

Ghana: Long Term Growth, Atrophy, and Recovery

A report for the OECD Development Centre project
Emerging Africa

by

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List of Acronyms

ADB	Agricultural Development Bank
AFRC	Armed Forces Revolutionary Council
AGS	Ashanti Goldfields Corporation
BBG	Barclays Bank Ghana
BED	Bank Examination Department
BHC	Bank for Housing and Construction
BMP	Black Market Premium
BOG	Bank Of Ghana
CDRs	Committees for the Defence of the Revolution
CMB	Cocoa Marketing Board
CPI	Consumer Price Index
CPP	Convention People's Party
DIC	Divestiture Implementation Committee
ERP	Economic Recovery Program
ESAF	Enhanced Structural Adjustment Facility
FINSAP	Financial Sector Adjustment Program
GCB	Ghana Commercial Bank
GOG	Government of Ghana
GSE	Ghana Stock Exchange
NAL	National Alliance of Liberals
NBFI	Non Banking Financial Institution
NDC	National Democratic Congress
NIB	National Investment Bank
NLC	National Liberation Council
NPA	Non-Performing Asset
NPART	Non-Performing Assets Recovery Trust
NRC	National Redemption Council
PDC	People's Defence Committee
PNDC	Provisional National Defense Council
PNP	People's National Party
SCB	Standard Chartered Bank
SMC	Supreme Military Council
SOE	State Owned Enterprise
SSB	Social Security Bank
SSNIT	Social Security National Insurance Trust
UGCC	United Gold Coast Convention
VAT	Value Added Tax
WDC	Workers' Defence Committee

Chronology of Regimes and Events Since World War II

- 1946 African majority in Legislative Council.
- 1948 Political agitation against 1946 constitution.
- 1951 New constitution granted internal self government; election won by Nkrumah in landslide.
- 1954 Further elections won by Nkrumah as Prime Minister, and again in 1956.
- 1957 Independence (March 6), Nkrumah as Prime Minister.
- 1960 Ghana becomes republic and Nkrumah President. Exchange controls imposed.
- 1964 Single party (CPP) government.
- 1966 Military coup, replaces Nkrumah and establishes National Liberation Council; Brigadier A.Afrifa initially Commissioner of Finance and later Chairman.
- 1967 Devaluation of Cedi from ₵0.71/\$ to ₵1.02/\$.
- 1969 Elections (August), and elected government led by K. Busia takes office (October).
- 1971 Devaluation of Cedi from ₵1.02 to ₵1.82/\$ (December).
- 1972 Military coup overthrows Busia government; establishes National Redemption Council with I.K. Acheampong, Chairman (January). Revaluation of Cedi to ₵1.28/\$, and import and exchange controls tightened (February).
- 1975 Acheampong replaces NRC with all military Supreme Military Council.
- 1977 Inflation exceeds 100% for first time.
- 1978 SMC replaces Acheampong with General Akuffo (July). Cedi devalued to ₵2.75/\$. Urban strikes and political unrest (June 1978 through May 1979).
- 1979 J.J. Rawlings attempts coup (May), put on trial; mutiny of lower ranks replaces SMC with Armed Forces Revolutionary Council (June), headed by Rawlings, which launches campaign against corruption and black marketeering. Acheampong, Akuffo, and Afrifa executed. Scheduled elections held (July), won by Limann who takes office (September).
- 1981 Rawlings leads new coup (December 31), establishes Provisional National Defence Council government.
- 1982 Disastrous events, including drought, murder of judges, expulsion of Ghanaians from Nigeria, and attempted coups.
- 1983 Economic Recovery Program launched, and gradual recovery of economy begins.
- 1992 Government budget deficit reopens. Elections for President won by Rawlings. Opposition boycotts parliamentary elections.
- 1996 Elections for President won by Rawlings, and several opposition members elected to parliament.
- 2000 Elections scheduled for December, Rawlings ineligible to run, and has declared intention to retire.

Introduction

Ghana's independence in March 1957 was celebrated with great flourish. “Free at last !” Kwame Nkrumah, the country's leader, proclaimed.

Yes, Ghana was free to follow an independent political course, and free to experiment with an independent economic direction. But the exercise of that freedom proved to be destructive. Gradually removing internal agents of restraint, and unconcerned about external constraints, Nkrumah pursued his grand vision of Ghana. But, that vision became a nightmare. More than a quarter century of increasingly chaotic political and economic turbulence followed.

Eventually a major reform program was launched, but after fifteen years its success has been modest. While the downward spiral has been halted, and real growth resumed, real GDP per capita and total factor productivity have barely exceeded the levels achieved at independence.

The long-run economic and political records are both lackluster, each limiting the potential of the other. The question is, why has Ghana not achieved sustained and rapid long-term growth? This study seeks to provide an answer.

As we review the experience of the forty plus years of independence, five explanatory themes recur.

The first theme is excess demand. Repeatedly, fiscal and monetary policies have been excessively expansionary, generating bouts of inflation, followed by painful adjustment. Ghanaian entrepreneurs have seldom been able to count on a stable macroeconomic environment for more than a few months into the future. Such a short-term horizon has been damaging.

Currency overvaluation is the second theme. Initially the problem was a fixed nominal exchange rate, maintained in the face of domestic inflation. Exchange controls followed, while inflation accelerated. The real price of foreign exchange was depressed to a small fraction of its level at independence, and forced the economy to become virtually autarkic. Recovery of the real exchange rate under the reform program has occurred, but its instability remains a serious source of uncertainty for all – exporters, import competing producers, and foreign investors alike.

Third, closely related to the foregoing, Ghana has frequently failed to realize the potential gains from pursuing and supporting its comparative advantage. Among the traditional exports, cocoa suffered from a variety of devices that suppressed the real producer price and depressed production to well below its optimum. Minerals, until recently, endured state ownership, and neglect of infrastructure.

The fourth theme is suppression of the financial sector. With the state heavily involved in running financial institutions, and repeated confiscation of assets both directly and via inflation, individuals are reluctant to hold financial assets. The financial sector, consequently, does not yet play its potential roles in bringing savers and investors together.

The fifth theme concerns the role of the state. The state was stretched far beyond its abilities. The overextended reach of government and the administrative complexity of many programs pushed the state well beyond the limits of activities that it could handle efficiently and without corruption. This seriously compromised the effectiveness of nearly everything the state was involved in, ranging from education to health care to state-owned enterprises to administration of economic controls. The outcome was a near collapse of the state. Not only was the state ineffective in its economic activities, but it failed to consistently control predation by its agents. Real assets were confiscated, both by direct seizure and indirectly by economic policies. At various times agents of the state extorted huge rents from society and beat hapless victims.

The lingering sense that such experiences might recur, leaves the economy achieving far less than its potential, in spite of significant economic and political reforms achieved over the past fifteen years.

To appreciate why Ghana's modern history unfolded in this way, it is necessary to understand both the political and economic dimensions. We begin in Chapter 1 with an overview of the economic and political record of the various regimes that governed Ghana from independence through to the launch of the economic reform program in 1983. Those reforms and the consequences are the subject of Chapter 2. The major conclusions are presented in Chapter 3.

1. Economic and Political Record

The heavy hand of history hangs over modern Ghana's economics and politics. Overlapping influences of ideology, regional interests, ethnic and religious groups, to say nothing of different economic interests, have all played a role. The rules of the political game have oscillated across democracy, varying degrees of authoritarianism, and different types of banditry. The participation of the state in the economic system has shifted from minimalist colonial oversight to heavy involvement in the means of production, and back towards a middle road.

The current and future economic development of the country thus derive from a complex of past economic and political events. For this reason, we begin this study with a review of the political and economic record from independence through to the launch of the major reform program in 1983.

The initial optimism and perverse economic policies of Nkrumah (1951-1966) were followed by a military coup. After a relatively brief period of resetting economic policies (1966-1969), the reins of government were turned over to the democratically elected Busia (1969-1971), only to be usurped again by the military, but this time with much more pernicious results (1972-1979). After depressing real incomes, and amid widespread disgust with the venality of the officers, a turbulent period followed. The military officers were thrown out by their juniors (1979), to be replaced by an inept elected government (1979-1981). A new attempt by the junior military ranks to restore morality to government (1982) elicited widespread public revulsion for its atrocities and exacerbated the mistrust of government by all economic agents. Finally, an economic reform program was launched (1983), but the economic and political history could not be erased.

The Nkrumah Years

Overview of Politics

Kwame Nkrumah led his country to independence in 1957. Yet even before independence, the foundation of a damaging politico-economic nexus had been laid. Demands that the power of the state be used to arbitrate distributional claims emerged in 1948 when violent anti-colonial protests erupted in Accra, based largely on discontents of urban lower classes. The colonial government seemed incapable of dealing with a range of pressing problems -- from diseased cocoa trees, to inflation, to unemployment of returned service men. When the riots led to looting and several deaths in various urban centers, the colonial government briefly jailed six leaders, including J.B. Danquah and Nkrumah, then respectively leader and organizing secretary of the United Gold Coast Convention (UGCC). This stimulated Britain, the colonial power, to consider constitutional changes beyond the modest 1946 granting of an African majority in the legislative assembly.

Internal self-government was ceded, effective 1951, including eight ministerial posts held by Africans. But this pace was too slow for Nkrumah and those he represented. Nkrumah had split with the more conservative UGCC in late 1949 to form his own Convention People's Party (CPP), and continued agitation for full and immediate "Dominion" status, similar to Australia, Canada, and various other former British colonies. Nkrumah was again jailed, and while still in jail garnered an electoral landslide in the first elections under the new constitutional dispensation (1951). This win was based in part on Nkrumah's reputation as leader of the anti-colonial movement, but also reflected his promises to respond to the interests of the urban lower classes. (See Austin 1966, and Bourret 1960.)

The need for basic services of all kinds was widely acknowledged, both in the colonies that were to become Ghana, and in Britain. It was implicitly assumed that these should be provided by government. The leading role of government was seen as justified by the fact that since the services did not exist, and since there did not appear to exist an African entrepreneurial class capable of offering the services, it was necessary therefore to rely on government. During the first few years of internal self government, Nkrumah and his ministers attempted to respond with large government expenditures, intended to promote rapid economic and social development. This was financed in part by the government surplus which had accumulated during the World

War II, and the high world price of cocoa which was part of the commodities boom induced by the Korean War. The seeds of future economic problems with a bloated public sector were planted.

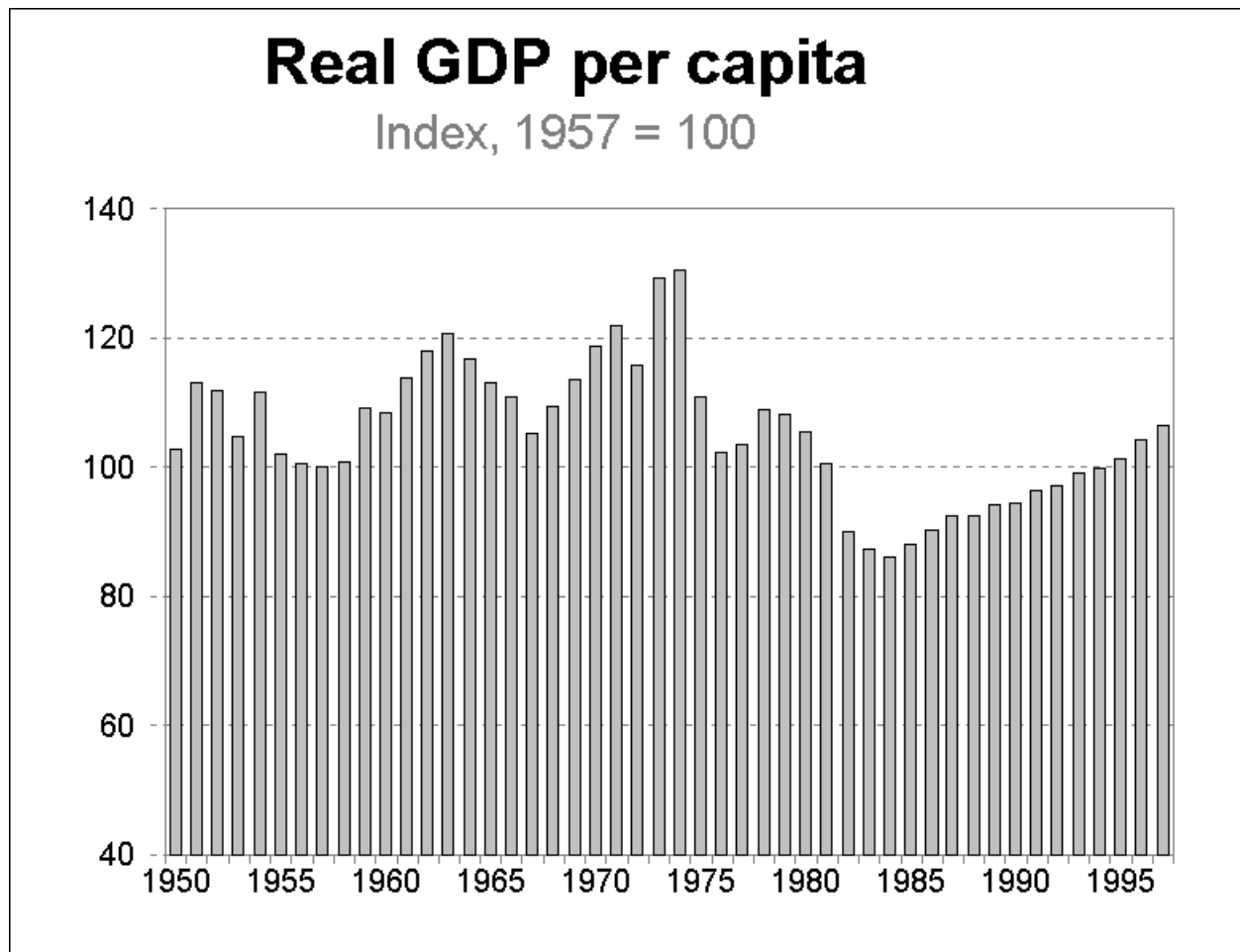
In spite of widespread agreement within the various parts of the future Ghana that independence was a desirable objective, there was not wide agreement on the constitutional structure. Nkrumah and the CPP sought immediate independence with a unitary state, while a combination of regional interests in Ashanti, Togoland, the Northern Territories, and the traditional rulers, sought a federal form of government with safeguards to prevent a post-independence government from altering the rules of the game. Following a decisive electoral win by Nkrumah's party in 1956, Britain acceded to Nkrumah's position, and granted independence effective March 6, 1957.

In the years following independence, the fears of the opposition proved justified. Three years later a plebiscite was held on a republican constitution, creating a unicameral legislature and placing substantial executive authority in the hands of a president. It is widely believed that the CPP manipulated the results to ensure a sizeable majority in favor of the constitution and of Nkrumah as president. This was followed, in 1964, by a referendum declaring Ghana a single party state, and the CPP the only party, which was allegedly endorsed by 99.9% of the voters. Nkrumah was preoccupied with pan-African matters, while the CPP, no longer forced to remain united in the face of an active opposition, became increasingly corrupt and rent by internal disputes. Both Nkrumah and the party were isolated from the society they claimed to represent. Finally, while Nkrumah was out of the country in early 1966, he was ousted in a military coup.

Fiscal and Monetary Policies

Nkrumah left Ghana no better off than when he started. GDP per capita in real terms, despite all its well known limitations, tells the story clearly and simply. (See Figure 1.) By 1966, GDP per capita was no greater than in 1951. This was the outcome of a destructive set of economic policies. The primary villain was an overly ambitious government expenditure program that pushed the budget deficit to over 6% of GDP. (See Figure 2.) For this reason, we begin our look at Nkrumah's economic policies by examining the sources of excess aggregate demand.

