **Internal Capital Adequacy Assessment Process** (ICAAP), will strengthen the supervisory review process, which is a requirement under Pillar II of the Basel accord.

29. We are also driving the **disclosure requirements** in conformity with Pillar III of the Basel accord to enhance appropriate information flow to market participants. Consequently, the Bank will ensure strict adherence to the

Guide for Financial Publication and the BSDI Act particularly with regard to publication of financial statements (both audited and unaudited), and other regulatory breaches.

30. In 2018, Banks will be required to strenghten their capital base with the **revision to the minimum capital requirement**. The GH¢400.00 million minimum capital requirement is in line with the broader financial sector reform plan which seeks to develop and strengthen the banking sector to support the government's transformational agenda. We will aggressively ensure that banks comply with this directive.

31. In view of this, we shall start **reviewing banks' capital build-up plans for compliance** to the directive and assist banks which would consider the option of mergers and acquisitions. We would also engage the Ghana Stock Exchange to facilitate processes for banks seeking long term equity financing to list on the exchange.

32. The key risk in the banking industry today, is the increasing level of impaired assets. This has heightened bank's risk aversion to credit delivery. Our immediate response is to reduce some of the structural bottlenecks in the credit process. Currently, we are reviewing the governing legislations on the credit reference and collateral registry systems. These are to ensure that banks submit both positive and adverse findings on borrowers to the bureaus and also address some thorny foreclosure issues.

33. I have requested in my last quarterly meeting with the Chief Executives of Banks, detailed plans on how each bank will resolve its non-performing loans on a loan by loan basis. We shall enforce our directive on loan write-off going forward, and require appropriate disclosure of written-off facilities in the published financial statements of banks. It is our expectation that the national identification program coupled with the improved economic prospects would support these measures and help in reducing the incidence of loan defaults in the banking sector.

34. In the coming year, Madam President, **crisis management** would be a more concerning issue, more especially the crisis response capacity of banks. This is a lesson I learnt the hard way when I assumed office earlier in April this year dealing with 2 banks nearly on the verge of collapse and it is a sure way for enhancing customer confidence in the system.

35. The **deposit protection scheme** is expected to come on stream next year in line with the BSDI Act and the Ghana Deposit Protection Act, 2016 (Act 931) to provide a safety net for vulnerable depositors in the event of a bank failure. I entreat banks to study the Ghana Deposit Protection Act to know the requirements for enrollment on the scheme.

36. The management of potential threats to financial stability and the **avoidance of systemic crisis** would also preoccupy our attention in the coming year. To ensure the safety and soundness of individual banks, our risk focus supervisory frameworks will gauge cross sectoral interactions among financial players. The financial boundaries are increasingly becoming blurred, hence there is need to adopt a holistic macro-prudential approach and implement consolidated supervision in line with the BSDI Act, 2016 (Act 930).

37. To this end, we shall continue to **engage other regulatory bodies, both domestic and external**, and share information and experiences. In particular, we shall continue our collaboration with the Central Bank of Nigeria (CBN) to conduct joint examination on banks with Nigerian parentage under the framework of the College of Supervisors of the West African Monetary Zone (CSWAMZ).

38. In recent times, there have been increased activities in the payment ecosystem as a result of innovation and its role in promoting financial inclusion which is a global goal. The Bank in order not to stifle innovation and also create the enabling environment drafted the Payment Systems and Services Bill to replace the existing Payment Systems Act 2003 (Act 662) and the Guidelines for Electronic Money Issuers (2015). The Bill is expected to enhance electronic banking, agency banking, and payments and also provide support for a strong and resilient banking sector.

39. I have noted that banks have formed various strategic alliances with Mobile Money Operators (MMOs) and financial technology firms to transform the way banking products are delivered. Through these partnerships the unbanked are able to purchase Government debt through the use of mobile phones, receive inward remittance on mobile device and link bank accounts to mobile money wallets for access to micro-loans.

40. Another form of partnership between the banks and MMOs is the holding of mobile money customers' funds by the commercial banks. All mobile money float currently resides with commercial banks as MMOs are not authorized to hold funds. The top 5 banks holding these float as at

October 2017 included Fidelity Bank, Ecobank, CAL Bank, Stanbic Bank and HFC Bank. We encourage all banks to take advantage of the telecos platforms to further support the financial inclusion efforts.

41. The Bank of Ghana is reviewing its licensing procedures when lower tier institutions such as savings and loans companies want to migrate to banking institutions. We are also reviewing definitions around fit and proper test in approving Directors of financial institutions including possible annual certifications of their knowledge of key banking risk assessments. We may impose requirements for directors and senior management of banks to certify related party transactions. We will impose swift sanctions to individuals and institutions that infringe or breach our regulations. We will scrutinize interbank borrowing and placements and review the manner in which we provide emergency liquidity support. We will advocate a whistle blower provision to protect individuals who raise alerts to the Bank of Ghana on malpractices by the banks.

42. To conclude Ladies and Gentlemen, the aim of the Institute of Bankers is to heighten professional excellence in the Banking Industry in Ghana. Your motto of Honesty and Integrity needs to be jealously guarded to positively project the profession of banking. Despite the daunting odds facing the profession, successive leaders of the institute have made significant strides to make the institute what it is today. I charge the Institute and current executive of the institute to up its game and conduct the necessary training and awareness programmes required to ensure high ethical and professional standards in the banking fraternity.

43. Madam President, on this note let me thank you for the attention and wish you all compliments of the coming festive season. Thank You.