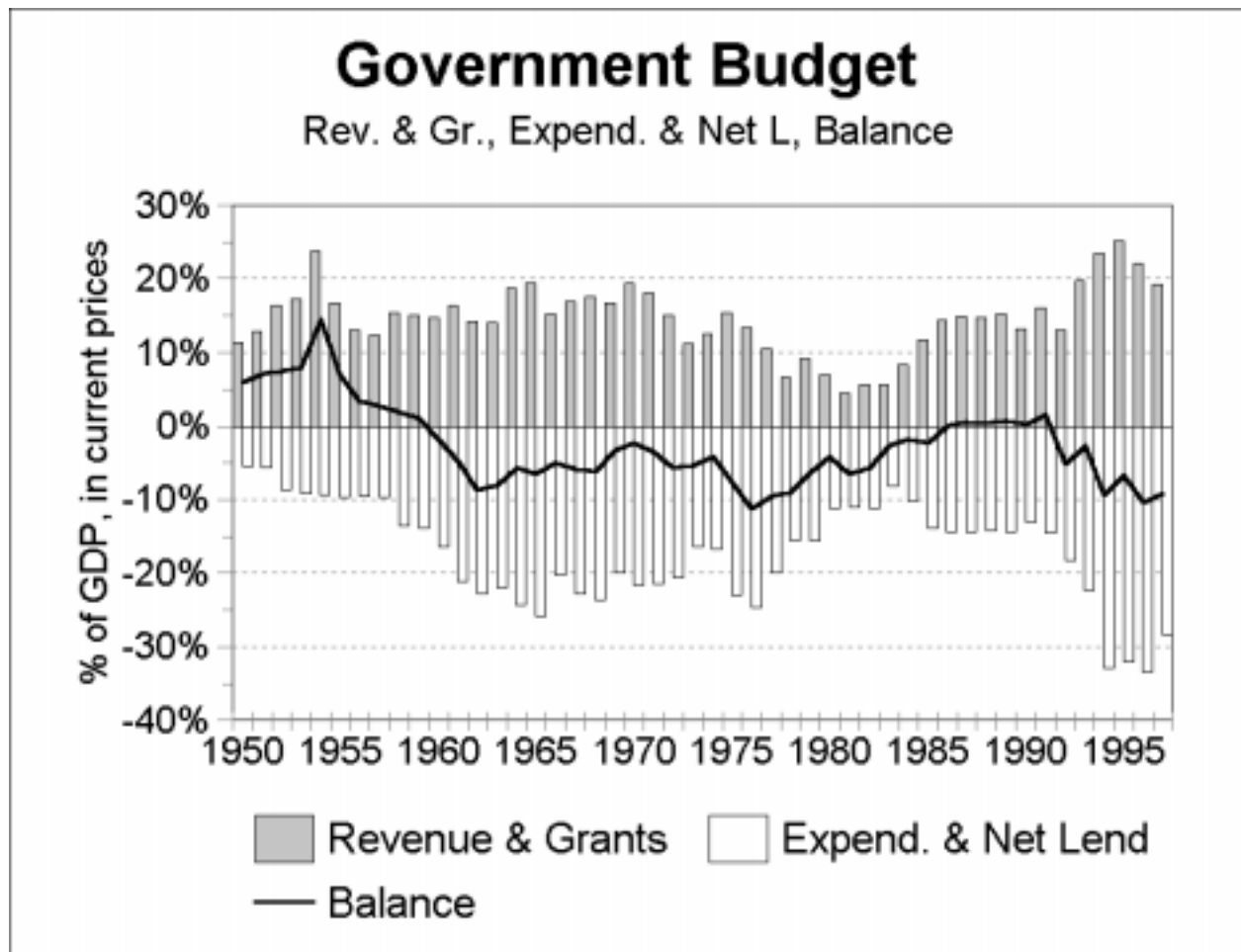
Figure 1



Source: International Financial Statistics

The colonial legislature had no power to pursue independent economic policies. Before the introduction of internal self government, taxation, mostly on foreign trade, including cocoa, was set by the British colonial administration. Similarly, government expenditure budgets were set by the colonial governors, and strict financial controls ensured that budgets were not overspent. The currency was the pound, issued by the West African Currency Board, in a typical currency board arrangement, with a fixed exchange rate against the pound sterling. Even when internal self government was granted in 1951, the finance ministry was not turned over to an African: it was reserved for a European.

Figure 2



Source: International Financial Statistics

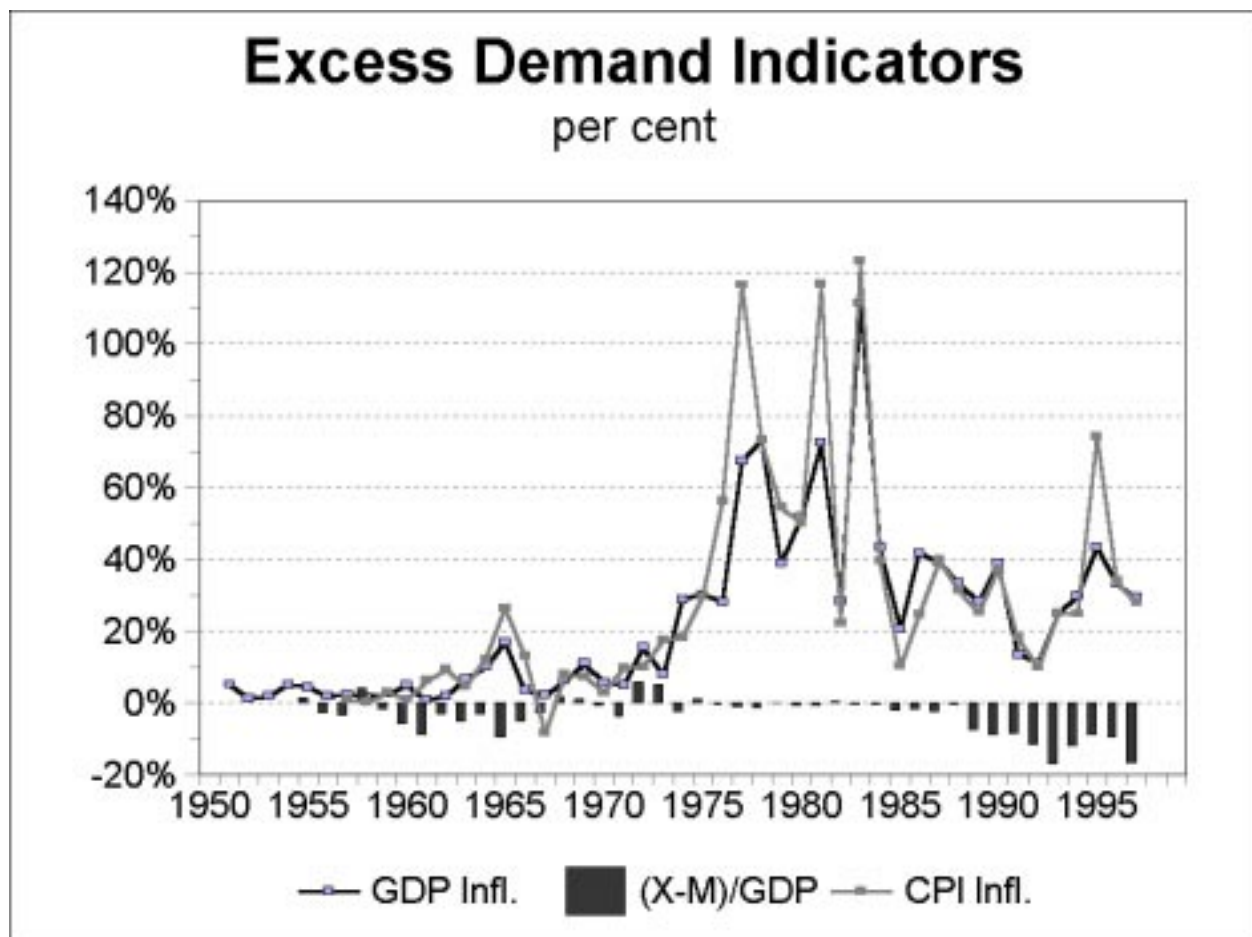
Nkrumah gradually stripped away these constraints. To see the consequences, we look first at various indicators of excess demand. We then turn to examine the sources of that excess demand.

The most common indicator of excess demand is the presence of inflation. There are various measures of inflation, the most widely cited measure being the rate of change of consumer prices. This uses weights that reflect the expenditure patterns of the typical family. Another common measure uses the GDP deflator, which reflects prices of the goods and services that are produced in the domestic economy. Both tend to move together, but because consumer price indexes

exclude items that may be a significant part of the domestic output, the CPI measure is usually more exaggerated in its movements.

From the perspective of the 1970s and early 1980s, inflation under Nkrumah was not substantial. However, from the perspective of the time and in view of the fixed exchange rate, it was significant. Further, both measures of excess demand pressure were accelerating. By 1965, Nkrumah's last year in power, CPI inflation had exceeded 20% (Figure 3).

Figure 3

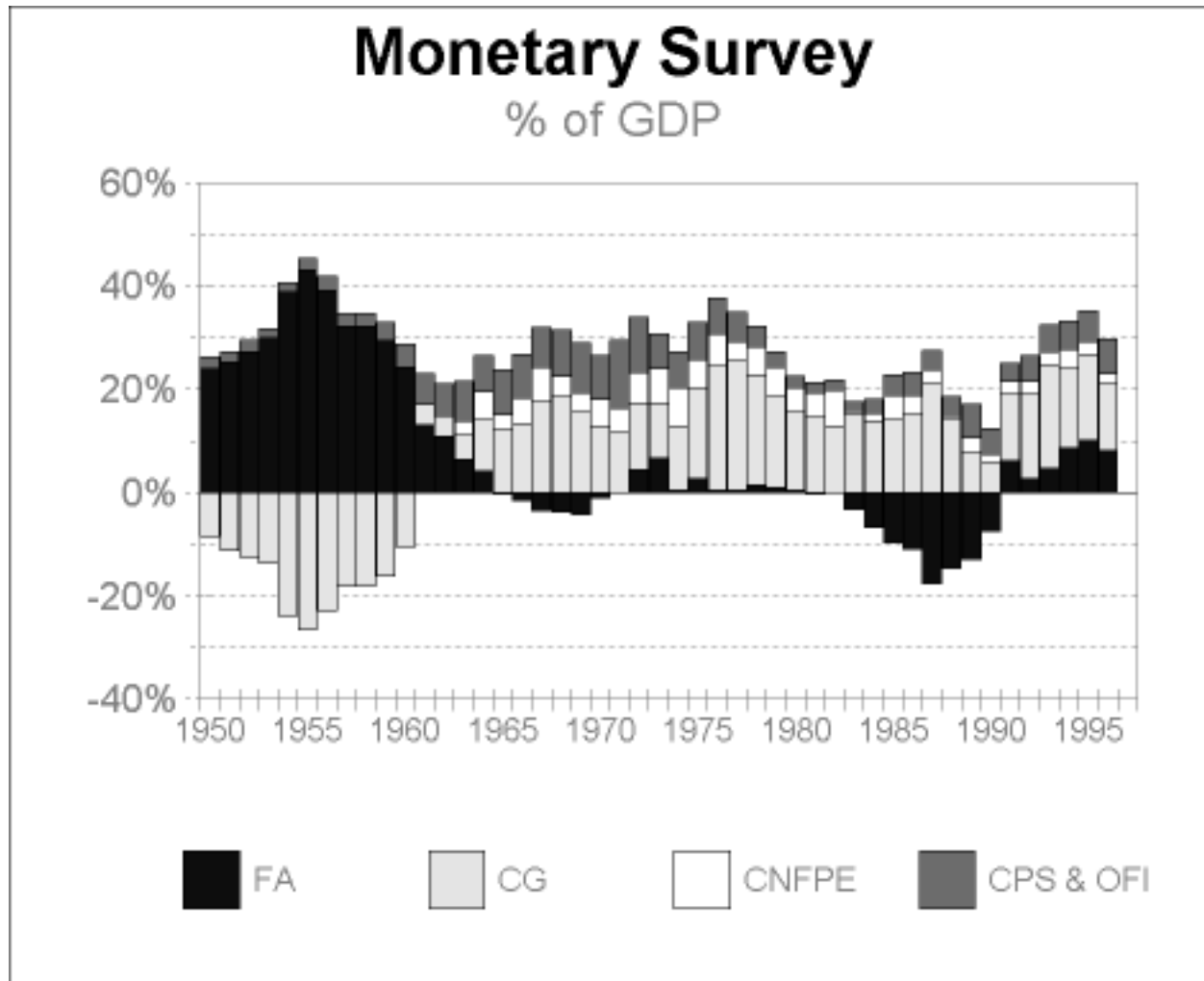


Source: International Financial Statistics

Yet, it is possible to have excess demand without inflation if the excess demand is being met by supply from outside the domestic economy. Given the possibility that the excess demand may show itself in different ways at different times, it is necessary to look at indicators of both the

external account and internal prices to identify the presence or absence of excess demand. In light of this, in Figure 3 we also report the exports minus imports of goods and services, relative to GDP. This reveals that during the first half of the 1960s a significant deficit was run. The cumulative effect of the deficits was to draw down the foreign assets of the banking system from a peak in 1955 of over 40% of GDP to zero at the end of 1965 (Figure 4).

Figure 4



Source: International Financial Statistics

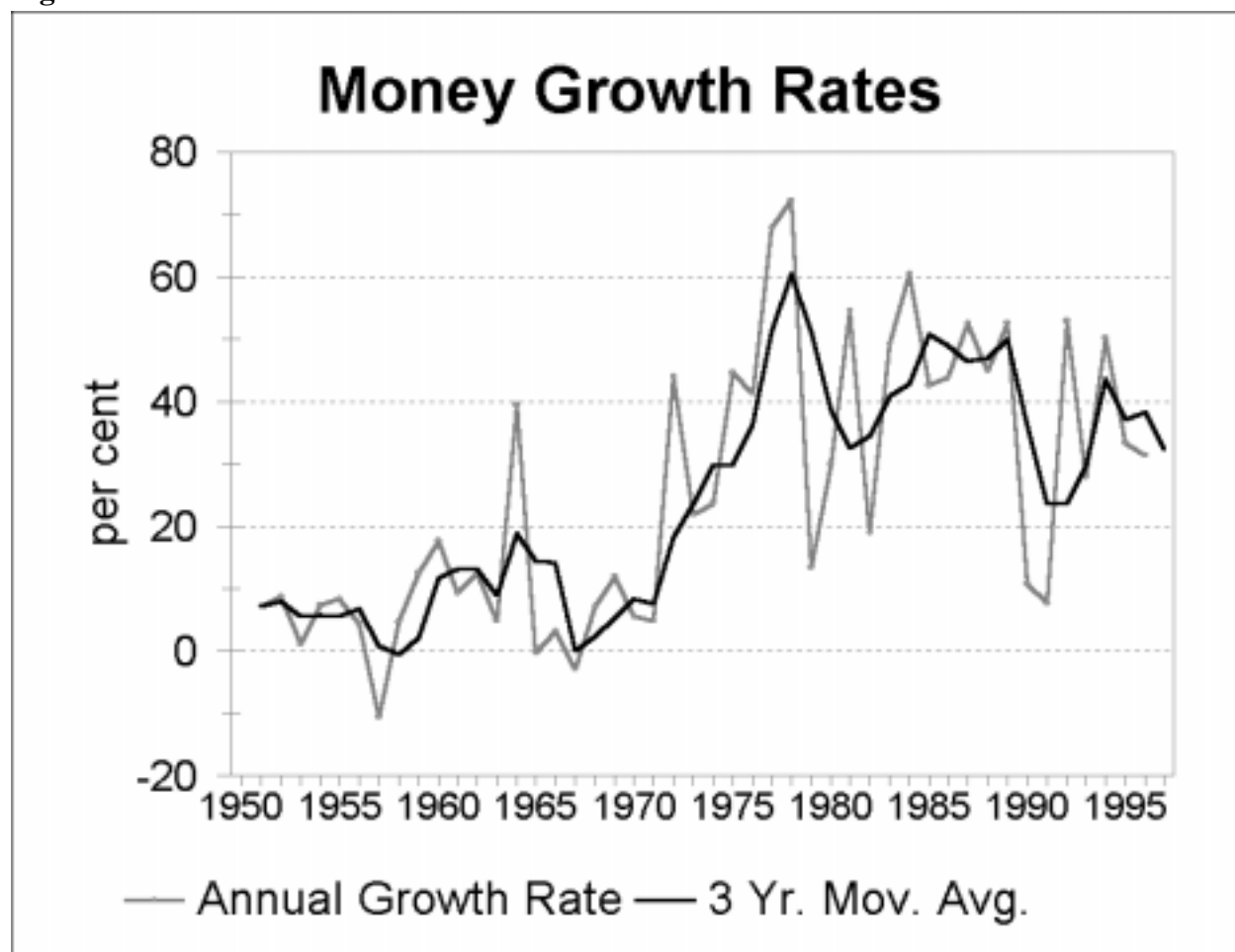
In addition to drawing down substantial foreign exchange reserves, Nkrumah incurred a significant foreign debt, in part for major development projects, but in part as suppliers' credits financing current purchases. Thus, the ability to run a current account deficit by drawing down reserves and taking on short-term debt enabled Nkrumah's government to keep inflation from becoming more serious in the face of a substantial excess demand.

It remains to identify the sources of that excess demand. Potential sources of excess demand include, of course, the government budget, and loose monetary policy. It is clear from Figures 2 and 5 that these were indeed the major influences at work in Ghana under Nkrumah's rule.

Government expenditure grew rapidly, even from the earliest days of internal self government. Although various devices to generate more revenues were implemented, by 1960 a significant and rising budget deficit was left to be financed. Further, the share of GDP taken by government expenditure was rising (Figure 2). In the early Nkrumah years some of the fiscal deficit was financed from foreign sources, including drawing down the foreign exchange reserves and debt, as noted above. A substantial portion was left to be financed from the domestic monetary system. Initially this involved simply drawing down government balances in the banking system, but by 1961 those balances were exhausted. As a result, government began to issue Treasury Bills in 1960, and in the next year became a net borrower from the banking system. Credit from the banking system to government increased rapidly, to the point that at the end of 1965 (shortly before Nkrumah was removed from office) it was 12% of GDP (Figure 4).

At independence the Bank of Ghana was established as the central bank, and the Ghanaian pound created. Monetary policy became *de jure* independent of the colonial arrangements in 1958 when the Bank of Ghana took over both the issue of currency and the foreign exchange reserves from the West African Currency Board. Ghana remained part of the Sterling area, which meant that: imports from within the Sterling area did not require prior authorization; payments inside the area for invisibles were freely made; surrender of proceeds from exports to the rest of the area was not required; and there were no restrictions on capital account payments with the Sterling area. Given the fixed exchange rate and foreign exchange reserves available to draw down, two important features followed from the absence of exchange controls vis-a-vis the rest of the Sterling area. First, the automatic monetary adjustment mechanism was at work: changes in the foreign assets were reflected in changes in the domestic money stock (Figure 4). This kept growth of the money stock within bounds (Figure 5). Second, Ghana's price level was directly linked to the price level in the Sterling area. Together, these features of the policy regime meant that inflation was negligible, and that money growth was on average only slightly greater than the rate of growth of nominal GDP, thus allowing for a modest rate of monetization.

Figure 5



Source: International Financial Statistics

The nascent excess demand could be vented on imports only as long as there were foreign exchange reserves. However, a sea change occurred in 1961. After many months of accelerating decline of foreign exchange reserves,¹ in July the exchange control net was drawn around Ghana rather than the Sterling area, and in December of that year import licencing was introduced. (See Figure 6.) In that same year, government exhausted its local currency bank balances, and started borrowing from the banking system. This combination had several related effects on the macro economy. First, monetary policy now became *de facto* independent of the sterling area. Excess

¹ The anticipation of exchange controls, of course, contributed to the acceleration of the hemorrhage of the reserves.

issue of money would no longer result in capital movement. Second, the consequence of excess issue of money would now be inflation. Third, the import licencing was intended not only to restrict imports, but also to promote import-substitution, industrialization, and geographic diversification of trade towards East-bloc countries. Fourth, as the excess demand for foreign exchange became larger and larger, making the rents to recipients of licences correspondingly larger, the inevitable corruption in the issue of licences emerged.

Figure 6



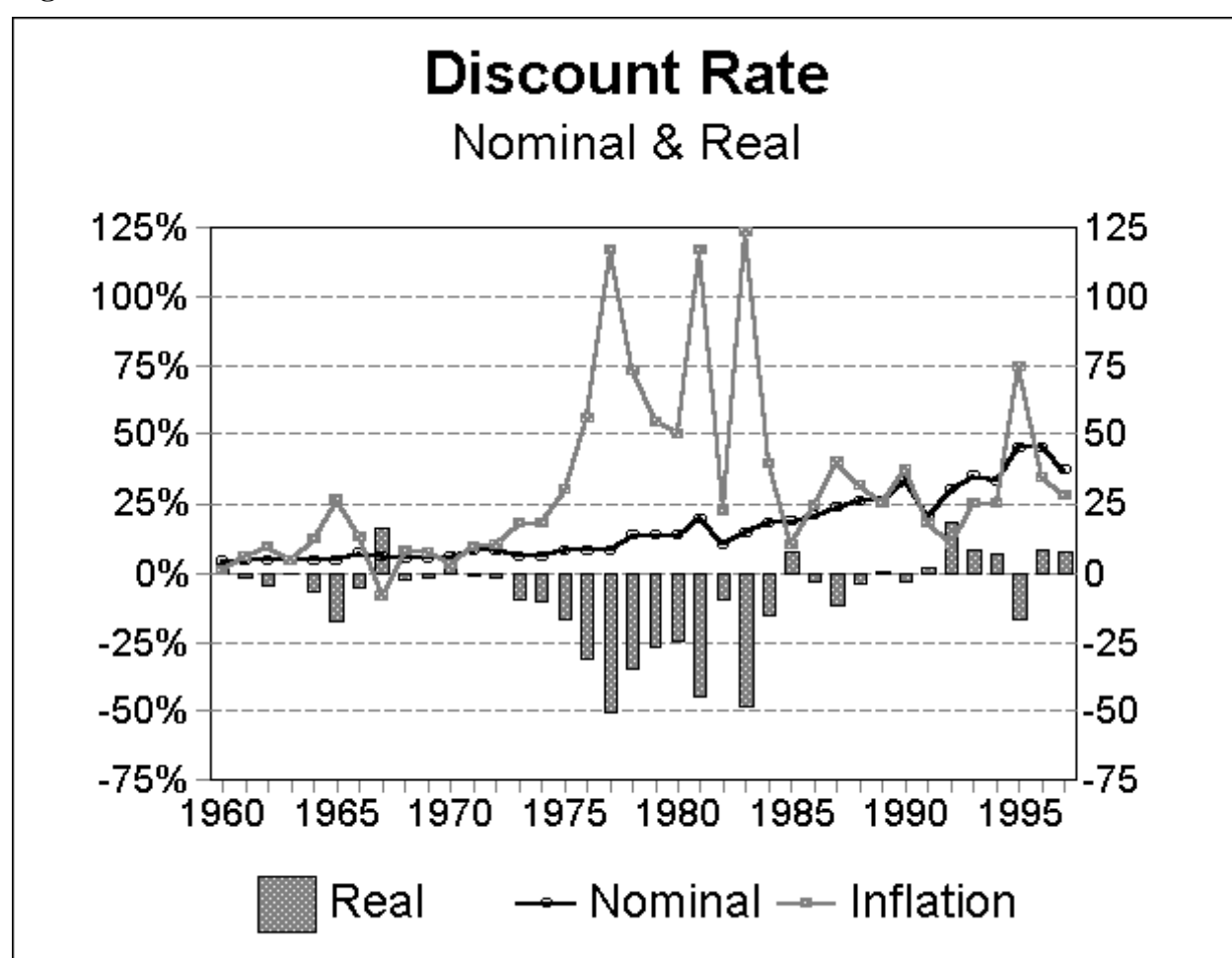
Source: International Financial Statistics

The first of these effects shows up in the monetary growth rate (Figure 5). The three year moving average rate of money growth exceeded 10% in the first half of the 1960s. The initial effect of this was to increase the Money/GDP ratio to over 15%. However, as has happened the world

over, excess money balances were spent, and with the economy now closed, the second effect emerged: CPI inflation rose to exceed 20% by 1965 (Figure 3).

The Bank of Ghana had increased the discount rate by half of one per cent in 1961 as part of the package associated with the introduction of exchange controls. But with inflation accelerating, the real interest rate became sharply negative (Figure 7). Both the private sector and the growing band of state-owned enterprises now had the incentive to increase their borrowing from the banking system, and the favored ones with access to credit responded accordingly.

Figure 7



Source: International Financial Statistics

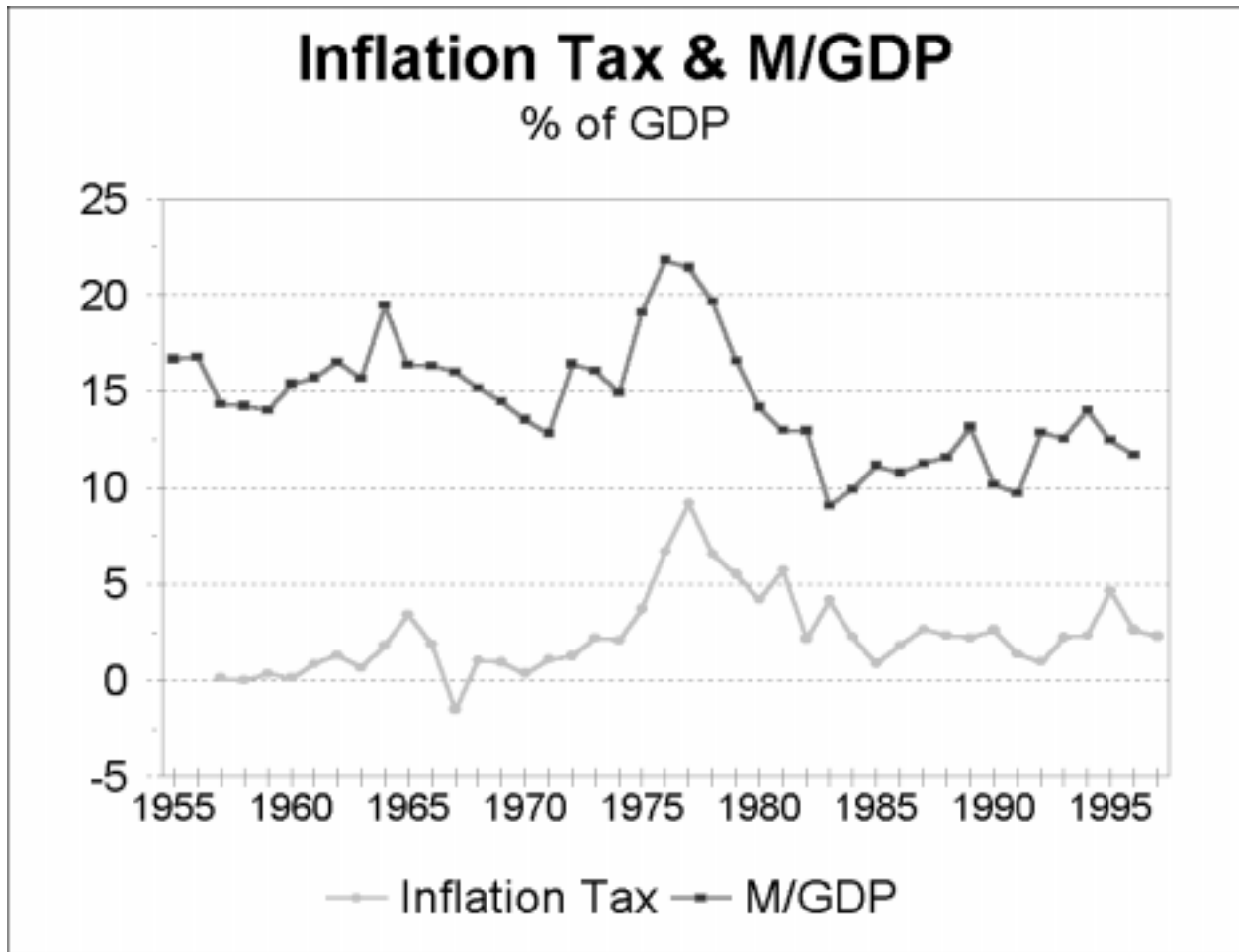
This trend was exacerbated by official policy favoring the state-owned Ghana Commercial Bank (GCB): all state-owned enterprises were expected to bank with GCB, and in 1961 financing of the marketing of the cocoa crop was taken over by the GCB. In addition, the National Investment Bank was set up in 1963, three quarters owned by government, which became a loan window to funnel credit to favored sectors.

With the monetary system insulated from the rest of the world by exchange controls, it was possible to collect an inflation tax.¹ From an initial situation of no significant inflation tax, by Nkrumah's last year it reached over 3.4% of GDP. The public responds to any tax by reducing its exposure to the tax -- in this case by reducing its holdings of money. Naturally this didn't happen immediately, and the incidence varied across agents in the economy. But respond the public did. Despite the fact that money growth and inflation were both sharply reduced following Nkrumah's overthrow, and remained below 10% through the end of the Busia government, the public's holdings of money steadily declined until the next round of accelerating money supply and subsequent inflation (Figure 8).

The decline in foreign exchange reserves understated the extent to which Ghana was living beyond its means. A significant part of the import splurge had been financed by taking on short-term debt. Two thirds of the debt outstanding in early 1966 was suppliers' credits and payments arrears. (See Leith 1974, Table II-6.)

¹ An inflation tax arises from the decline in the real value of non-interest bearing money held by the public. The tax rate, as a proportion of money balances, is the inflation rate divided by $1 + \text{the inflation rate}$. It is also useful to calculate the amount of the tax in value terms, and express that relative to GDP.

Figure 8



Source: International Financial Statistics

Not all of the debt was inappropriate. About 20% of the debt was long-term, some of which had been invested in high return projects. Among the successful projects must be counted the Volta dam. Its purpose was to generate large volumes of cheap electricity to fuel Ghana's industrialization. The principal anchor was an aluminum smelter, but Nkrumah's ambitious industrialization plans anticipated many other uses for the electricity. The dam itself cost the equivalent of over 60% of a year's merchandise export earnings, and was financed in part by Ghana itself (41%), the World Bank (34%), and loans from the US and the UK governments (25%).¹ The presence of the World Bank proved to be an important agent of restraint on

¹ Cost information is from Killick (1978), p. 249.

discretionary action by Ghana, which ensured the effective running of the project while the Bank's conditions remained in force.

Nkrumah's legacy also included a sizable state-owned enterprise sector. The share of value added in the state-owned sector reached one quarter of GDP in the mid 1960s. The share of employment was even higher, largely because some state-owned activities were generating low, and in some case even negative value added -- i.e., a value of output less than the value of purchased inputs. Killick (1978) reports several measures of relative inefficiency of the state-owned enterprises, which indicate low productivity, low profitability, and considerable overstaffing.

Exchange Rate Policy

The Nkrumist rhetoric implicitly assumed that all demand and supply elasticities were close to zero, and hence that relative prices did not matter. Consequently, there was virtually no policy attention paid to relative prices in general, and to the exchange rate in particular. The neglect of exchange rate policy may be seen clearly in Figure 9.

From 1956 through 1960 there was a modest fall in the real price of foreign exchange (real appreciation of the currency), as excess demand was being met by drawing down foreign exchange reserves, keeping Ghana's inflation only slightly greater than that of the major industrial countries. With the tightening of exchange controls and import licencing in 1961, Ghanaian inflation accelerated, while the exchange rate remained fixed. This yielded a sharp real appreciation of the currency.

The changes in incentives due to real appreciation of the currency were substantial. On the export side, even before allowing for increases in taxes on various exports, by 1965 the real exchange rate was nearly 50% less than at independence. The response of exports was predictable: exports dropped from about 30% of GDP at independence to less than 18% in 1965 (Figure 9). The fact that a part of this effect was due to terms of trade deterioration may have obscured the importance of the real exchange rate for export earnings. Whatever the reason for the failure of policy makers to recognize the source of the problem, the deteriorating export performance was serious. (See also Leith 1971.)

Equally important incentive effects were emerging on the import side. With the volume and composition of imports controlled by a system of import licencing, large rents attributable to those licences emerged. Ghanaians learned quickly that rent-seeking had become far more rewarding than any directly productive activity. Sometimes the rent-seeking consisted simply of investing in favored import-substitution activities, where inputs could be imported cheaply and competing imports were excluded. More seriously for the long-term, the rent-seeking also took the form of corruption, a pattern which was to be repeated again and again.

Figure 9



Source: International Financial Statistics

The exchange rate-cum-import licencing policy contributed to the fiscal deterioration, which was itself causing the real exchange rate deterioration. With the volume of imports/GDP dropping (because the export/GDP ratio was falling and no further financing was available), and because the composition of imports was increasingly biased towards low duty rated items which were

deemed “essentials” and therefore worthy of lower rates, import duties started to shrink, not only relative to GDP, but also relative to other government revenue sources.

Cocoa Policy

Nkrumah's government had a highly ambivalent attitude towards cocoa. The peasant farmers, responsible for the vast bulk of production, were not part of the urban-based statist constituency that had put, and kept, Nkrumah in office. The world market was largely dominated by multi-nationals, which Nkrumah deeply mistrusted, and the world price exhibited a high variance. Government, therefore, had many reasons to ignore the cocoa interests in its policy formulation. Yet in 1957 cocoa exports were both the most important export and the largest single source of government revenues. Government could not, therefore, afford to mis-play its cocoa policy: but it did.

The peasant farmers are located in several parts of the country, but largely in the inland regions beyond the costal plain: Ashanti, Brong-Ahafo, Eastern, and Western regions, with smaller volumes coming from Central and Volta regions, but not from the north. Cocoa is a tree crop, which takes a number of years to mature. The pods are harvested, and preliminary processing in the form of fermentation and drying of the beans, is done in the immediate growing area. The dried beans are generally carried in headloads from the farm to the buying stations located on a feeder road or rail line, where a producer price that varies by grade but which is usually fixed for the crop year, is credited to the owner.¹ From there the beans are shipped to the coast, and then overseas, with some diverted to local processing.

At the turn of the century Ghana accounted for about 1% of total world production of cocoa beans. Following a rapid expansion of production during the first two decades of the twentieth century, Ghana became the largest single producer in the world. The 1920/21 crop year gave Ghana a 32% share, which grew slightly over the next two decades, and remained in the mid-30% range until the early 1960s. (See Amoah, Vols. 1, 1995, and 2, 1998, for detail on the cocoa sector.)

¹ In different times the payment was made in currency and at other times by cheque. In either case, as a recipient of a large annual cash payment the producer was particularly vulnerable to the inflation tax.

The internal purchasing and external marketing of cocoa were handled by private firms prior to World War II. With the war, the colonial government took over the purchase of cocoa and sold it to the British food ministry. In 1947 this was replaced by the Cocoa Marketing Board (CMB), which was given a monopsony position in purchase for export and monopoly in export marketing from the Gold Coast.¹ Initially the producer price paid by the CMB was determined by the world price less a modest tax, with profits paid to government. However, as time passed, the nominal producer price was fixed and kept at levels that yielded larger and larger shares to the CMB and government.

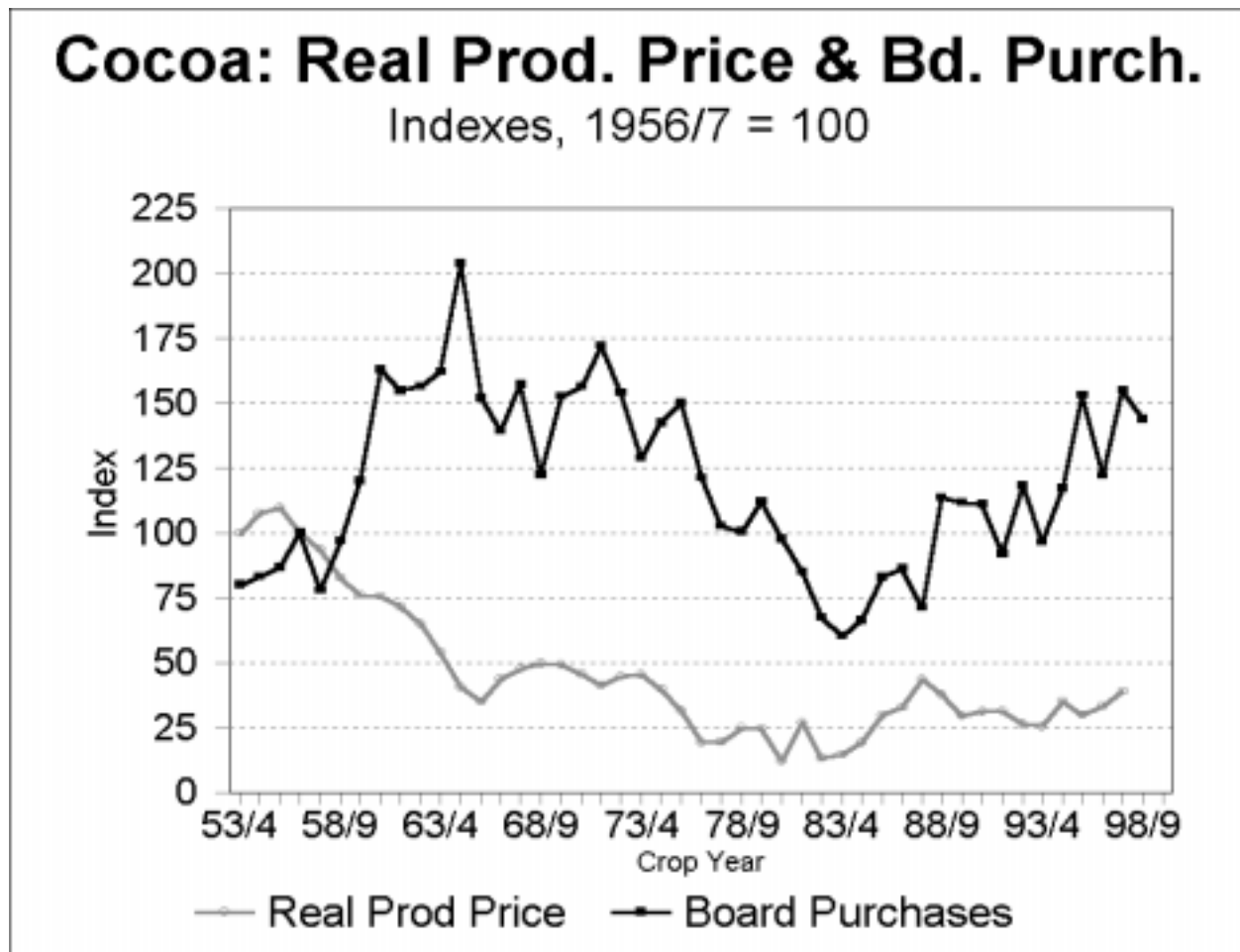
As Nkrumah took the reins of the internal self-government in the early 1950s, the world price was high by historical standards, due largely to the commodity price boom associated with the Korean war. This permitted government, through the CMB, to set a relatively high producer price, which encouraged a substantial expansion of Ghanaian capacity in the form of new plantings of trees. As independence neared, world prices dropped, and so did the price paid by the CMB to producers. However, once trees have been planted, the short-run supply response to a real price fall is not large.² Consequently, sales to the CMB grew dramatically, doubling from the early 1950s to the early 1960s, even as the real price paid to producers was falling, equally dramatically (Figure 10). Much to the dismay of Nkrumah, this also depressed world cocoa prices, for at that time Ghana had about one third of the world market. (See Figure 11.)

Again, the interaction of the excess demand and the exchange rate policies acted to amplify the effect of another set of policies. In the cocoa case, the domestic inflation and the fixed nominal producer price accelerated the decline in the real producer price. The effect on production, and hence CMB purchases, was not immediate but, nevertheless, during Nkrumah's later years purchases began their long decline, both in absolute volume, and share of world production. (Figure 11).

¹ The formal title of the Board changed over the years, and is now called the Cocoa Board. It was not until 1961 that the Nkrumah government established it as a single monopsony buyer at the local level.

² It should be noted, nevertheless, that over the longer term, as smuggling channels to neighboring countries developed, sales to the CMB began to decline more rapidly than the harvest of cocoa pods.

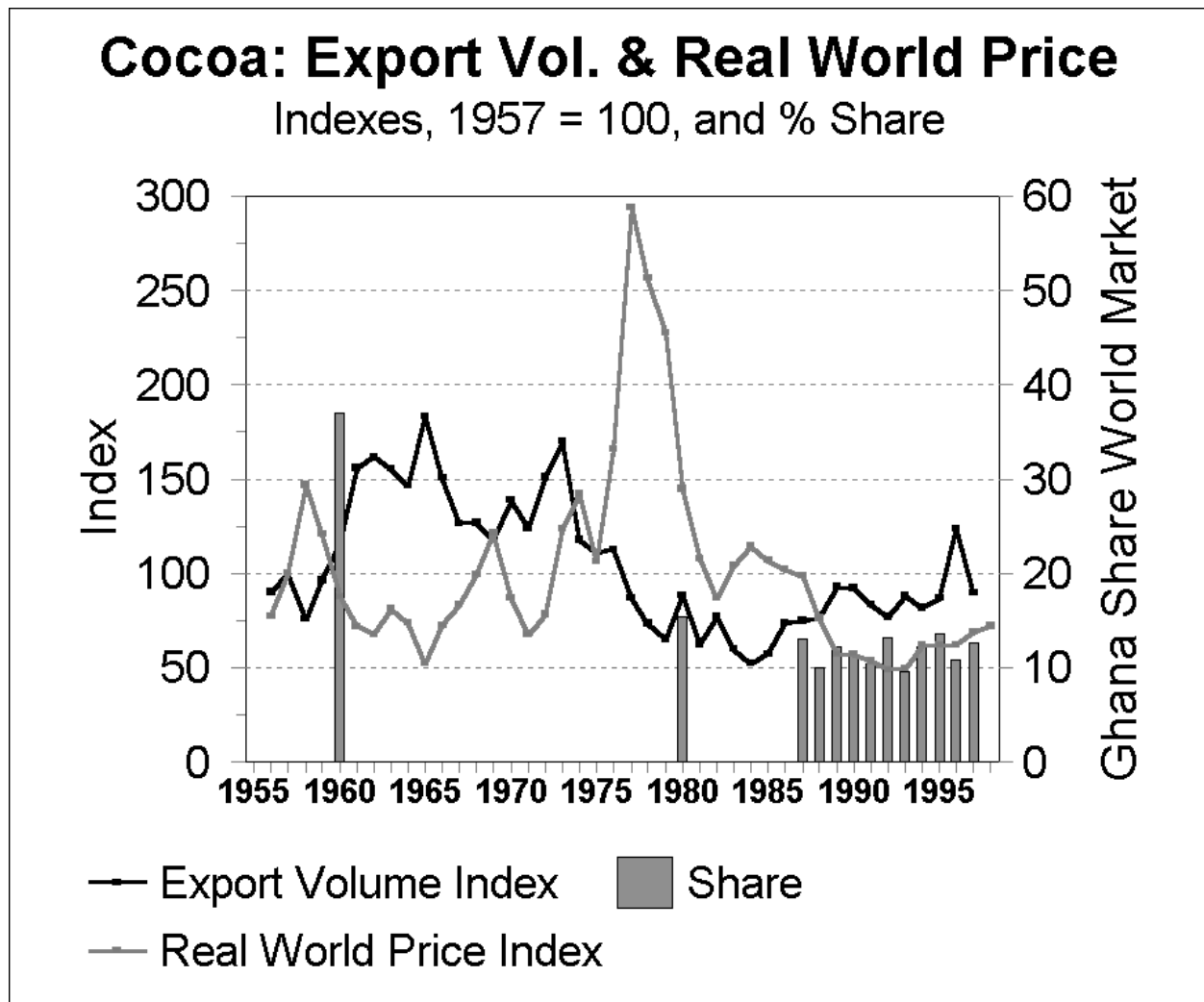
Figure 10



Source: Cocoa Board, Accra

In addition, Ghana negotiated several bilateral trade pacts, mostly with other African and east-European countries. This helped Ghana to diversify modestly its cocoa export market, but mostly it simply created bilateral balances which Ghana found of little value in making its other external payments. The USSR got the cocoa, and Ghana got a ruble balance.

Figure 11



Sources: Amoah (1998) for share, International Financial Statistics for other.

The Nkrumah Legacy

The Nkrumah regime initiated the first failure – to maintain macro balance – and exacerbated the effects by fixing the nominal prices of foreign exchange and cocoa. The returns to holders of money, and export-earning assets such as cocoa trees and mineral deposits were thus altered dramatically by the state. Even if those returns were subsequently restored to their initial rates, the response would be tempered by the knowledge of the risks which experience had demonstrated.

The National Liberation Council

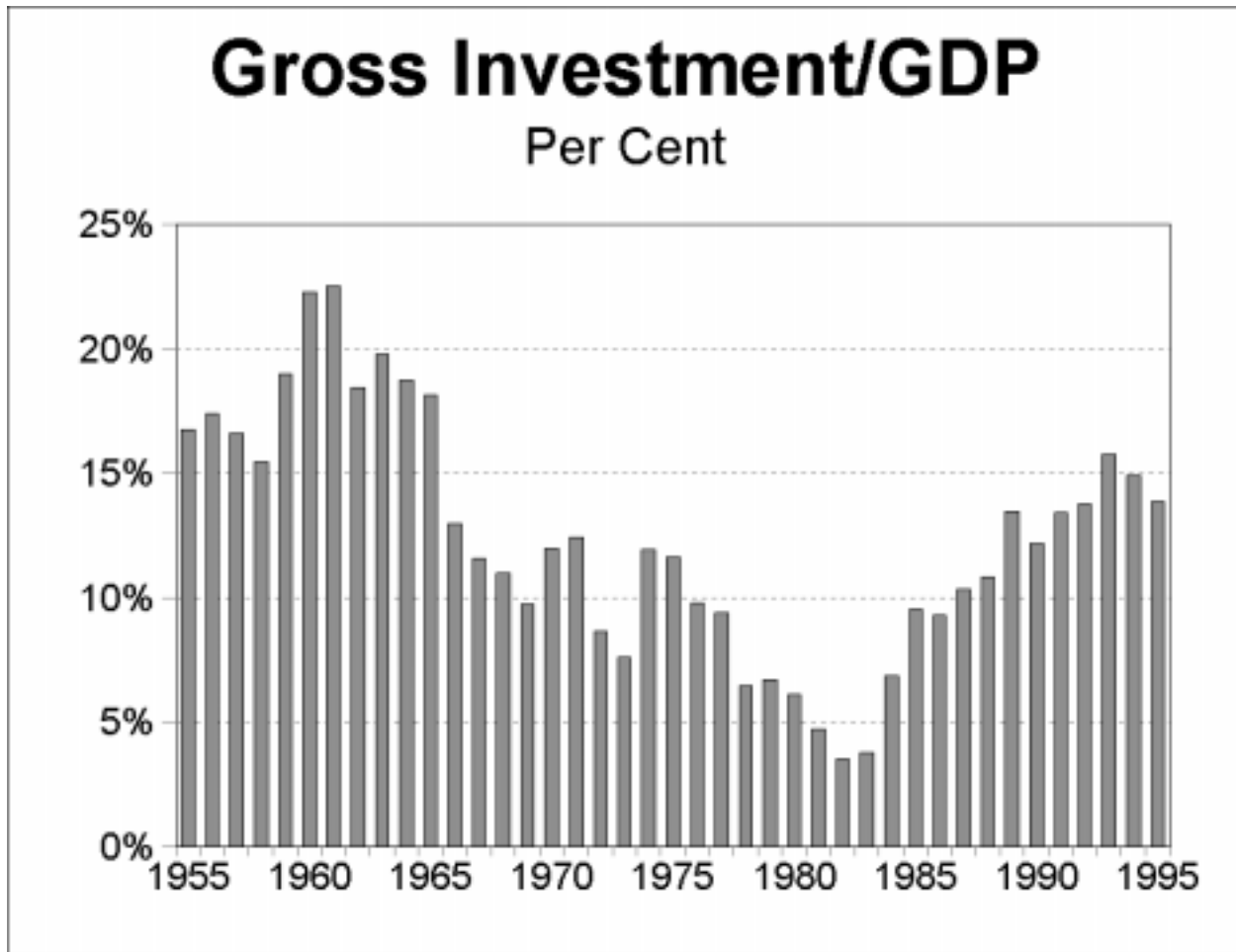
The leaders of the coup that ousted Nkrumah in early 1966 installed a government called the National Liberation Council (NLC) which was heavily dominated by military officers. Several justifications for the coup were offered, including the oppression of political critics, the corruption of government officials, and economic mismanagement. The political system developed by Nkrumah was dismantled, and a commission of enquiry into corruption was launched.

The most pressing economic problem facing the NLC on taking over from Nkrumah was the balance of payments, for the foreign exchange reserves were slipping rapidly, in spite of continued use of import-licencing and exchange controls. By the end of 1966 net foreign assets in the monetary system were negative. Yet there was little recognition of the fact that the balance of payments pressure arose fundamentally from excess demand due to loose fiscal and monetary policies. Rather, the NLC blamed the problems facing the Ghanaian economy on the poor management and corruption of the Nkrumah government. Government appeared to believe that it was possible to construct a more equitable and carefully managed control system.

Fiscal and Monetary Policy

The NLC did cut total government spending in its first year (Figure 2), but this was largely the product of slashing the capital budget, contributing to a marked decline in the gross investment to GDP ratio throughout the NLC period (Figure 12). The NLC was able to negotiate a major rescheduling of short-term debt, thus providing some immediate relief of both government's budgetary problems and pressure on the balance of international payments. Government revenue also fell under the NLC, allowing the overall government budget deficit, to continue to run in excess of 5% of GDP until 1969 when the deficit was reduced to 3.3 % of GDP. Some monetary policy restraint was introduced, with the discount rate bumped from 4.5% to 7% in 1966. This sharply reduced the rate of growth of the money supply, which contributed to a reduction of inflation.

Figure 12



Source: International Financial Statistics

The NLC was also the beneficiary of a considerable dose of good luck. Excellent weather produced good food crops in 1966 and 1967, contributing to an absolute reduction in the CPI for the latter year¹ while the GDP deflator inflation was modestly positive.

Exchange Rate

It was soon clear, however, that a more drastic measure than modestly tighter fiscal and monetary policies would be required -- devaluation. With a fixed nominal exchange rate, the cumulative

¹ The food component of the CPI had a weight of more than 50%. The fall in the recorded index may also have been attributable to the NLC's more vigorous enforcement of the price control regulations.

inflation of the Nkrumah era had generated a significant real appreciation of the currency vis-a-vis the major industrial countries. By 1966 the real price of foreign exchange had fallen to 50% of the level at independence. This was having serious consequences for Ghana's export competitiveness, which in turn substantially depressed the share of exports in GDP (Figure 9). Further, foreign exchange reserves had continued to slide, and private foreign investment was increasingly concerned about the exchange rate risk.

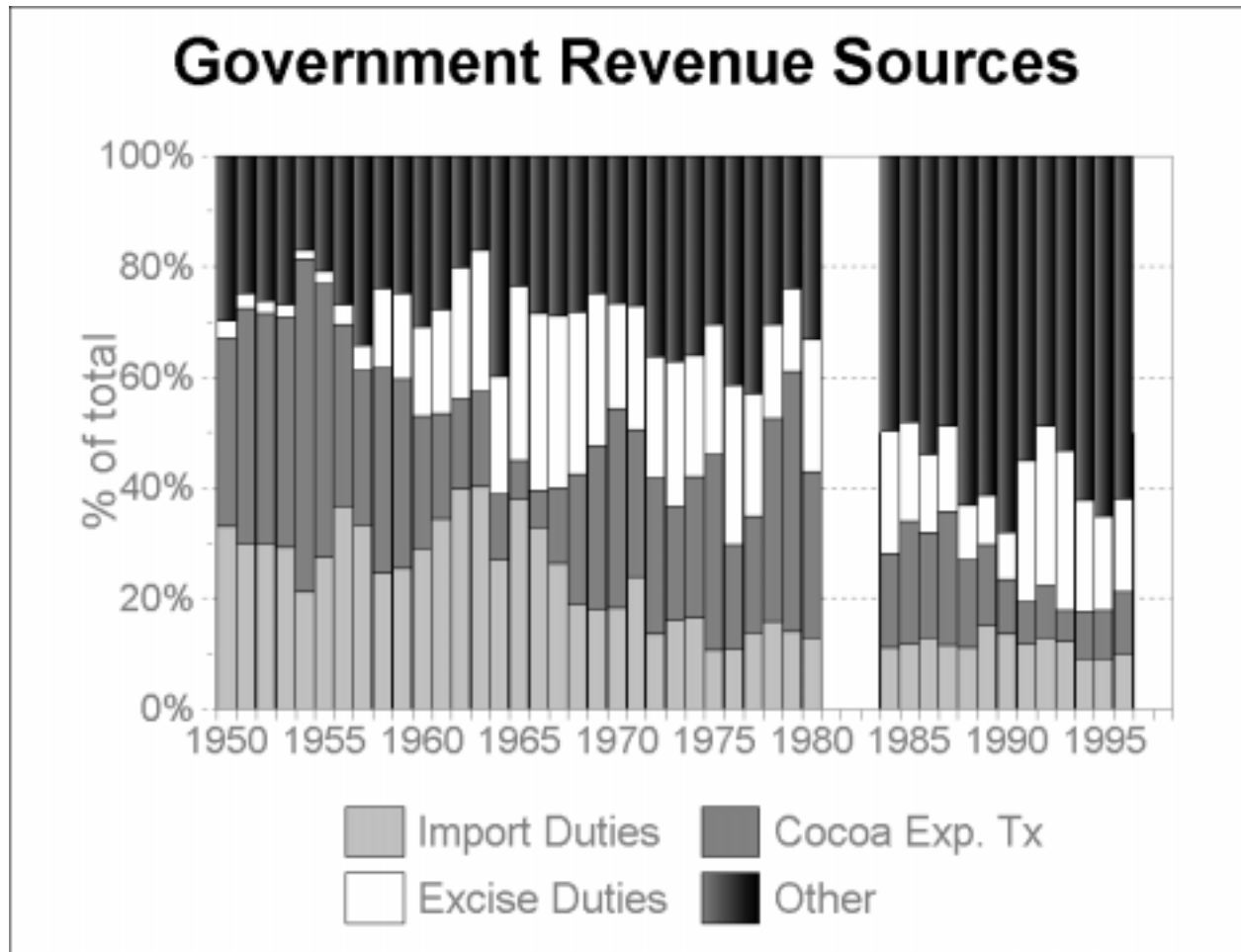
In July 1967 the NLC finally decided to devalue. The official price of foreign exchange was increased by about 43%. This, of course, was not enough to restore the real foreign exchange price to the level of 1957: the average real exchange rate index for the following year was 75, compared with the previous year of 50 (1957 = 100). But the devaluation was sufficient to reverse the trend of exports relative to GDP, and to temporarily stop the decline of foreign exchange reserves.

The devaluation package also included an increase in the fixed nominal producer price of cocoa, and modest increases in the minimum wage (7.7%) and government wages (5%), plus a commitment to liberalize import controls. This did in fact occur, as the ratio of imports to GDP edged up.

Cocoa

The increase in the producer price of cocoa, announced as part of the devaluation package, was 30%, in contrast with the rise in the official price of foreign exchange of 43%. This was far from sufficient to reverse the cumulative effect of many years of keeping the nominal increase in the producer price of cocoa less than the inflation rate. Indeed, by not matching the devaluation, government was, once again, taking a larger slice of the cocoa pie, and increasing its dependence on cocoa revenue (Figures 10 and 13).

Figure 13



Source: Quarterly Digest of Statistics, Statistical Service, Accra

The NLC was also blessed by a major recovery of world cocoa prices, which had reached a trough in 1965. The following year, the NLC's first in power, world cocoa prices in real terms increased by 38%, and a further 15% , 19%, and 22% (compounded) in each of the subsequent years. The real price of cocoa in world markets for 1969, the year the NLC turned over power to the elected Busia government, was significantly more than twice what it had been in 1965 (Figure 11).

Debt

At independence, Ghana had foreign exchange reserves of around \$500 million while the external debt was virtually non-existent. By the end of Nkrumah's rule this situation had changed

dramatically. Reserves were nearly depleted and the external debt amounted to an estimated \$790 million. (Leith, 1974, p. 29 converted at £1.02/\$). As noted, lavish government expenditure and declining revenues in combination with an increasingly overvalued currency were mainly to blame for this development. A certain amount of credit pushing also took place, supported by export promoting agencies in the creditors' countries (Hardy, 1982). Poor use of foreign capital, compounded by excessive reliance on medium term financing – primarily suppliers credit – aggravated the difficulties in servicing the debt and put severe pressure on the balance of payments. Shortly after the NLC government took power, a major rescheduling of Ghana's debt was negotiated in 1966. This provided some temporary relief of both government's budgetary problems and pressure on the balance of international payments. Two more reschedulings took place in 1968 and 1970. By the end of 1971, the debt had been pared back to US\$542.

The NLC Legacy

The National Liberation Council returned Ghana to democratic rule in 1969, but first carefully set the stage. The new constitution re-established the position of Prime Minister as executive head of government, while the role of President as head of state was more ceremonial.

The NLC had restored macroeconomic balance and some of the incentive to export, both of which were important for future economic growth. Yet in the very act of the coup overthrowing Nkrumah, the military created a dangerous precedent – that the power of the state could be usurped on the decision of a few, however high-minded those few might be. In the hands of the NLC that power did not prove damaging to economic growth, but the precedent would prove to be.

The Busia Government

Elections in August 1969 were won with a substantial majority by the Progress Party, led by K.A. Busia, with 59% of the votes and 75% of the seats. Busia's Progress Party government took office in October 1969, with great expectations for the restoration of a democratic system of government. The overall economic record is mixed. Real GDP per capita continued the growth that had resumed under the NLC. The Busia government was highly critical of the economic management under Nkrumah, but there was not a comprehensive attempt to reverse the changes that had been wrought by Nkrumah. Once again the confusion between poor policy and poor administration as the source of economic troubles was evident.

Support for the Progress Party was centered primarily in the predominantly Akan-speaking regions which were also the principal cocoa growing areas. (See Austin 1976.) Indeed, at one time Busia had been active in the campaign for Ashanti secession. The opposition National Alliance of Liberals (NAL), was led by K.A. Gbedemah, an Ewe from the Volta Region, and a one-time lieutenant of Nkrumah who had later fled in the face of Nkrumah's suppression of all dissent.

The government of Prime Minister Busia initiated some economic reforms, and modest economic growth ensued. However, there were two major problems. First the contest over the political system had not yet been resolved. Second, the Busia government mishandled the import liberalization.

The fragility of the political system, not entirely appreciated at the time, was illustrated by a number of early actions of the new government. The constituent assembly had included a clause in the constitution barring criminals from office. The clause was written in such a way that it could be applied to Gbedemah, who had been found by one of Nkrumah's enquires unable to account for a small portion of his assets. Shortly after Gbedemah won his seat in the election, his local opponent successfully launched legal action to unseat him. In a similar vein the government moved in early 1970 to dismiss 568 public officers, most of whom were seen as having been supporters of the opposition, and not one of whom was Akan.

The precarious political balance was also reflected in the Busia government's expulsion of large numbers of aliens in late 1969. (See Austin 1976.) These were seen as depriving Ghanaians of jobs, and were easy targets for a government seeking popular support early in its mandate.

Fiscal and Monetary Policies

The Progress Party committed to a gradual elimination of import licencing. To this end, the first budget (August 1970) introduced a considerable liberalization of the list of items subject to licencing, complemented by a differentiated scheme of surcharges on those imports not subject to licencing. Further revisions to the details of the surcharges were made during 1971, with the effect of increasing marginally the share of import duties in government revenues. Yet the necessary condition for success in this venture -- an appropriate level of aggregate demand -- was not enforced. The government budget deficit continued, albeit somewhat reduced in 1970, but returning to 1969's rate in 1971.

Monetary policy, as indicated by the discount rate, which had been eased somewhat under the later years of the NLC, remained passive, continuing to yield a negative real interest rate. The major impact on the monetary front was a further reduction of credit to government (relative to GDP) that had begun under the NLC, while credit to the private sector grew rapidly in 1971.

State owned enterprises (SOEs), that had been built up by Nkrumah, had not been dismantled by the NLC.¹ The Busia government attempted some minor changes, but chose not to withdraw government from the "commanding heights" of the economy. Thus, the SOEs continued to be a drain on both the fiscus and productivity. Killick (1978, p. 219) reports data from the Auditor General's *Annual Reports* indicating losses incurred by various enterprises amounting to over £15 million in 1969-70, including a £6.75 million loss for the State Gold Mining Corporation and £2.85 million for Ghana Airways.² He also shows substantially lower productivity in state-owned enterprises. More seriously for the future, the Busia government's choice to retain a large number of state-owned enterprises created a considerable opportunity for the distribution of rents in the

¹ A few SOEs were divested in 1966/67, but allegations of impropriety in the divestiture process remain to this day.

² To provide some perspective, government revenue in 1969 was £332million, and the value of gross output for the metal mining sector (which included bauxite and manganese mines as well as a substantial private gold mine) was £37.2 million.

political process, which plagued the economy in the next decade, and which would subsequently form a significant drag in the reform program.

The 1971 budget of the PP government contained a response to the increasingly negative real interest rates afflicting the financial system. Nominal interest rates were increased, but in doing so the authorities continued the practice of regulating the interest rates that banks were to pay on their deposits and charge on loans. Further, the spread between deposit and lending rates was narrowed. This meant that the banks were caught in a bind between higher deposit rates and regulated loan rates, forcing them to ration credit on some other basis. The Bank of Ghana's discount rate was also raised from 5.5% to 8%, but this still did not make the real rate facing the commercial banks positive.

With no substantial tightening of either fiscal or monetary policy, the overall excess demand pressure was not alleviated. This put in jeopardy the government's liberalization of the import licencing and exchange control regime, as foreign exchange reserves were falling, once again to record low levels.

Cocoa

Despite the fact that the Busia government's support came largely from regions of the country where most of the cocoa was grown, the producer price of cocoa for the 1969/70 crop year was not increased in real terms. At the same time, good weather yielded a good harvest and, crucially for the balance of payments, world cocoa prices in 1969 continued to recover from the trough of 1965.

But the cocoa boom did not endure, and the liberalization of import licencing which was predicated on the continuation of strong cocoa export earnings was not, therefore, sustainable. In the absence of a substantial tightening of aggregate demand, the liberalization would have been manageable only if world cocoa prices had remained at the 1969 peak. World prices fell during 1970, and again during 1971, leaving the real price for 1971 roughly half that of 1969 and export earnings for 1971, about \$100 million short. (See Leith 1974, p148.) This was not trivial, for it

amounted to more than 25% of the previous year's imports. Nevertheless, the budget presented to Parliament in July 1971 continued with the import liberalization process.¹

Exchange Rate

The task of dismantling the foreign exchange control system proved difficult. Liberalization of the import licencing had begun following the 1967 devaluation, but taxes on imports were not increased enough to compensate for the removal of licences. Further, aggregate demand pressure was not constrained. Consequently, from 1969 to 1971, when export earnings declined marginally, imports grew by 14%. Foreign exchange reserves fell to dangerously low levels. Something more than the timid fiscal and monetary restraint was clearly required in order to restore some semblance of external balance. In an effort to solve both its balance of payments problem and its fiscal deficit problem, the Busia government decided on a very substantial devaluation from ₵1.02 per US dollar to ₵1.82 per US dollar, which was announced on December 27, 1971. Since the US dollar had just been devalued by about 8% the week before as part of the Smithsonian Agreement, the cumulative devaluation was almost a doubling of the price of non-dollar currencies. (See Leith 1974.)

The package included abolition of several complicated surcharges on foreign exchange payments and bonuses for non-traditional foreign exchange earners. In addition, the nominal producer prices of cocoa, and other crops handled by the CMB, were increased by 25%, much less than the increase in the price of foreign exchange. Since the cocoa export tax was steeply progressive in nominal cedi terms, and since the government's expenditure budget was already set in nominal cedi terms, the combination would have significantly reduced the fiscal deficit.

For those with incomes fixed in cedis, but with heavy expenditures on imports, which included the military, a devaluation of this magnitude meant a huge cut in real income. On January 13, 1972 Ghana experienced another military coup.

¹ The liberalization process was, however, becoming increasingly complex. For details, see Leith 1974.

The Busia Legacy

The attempt by the Busia government to restore both macroeconomic balance and the incentive to export could have set Ghana on a sustainable long-run growth path. Yet the attempt to obviate that failure triggered an even more pernicious failure – the use of the state for the interests of the few.

The National Redemption Council/Supreme Military Council

Military officers the world over are not renowned for their grasp of the fundamentals of fiscal, monetary and exchange rate policy. Colonel Acheampong, the leader of the coup, and his colleagues were no exception to this rule. Calling themselves the National Redemption Council (NRC), they proceeded to focus on an agenda that ignored even the most elementary economic constraints on their ambitions.

Among its first acts, the NRC decreed: a *revaluation* of the Cedi; a return of control prices to their pre-devaluation levels; a refusal to pay “unjust” foreign loans that had been taken out by previous civilian governments; and a fourfold increase in the minimum wage. The early NRC also launched with great fanfare “Operation Feed Yourself,” to achieve national food self-sufficiency.

The NRC government evidently believed that an economy could be run in the same way as the military -- by command rather than by incentive. In the early days this may have been simply naivete, but as time passed, evidence mounted that implementation of the various decrees was not happening. (See Chazan 1983.)

Under the NRC, the economy entered what turned out to be an extended period of considerable instability, directly exacerbated by growth-retarding policies, and indirectly by acute corruption. The full magnitude of the destructive policies was masked initially by an exceptional set of circumstances in the world cocoa and gold markets. Ghana's cocoa export volume expanded to the second highest level in the post World War II period, while the world cocoa price also increased, contrary to the usually negative relationship between Ghana's export volume and world price. As a result, cocoa export earnings in 1972 and 1973 boomed. Furthermore, another major export, gold, was affected by an equally exceptional combination of events: the additional devaluation of the US dollar in early 1973, and the freeing of the price of gold, which led to a two-thirds increase in the dollar price of gold in 1973 and a further increase of nearly the same proportion in 1974. These windfalls kept inflation under reasonable control in 1972 and 1973, and saw Ghanaians enjoying the highest real per capita GDP in 1973 and 1974 that they have ever seen, before or since. (See Figures 1 and 3.)

Exchange Rate

Having seized power on the basis of the Busia government's devaluation, the NRC immediately decided to revalue the Cedi, from $\text{¢}1.82/\text{\$}$ to $\text{¢}1.28/\text{\$}$. The nominal exchange rate became a matter of national pride for the NRC. Regardless of the amount of inflation, regardless of the adverse economic consequences for the nation, and heedless even of its own narrow interests, the NRC persistently refused to contemplate any devaluation of the Cedi. Even when the US dollar was devalued in February 1973, the Cedi did not follow suit, and consequently appreciated further to $\text{¢}1.15/\text{\$}$.

Yet the exchange rate became the root of its problems. With a fixed exchange rate and accelerating inflation, exports became increasingly uncompetitive, while the excess demand for imports continued to mount. (See Figure 9.) Volumes of both cocoa and non-cocoa exports fell precipitously. With less foreign exchange available for imports, the import licence premia and the corruption associated with the system mounted.

It was not until 1978 that there was any further movement of the nominal exchange rate. In June of that year "a more flexible exchange rate system," under which "the exchange rate of the Cedi against the US dollar would be adjusted to reflect the underlying economic, financial, and balance of payments situation" was authorized. (IMF, *AREA* 1979, p. 177.) In June there was a 17.4% depreciation, a further 8.1% in July, and 15.8% during August. Compared with the cumulative inflation which had occurred over the years, the change was trivial.

Cocoa

The NRC government may have been lulled into a false sense of confidence by developments in the cocoa market. Just as the previous military government had benefitted from a windfall in the world cocoa market, so too did the NRC. In its first two years, both the world price and Ghana's export volume increased. In 1974 cocoa export earnings in dollar terms exceeded the previous peak of 1970. This permitted the government to increase the nominal producer price in each of 1972 and 1973 by more than the CPI inflation. But the gap between the producer price and the world price remained substantial.

Monetary and Fiscal Policies

The underlying economic fundamentals were deteriorating. Budgetary limits on government expenditures were often ignored, and various revenue raising measures were introduced but not enforced. The budget deficit grew year after year, by 1976 reaching a record level of over 11% of GDP. This was financed almost entirely from the domestic monetary system, and not by international borrowing. The rapidly accelerating money growth did the same to inflation, pushing CPI inflation to over 100% in 1977 (Figures 3 and 5).

In the face of that inflation, regulated nominal interest rates and exchange rates were kept fixed at levels that bore no relationship to their true scarcity value. Both the real interest rate and the real exchange rate plummeted. (Figures 7 and 9). Thus, those with favored access to credit (via either the state-owned Ghana Commercial Bank or one of the specific government loan windows) and/or imports (via the licencing system) could make fortunes simply on the basis of their favored access, rather than from any directly productive activity.

Inflation, while caused in the first place by the government budget deficit, given the other economic policies, contributed to a deterioration of government's own revenue base. Real import duty collections dropped as the volume and local currency value of imports declined due to the lack of foreign exchange at the fixed nominal exchange rate, and as goods were increasingly (mis)classified as low or duty free. Delays in collecting taxes became more pronounced and costly in terms of real revenue foregone as inflation surged. By 1978 government revenue amounted to a mere 7% of GDP. The increasing reliance on the inflation tax ate into the tax base – holdings of currency and demand deposits. After peaking at 22% of GDP in 1976, money holdings began to slide perceptibly as the public sought out and found other means to carry out transactions and store value, such as barter and the use of foreign currencies (Figure 8).

With ever shrinking sources of funding, government expenditures also shrank (Figure 2). Gross investment, which in the early years of independence had exceeded 20% of GDP, fell to about 5% of GDP in 1979. (See Figure 12.) Both private and public investment lagged behind even replacement rates, and routine maintenance lapsed, making the true depreciation even greater than the reported depreciation of the capital stock. Symptomatic of the deteriorating situation was the impairment of government's ability to carry out even the most elementary functions. Roads, schools, communications, and health facilities ceased to function in many parts of the country.

The political fundamentals also worsened. The NRC had been designed as an alliance of the military and bureaucracy, cutting out the politicians. The excising of the easily identified politicians did not, however, eliminate internal opposition. Further, the leadership of the NRC became increasingly arrogant and intolerant of any opposition. For example, J.H. Mensah, Busia's Minister of Finance, who had been detained following the coup, was re-arrested in September 1975 for circulating a pamphlet critical of the NRC's economic policies. He was sentenced to 8 years in prison at hard labor.¹

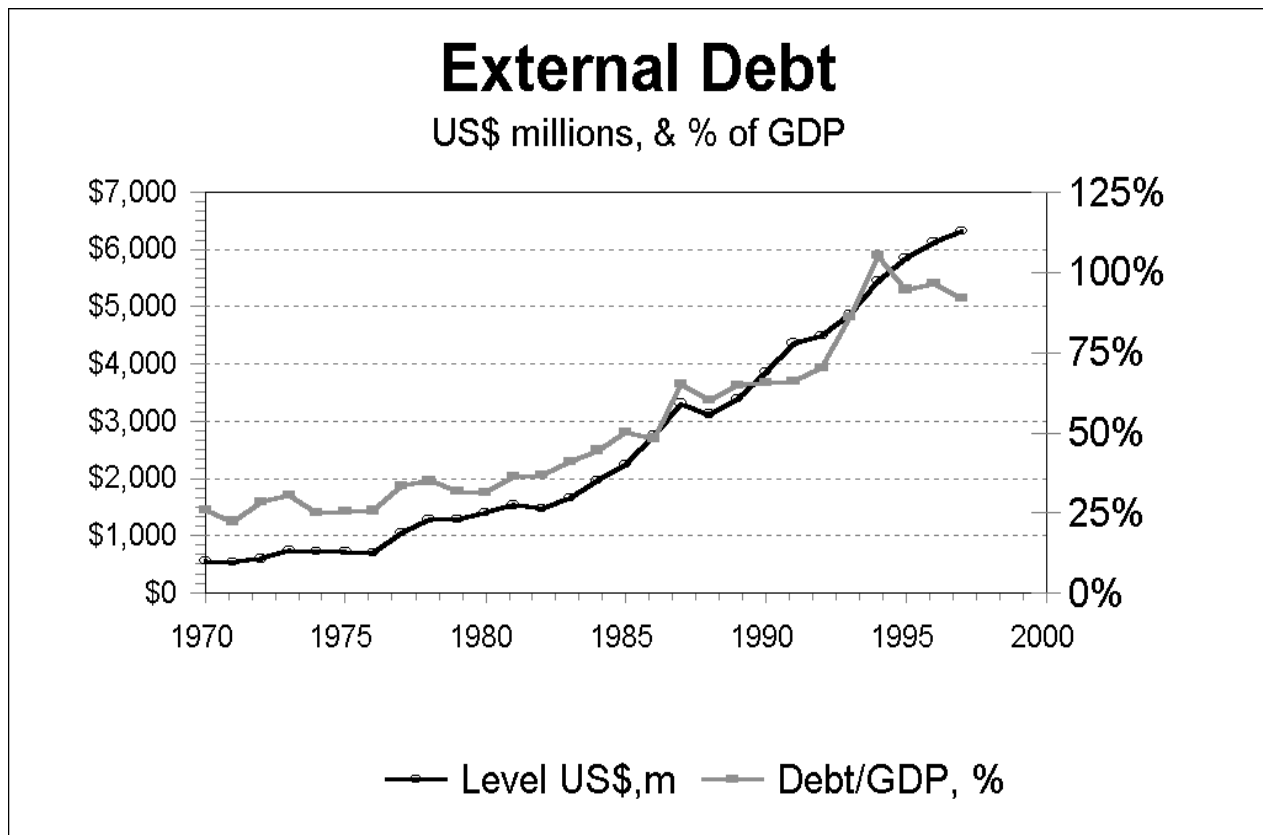
The military's solution to the problem of the deteriorating economic and political situation was to remove the non-military participants in the NRC, creating instead the Supreme Military Council (SMC).

Debt

In keeping with the theme of self reliance promulgated by Acheampong on taking power, the early NRC/SMC did not add to Ghana's foreign debt. However, the NRC government's debt servicing capacity deteriorated and it became clear that Ghana would not be able to honor its rescheduled pre-1966 supplier's credits, in addition to the regular debt service, when they were to fall due. Hence, in 1974, the Paris Club took the, then highly unusual, decision to include a substantial grant element by allowing Ghana to repay its entire previously consolidated debt over a 28 year period, including an 11 year grant period at a 2.5 percent moratorium interest rate. According to Hardy (1982), the financial effect of the rescheduling was equivalent to a 45 percent write-off of Ghana's nominal debt. While generous for the time, the rescheduling of the debt had no effect on either the nominal exchange rate or the internal policies of the regime, thus allowing the currency to become ever more overvalued. It did mean, however, that Ghana, in contrast with many developing countries that had taken on enormous debt loads to cushion the shock of the OPEC oil price increase, did not increase its debt. At the end of 1976 Ghana's debt was still less than at the overthrow of Nkrumah a decade earlier (Figure 14).

¹ See Amnesty International, *Annual Report*, 1975-76. Mensah and his co-accused were released on appeal in June 1978 (Amnesty International, *Annual Report*, 1977-78).

Figure 14



Source: World Development Indicators.

Rent-Seeking

The architecture of the economic system, including exchange control, import licencing, and a large state-owned enterprise sector, was fundamentally unchanged from the one built by Nkrumah, for it was never fully dismantled by the NLC and Busia governments. Indeed, in December 1972 the NRC government acquired by decree a 55% equity participation in foreign owned mining and timber companies operating in Ghana, thereby extending the role of the state in the economy. This was followed by nationalization of Ashanti Goldfields, the Volta Aluminium Company, and a requirement that the majority of commercial bank shares be held by Ghanaians. These were summed up in an “Indigenization Decree” in 1976. (See Chazan 1983.)

While the NRC/SMC government was proceeding as if it could ignore incentives and run the economy by command, the military officers were themselves rapidly responding to the incentives

created by the economic system. The most important feature of the system was the enormous discretionary economic clout it placed in the hands of officials, now mostly military officers. Valuable rights could be acquired for far less than their true market value, and resold, thus generating significant rents for the owner of the right. Those rents, in turn, were used both for personal enrichment and to purchase political support for the regime. Rent creation and distribution became the central feature of the NRC/SMC government.

As with Nkrumah, no attempt was made to deal with the fundamental sources of the economic problems facing the nation. What was different about the NRC/SMC government, compared with Nkrumah's, was the extreme to which it pushed all the deleterious economic policies. The rent-seeking thus generated was not simply a benign transfer of income to those in positions of power. It was both a waste of resources, and a corrosive force within Ghanaian society. An ever-widening circle of corruption displayed its venality for all to see, coercing more and more individuals into participation as the price of survival. In the face of the increasingly hopeless situation, Ghanaians sought out exit options. Those with internationally marketable human capital emigrated. Those whose only option was to return to the land did so in a desperate bid to ensure that they would at least be able to feed themselves.

General Akuffo

The political and economic direction of the SMC changed slightly in June 1978 when General Akuffo forced General Acheampong to step aside, in the face of growing public unrest. The new leader was evidently somewhat more willing to contemplate hitherto unthinkable policies. He immediately ordered the release of fifty people, including senior members of the Busia and Nkrumah governments, who had been detained in April for contesting the results of a referendum held on a possible future form of government.

Following the first tentative steps towards a more "flexible" exchange rate policy begun in June, at the end of August a substantial formal devaluation of the Cedi from $\text{¢}1.69/\text{\$}$ to $\text{¢}2.75/\text{\$}$ was taken. While the cumulative change from June through to the end of August was the largest devaluation ever undertaken to date by Ghana, the 139% increase in the price of foreign exchange did little more than offset the previous year's CPI inflation, and did nothing to restore the real exchange rate to an appropriate level (Figure 9). The nominal discount rate was also raised, but similarly by not nearly enough to do what was necessary: the real discount rate remained below minus 30% (Figure 7).

Akuffo was rather more willing to take on external debt than Acheampong. By the end of 1979 the debt had almost doubled, reaching US\$1.3 billion.

Akuffo did not put an end to arbitrary economic interventions, however. Large volumes of Cedi banknotes had been smuggled out of the country to be exchanged in black markets in neighboring countries, and more Cedi banknotes were being held outside banks. As a crude measure to reduce the money supply and to tackle the externally held currency, in March 1979 a mandatory exchange of old for new was carried out. Holdings of up to ₵5,000 received 70% of their funds, and larger holdings only 50%. Needless to say, such a measure was especially hard on peasant farmers who received cash payments for their annual crops.

These measures did succeed in bringing down the money supply growth rate, and reduced the real budget deficit the following year. But the fundamental problems of excess demand and regulated prices of many key items remained. In other words, nothing fundamental was changed, including the colossal corruption.

The political unrest continued. Finally General Akuffo put in place a plan to return government to civilian hands, including elections scheduled for June 1979.

The NRC/SMC Legacy

Having taken power in pursuit of its own narrow interest, the military still had an interest in maintaining a sound economy. As Olson (2000) has explained, a “stationary bandit’s” interest is in a prosperous economy because his income is maximized when the national product is. Yet the military failed to act in its own collective long-run interest. It allowed virtually unlimited access to the rents of the control-cum-state-owned-enterprise-regime. The economic policies went well beyond the optimum, shrinking the rent pool. And, as the political agitation grew, the horizon of the military officers became ever shorter. (See Leith and Lofchie 1993.) In brief the state had become a predator.

The First Rawlings Intervention

Extraordinary events in May and June 1979 intruded before the elections were held. Growing unrest, sparked by the generals' attempt to grant themselves immunity from prosecution after they left office, precipitated a mutiny in the lower ranks of the military. Under the leadership of Flight-Lieutenant Jerry Rawlings, a coup was attempted in May 1979. The coup failed, and the leader was put on public trial. (See Yankah, 1986.) During the trial, Rawlings was eloquent in his condemnation of the corruption brought upon the country by his superiors. This inspired a successful mutiny by the lower ranks which then installed Rawlings as head of the Armed Forces Revolutionary Council (AFRC).

The new government committed immediately to proceeding with the elections as scheduled, a scant two weeks later, and to turning over power to the elected government three months later. It honored those commitments, but from early June until late September the AFRC launched a massive anti-corruption campaign that left a permanent imprint on the minds of all Ghanaians. Goods and property allegedly acquired by corrupt means were seized, and alleged speculators and hoarders were beaten or shot. The anti corruption campaign extended to the execution of a number of generals, including the former heads of state Generals Afrifa (who had turned over power to the elected Busia government), Acheampong, and Akuffo. The regime also attacked the symptom of the high prices of essential commodities by burning the central Accra market. Notably, nothing was done to tackle the underlying source of the problem.

The 1979 elections were won by the People's National Party (PNP), with 71 out of 140 seats. The PNP leader, Hilla Limann, had to face a run-off election for President, but won that handily. The PNP, which had links with Nkrumah's CPP, but was less ideological, successfully captured seats in every region of the country. The two largest opposition parties, which between them won 55 seats, both had connections with the PP of Busia. (See Chazan, 1983; and Wiseman, 1990.)

The Limann Government

The inauguration of the Limann government in September 1979 provided some relief from the chaotic rooting out of corruption. However, the government faced a daunting task: to restore the institutions of civil society that had been set aside during more than seven years of increasingly corrupt and autocratic military rule; to rejuvenate an economy that was collapsing; and to do this with Rawlings watching from the wings. The government was clearly not up to the task. It did nothing about the exchange rate or the abysmal state of infrastructure, both of which were necessary for a successful resuscitation of agriculture. It dithered about taking IMF and World Bank loans with the associated conditions. Inflation accelerated. Corruption continued, albeit on a lesser scale than under Acheampong.

At the heart of the problem was the government's unwillingness to tackle the fundamental economic problem of excess demand. Government revenue, which Akuffo's SMC had brought up to nearly 10% of GDP, once again dropped, sliding to less than 5% of GDP in 1981. This severely constrained the government's ability to engage in even the most urgent restoration of the functions of the state. Roads were impassible. Schools were without teachers, books or roofs. Clinics were without staff or medicines. Monetary policy continued with the same nominal discount rate that had been fixed by the SMC under Akuffo, and money supply growth was not brought under control. CPI inflation, which had dropped to around 50%, rebounded to over 100% again in 1981. But, with the much smaller monetary base, the inflation tax garnered just over 5% of GDP. The nominal producer price of cocoa was increased in line with inflation, but the nominal exchange rate was kept fixed at the rate set by Akuffo, making it appear impossible to grant any catch up for past inflation.¹ Investment continued its slide, dropping well below even a replacement rate. GDP per capita continued to atrophy, falling below the level of 1950. All in all, the urgent need for macroeconomic reform was not being met.

The ineptitude of the Limann government in dealing with the problem of excess demand and its unwillingness to dismantle the underlying licencing-price-control-cum-state-owned-enterprise

¹ One curious result of the combination of increasing the producer price while keeping the exchange rate fixed was that the producer price exceeded the world price, when converted at the official exchange rate. Yet the producer price was still well below what was necessary to restore the coca sector to health.

system, meant that shortages became even more severe, and hence the source of the corruption remained entrenched in Ghanaian society.

Rawlings, who had issued a clear warning to Limann to meet expectations of Ghanaian society as he stepped aside in September 1979, was forced to retire from the military. He remained in Accra, however, keeping a wary eye on the government while publicly proclaiming the purpose of his AFRC intervention. Eventually, on December 31, 1981, Rawlings led his second coup, installing the Provisional National Defense Council (PNDC) while affirming that there must be a complete revolution in Ghana.

The Early PNDC Government

The second Rawlings government, as with the first, was concerned primarily with the corruption that had permeated Ghanaian society. Styling itself as the Provisional National Defense Council (PNDC), the regime immediately began another housecleaning, following a populist Libyan model.¹ (See Agyeman-Duah 1987.) The approach was to establish People's Defence Committees (PDCs) in local communities, along with Workers' Defence Committees (WDCs) at places of employment. These challenged the authority of chiefs, managers, professionals, and even military officers. Later in the year the local councils were placed under the PDCs/WDCs. District and regional councils were re-constituted, to place them under grassroots control. A parallel system of tribunals was also established during 1982. To tackle the ill-gotten wealth garnered under the old regime, the largest denomination banknotes were recalled and exchanged for frozen bank deposits, while bank deposits in excess of ₵50,000 that could not be justified were confiscated. Market women and farmers were forced to sell food at controlled prices. Such arbitrary actions exacerbated the mistrust with which all economic agents – both corrupt and honest – viewed the regime.

Despite the fact that Rawlings had come to rule a second time amidst considerable popular approval, he was by no means securely in power. His tenuous hold was apparent in the traumatic events of 1982. In June, four persons, including three senior judges, were kidnaped and murdered. Two members of the PNDC were implicated. While one was tried and later executed, the public revulsion at this alien political style was palpable. The Ghana Catholic Bishops Conference aptly summed up the feeling which was widely felt:

“In the wake of the “revolution” atrocities of all sorts have been committed against innocent civilians by some members of the armed forces and various groups purporting to support the revolution. The wanton killings, senseless beatings, merciless molestation and general harassment continue without the Government showing any willingness or ability to do anything about them.”²

¹ In addition, support was canvassed from Libya, and the fast-fading Soviet Union, but little help materialized.

² Quoted in Herbst 1993.

With the economy and the state in shambles, no attention was paid to the underlying economic reasons for the corruption and the failing economy or to the now very limited ability of the state to carry out even the most elementary functions. Even as the economy was hitting new lows, disastrous shocks to the economy were further exacerbating the situation. Severe food shortages in the urban areas, due to the combination of attempts to control prices, even as inflation continued,¹ and the breakdown of the transportation system, were commonplace. These became even more serious in 1982 as drought returned to West Africa with a vengeance. Forest fires raged in the middle regions of the country, destroying vast sections of the forest where cocoa trees grew. While this was happening, Nigeria chose to expel hundreds of thousands of Ghanaians who were illegally living there, just as the Busia government had expelled Nigerians and other aliens in 1969.² The task of reabsorbing these individuals placed enormous strain on an already crippled Ghanaian economy and society.

It became clear to many in the PNDC that the actual path was not working -- both in political and economic terms. In the third quarter of 1982 a special committee was struck to explore alternative economic paths. The statist approach of Nkrumah, and the consequent rent-seeking associated with the regimes of Acheampong, Akuffo and Limann, had produced economic atrophy and corruption. Yet the populist approach was continuing the economic atrophy. This left room for consideration of a third way -- an outward looking market-oriented approach. This held out the genuine hope that the reforms would not simply increase GDP, but also address poverty and eliminate rents for the corrupt.

It was in this context that the PNDC chose to launch a market oriented economic reform program in the April 1983 budget. Work had commenced during 1982 to devise alternatives to both the kleptocracy of the old regime and the populism of the early PNDC. Critically, both Rawlings and his heretofore leftist Secretary for Finance and Economic Planning, Kwesi Botchwey, were persuaded that a market oriented reform program was the only escape from the continued downward spiral. Not all of the PNDC supporters were persuaded, for in November, as word of

¹ The official inflation figure for 1982 is considerably lower than that of 1981. However, in the chaotic atmosphere of 1982, it is dubious that the statistics reflect the true situation.

² The number of persons affected is not known exactly. Estimates range from 600,000 to 1,000,000 persons.

preparation of the alternative leaked, another coup was attempted. With the failure of that coup, the fate of the radical populist economic strategy was also sealed.

The Legacy of the Early PNDC

The early PNDC government faced the monumental task of restoring the health of both the state and the economy. The provocation of the Acheampong/Akuffo regime and the ineptitude of the Limann government may have justified extreme measures. Yet in the process, the view of the state and its agents as predators became firmly fixed in the minds of entrepreneurs. This would continue to haunt the Rawlings led government, even as it restored macroeconomic balance and moved to establish a modicum of democracy. Thus, the damage which the previous regimes, and the populist phase of the PNDC, had inflicted on the economy, would remain for many years.

2. The Economic Reform Program

Setting for The Reform Program

Rawlings saw corruption destroying Ghanaian society. Having failed in his attempt to eradicate the corruption by force, with a precarious hold on power, and a feeble state apparatus, Rawlings had few alternatives in his quest for reform. Yet in adopting the Economic Reform Program (ERP), with the support of the IMF and the World Bank and their emphasis on freeing up markets and eliminating the government budget deficit, he embraced an approach that had become anathema to many in the third world for its alleged association with severe social hardship. But Ghana in 1983 was different.

What was different? Most of the adjustments which an IMF program would impose had already taken place. Government expenditure (at 11% of GDP) had shrunk to the point that the state was unable to perform the most elementary functions, and public sector wages had long failed to keep up with inflation. Many state-owned enterprises had become mere shells, unable to obtain raw materials or cash to pay employees. Domestic prices of importables, and easily smuggled exportables, had already risen to reflect the scarcity value of foreign exchange. But government revenue from foreign trade had not kept pace, because the official nominal exchange rate was used to calculate the duties. The index of the real official exchange rate stood at a mere 7% of its value at independence. It was obvious to Rawlings and his advisers¹ that producers of exportables had responded to the real incentives facing them. Production of the two major export commodities, cocoa and minerals, had dropped to less than half of the level during Busia's administration, and the value of exports (through legal channels)² now amounted to a puny 5% of GDP, reflecting the fact that non-traditional exports had become uncompetitive in world markets. A reform program that raised the price of foreign exchange to its scarcity value, and balanced the government budget, need not engender serious social hardship, while holding out the promise of reversing the long descent of the Ghanaian economy.

Subsequent Evolution of Reforms

The reform program was launched by an authoritarian government that had seized power by force of arms, and was prepared to use that force to retain power. Members of the small inner circle of economic policy decision-makers were convinced of the importance of maintaining a disciplined approach to sustain the Economic Reform Program in the face of both internal and external constraints. The PNDC government (1982 through 1992) was thus relatively insulated from interest group pressures – relative to western style democratic regimes and relative to the subsequent Ghanaian democratic regime.

¹ The leader of a small group of technocrats that designed the reform program was J.L.S. Abbey. For his reflections on the lessons, see Abbey (1989).

² There is considerable evidence to suggest that smuggling of exports became substantial, even despite the much higher costs of moving goods clandestinely. See, for example Bulir (1998).

Some sensitivity to various interests must have remained, nevertheless. Two facts suggest this interpretation. First, most of the reforms that the PNDC chose to institute in the first few years of the ERP were easily implemented, both politically and administratively. Prior adjustment meant that the reforms had little effect on relative prices, making the changes easier in political terms. (See Leith and Lofchie 1993, and Kanbur 1995.) Abandoning a complex rationing system in favor of a market based system meant that the reforms reduced the strain on an already overburdened administrative system. Second, several politically sensitive and administratively complex reforms were left incomplete, including the cocoa sector, state-owned enterprises, and, critically, effective tax collection and expenditure control systems for government. The failure to complete these before the return to electoral competition in 1992 left the economic reforms vulnerable to the vagaries of electoral competition, in contrast with an authoritarian government.

The resumption of electoral competition in 1992 marked a fundamental change in the political economy of Ghana. With elections in view, Rawlings and his party were now subject to the prospective discipline of the electorate. This considerably shortened the time horizon of the government, and made attention to the demands of different interests much more immediate. Further, a key member of the inner circle, Dr. Kwesi Botchwey, PNDC Secretary for Finance and Economic Planning, left government in March 1992.

With this background, we now turn to review the major elements of the reform program, from its launch in 1983 through the late 1990s.

Exchange Rate Reforms

From Fixed to Market Exchange Rate

The first step in the reform program was to break the taboo that associated devaluation with government overthrow. An imaginative scheme of export bonuses financed by import surcharges was the start in April 1983. This raised the official nominal effective exchange rate from $\text{¢}2.75/\text{\$}$ which Akuffo had set, to an average of about $\text{¢}25/\text{\$}$, roughly offsetting the cumulative inflation from 1978 through 1983, without creating a budgetary drain on government. Yet this solution had two major problems associated with it. First, the scheme constituted a multiple exchange rate, which is classified by the IMF as a cardinal sin. Such an arrangement could not be retained as a permanent feature of an IMF-supported program. Second, the government was severely constrained in its ability to carry out any reforms that required competent administration, and the scheme was intensive in administration. Consequently, later in 1983 the scheme was abolished, and replaced by a unified rate of $\text{¢}30/\text{\$}$.

The new fixed exchange rate of $\text{¢}30/\text{\$}$ was clearly much more competitive than before the reform program had been launched, but it was still less competitive than the real rate prevailing in the late 1970s. A more aggressive increase in the real price of foreign exchange was required. In March, August, and November of 1984 further devaluations were introduced, taking the exchange rate to $\text{¢}50/\text{\$}$ at year end, restoring the real exchange rate to about the level achieved immediately following Akuffo's devaluation of 1978. The same approach of periodic devaluations was followed in 1985 and early 1986, taking the exchange rate to $\text{¢}90/\text{\$}$ on January 13, 1986. With inflation substantially less than these exchange rate changes (and declining) this represented a further real depreciation.

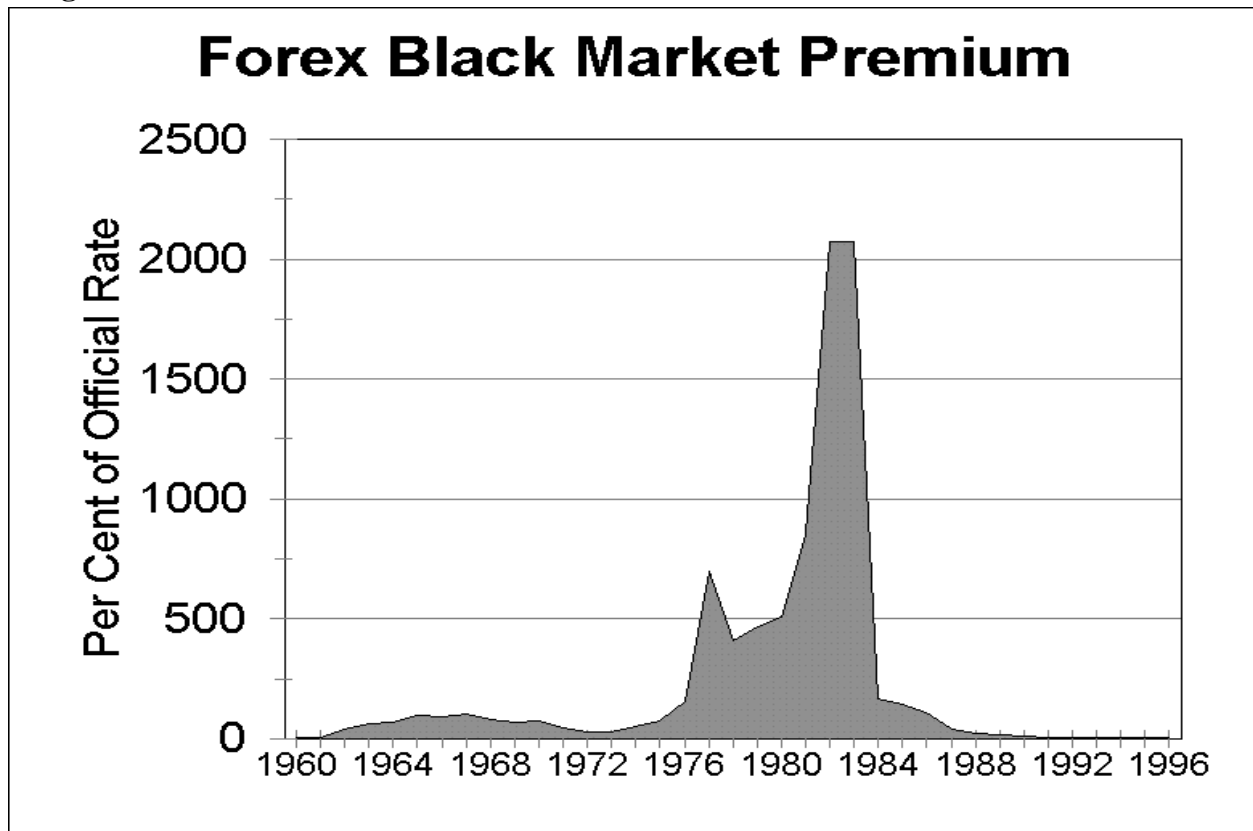
Yet this approach was again starting to generate the same sort of negative political reactions that previous governments had experienced. A discrete action had to be taken each time, and now that most of the rents had been removed from the system, there was a pass-through to domestic prices of importables following each devaluation. To depoliticize the exchange rate setting, a weekly auction system was introduced in September 1986. At first this involved a reintroduction of a dual exchange rate, as not all transactions through the official banking system were eligible to obtain foreign exchange through the auction. However, in February 1987 the rate was unified at the auction rate.

These moves were successful in propelling the real exchange rate to a more competitive level. The real Cedi/SDR exchange rate average for 1987 reached a level roughly comparable to that of 1968, the first full year following the 1967 devaluation. Yet this was still roughly only three-quarters of the real exchange rate at independence (Figure 9). More remained to be done.³

³ Throughout we use the 1957 real exchange rate of the Cedi/SDR as a convenient benchmark. It should be noted, however, that comparisons extending over decades cannot take the original base value to be necessarily the ideal. There are two important reasons for this caution.

From the time Nkrumah imposed exchange controls in 1961, a black market on foreign exchange had developed. Information on rates in this market is inherently impressionistic, with numbers reported by unknown informants reflecting unknowable volumes of transactions. Nevertheless, the very fact that a black market exists indicates that some desired transactions are not being accommodated through the officially sanctioned markets. The premium that black market foreign exchange was earning had grown under Nkrumah, subsided under the NLC and Busia, grown again under the military and Limann, and exploded during the early PNDC government (Figure 15). The exchange market reforms just noted had dramatically reduced the black market premium. But nevertheless, a premium remained.

Figure 15



Sources: 1960 to 1984 from Wood (1988); after 1984: African Development Indicators.

The auction system was run by the Bank of Ghana, which gave rise to suspicions that the rate was subject to some manipulation. In retrospect, the monthly average of the auction rates from

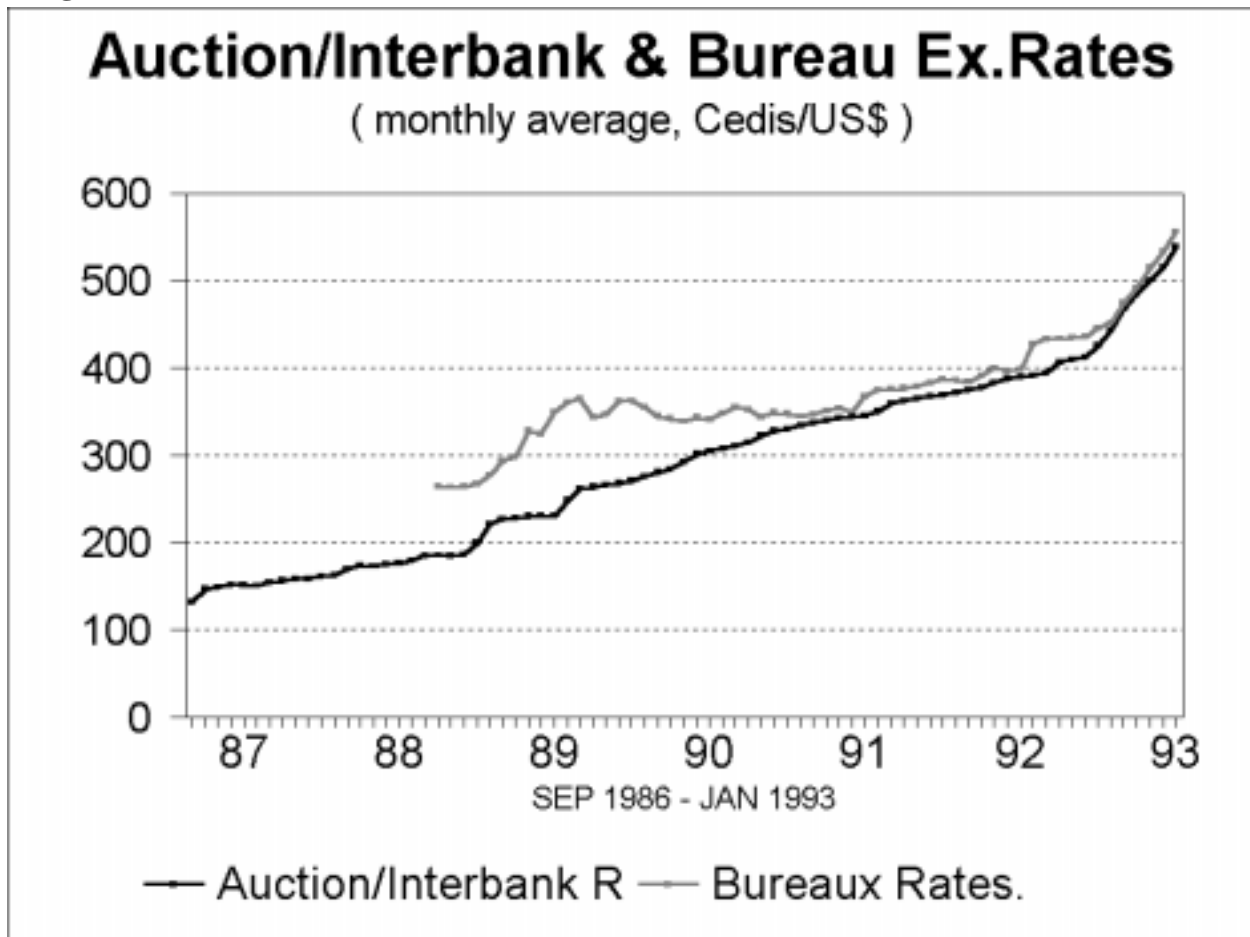
First, the initial value may not have been an equilibrium. Second, the various series may not capture all important elements of the changes that take place.

early 1989 through early 1992 shows a remarkably smooth progression. A major step towards freeing up the foreign exchange market occurred in 1990, when an inter-bank market was set up to handle wholesale transactions in foreign exchange. This was run in parallel with the auctions until 1992 when the auction window was closed. With this move, the transition to a more transparent, market determined, exchange rate was largely complete.⁴ The steep recovery of the real exchange rate stopped, however. The average real exchange rates for the years 1988 through 1991 all fluctuated in the range of 77% to 83% of the rate at independence.

The very existence of a black market implied some corruption and therefore, in the eyes of the PNDC, justified an attack. In keeping with the thrust of the reform program, the ingenious solution was to legalize the black market in the form of officially sanctioned, but privately operated, foreign exchange bureaus. From February 1988 onwards, these have functioned, freely buying and selling foreign exchange, mostly cash, on a “no questions asked” basis. Initially there was a modest premium over the official auction rate, but gradually by the end of 1992 the two rates had largely converged, except for a small premium reflecting the retail nature of the bureau transactions (Figure 16).

⁴ It was not entirely complete, however, for cocoa receipts continued to be channeled through the central bank, which then had a source of foreign exchange to use to intervene in the market.

Figure 16



Source: Bank of Ghana

By the time Rawlings put himself forward as a candidate for election to President in 1992, a market-determined exchange rate had become widely accepted in Ghana. A substantial constituency now benefitted from a competitive real exchange rate, and was well aware of that fact. Any attempt by a future government to suppress the market in foreign exchange would inevitably have to deal with a thriving market with large numbers of participants now familiar with the market details. In other words, it would be much harder for any future government to resume foreign exchange rationing than it had been for Nkrumah to introduce it in the first place and for his successors of various political stripes to retain it.

Foreign Exchange Policy Under Elected Government

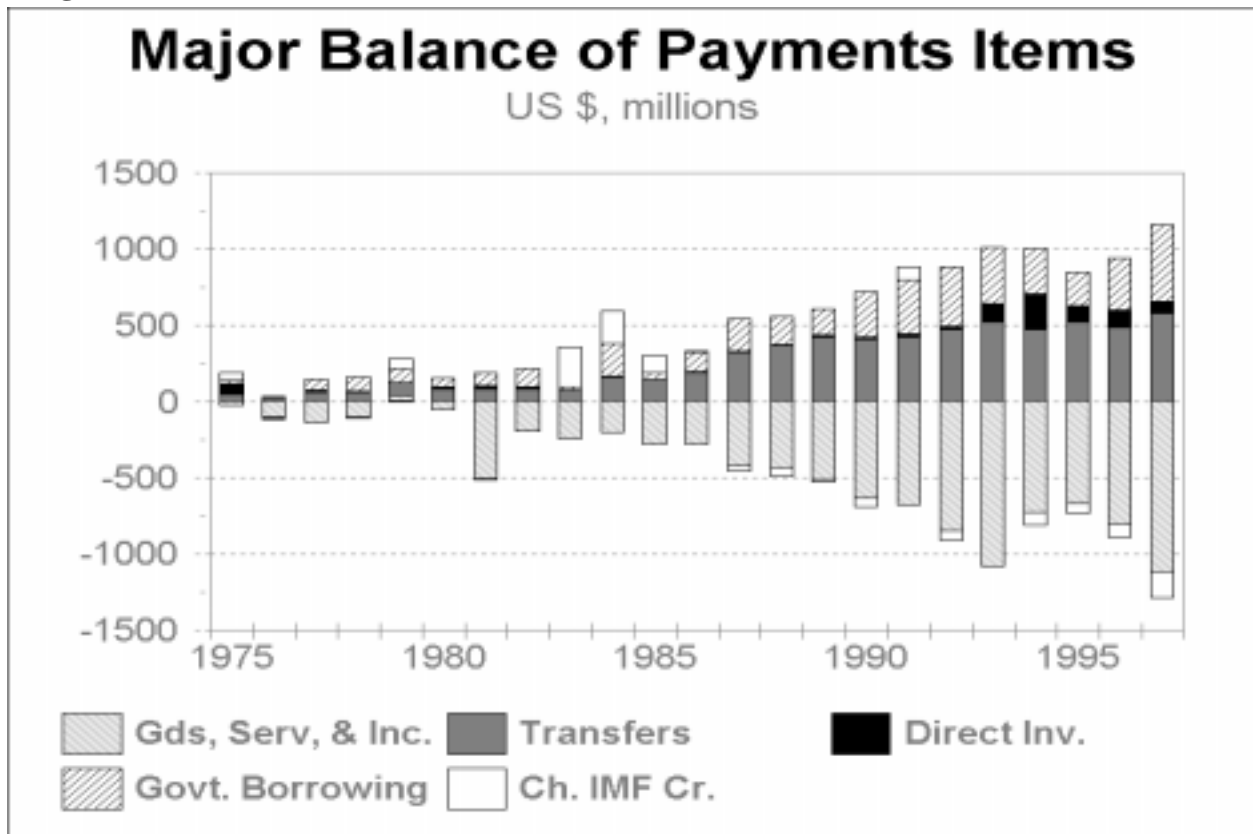
The return to electoral politics in 1992 not only affected government, but it also bore on the foreign exchange market, both directly, and indirectly. The expanding government budget deficit and acceleration of inflation spilled over into expectations of rapid depreciation of the Cedi in the

foreign exchange market. This became a self-fulfilling prophesy, as the real exchange rate depreciated rapidly. From 1991 to 1994 the real exchange rate of the Cedi vis-a-vis the SDR depreciated by 60%. This doubtless stimulated the growth of exports, which reached shares of GDP similar to the early 1960s (before exchange controls had started to bite). Yet the rapid depreciation of the real exchange rate appears to have had little dampening effect on imports (Figure 9). In part this was attributable to the substantial financing of government's budget by transfers from foreign donors and foreign borrowing (Figure 17). As a result, the imports to GDP ratio moved from 25% in 1991 to 38% in 1997.

A major reversal of exchange rate policy appears to have taken place in 1995, as the Cedi appreciated markedly in real terms during 1995 through 1998, returning the real index to the level that had prevailed on average during 1992. It appears that the authorities, faced with a jump of inflation to over 70% in 1995, attempted to dampen inflationary expectations by jawboning foreign exchange dealers into slowing the rate of nominal depreciation. But to the extent that some individuals' demands for foreign exchange were no longer being met in the interbank foreign exchange market and the forex bureau market, the incentive to turn to a curb market reappeared.

While inflationary expectations may have been dampened by the exchange rate strategy, signals on other dimensions of policy were inconsistent. For example, a competitive and stable real exchange rate is fundamental to an export oriented long term growth strategy. With the significant real appreciation from 1995 to 1999, potential exporters could no longer rely on such an incentive.

Figure 17



Source: International Financial Statistics

The combination of a substantial fiscal deficit, financed by monetary expansion and foreign borrowing, while keeping the rate of nominal depreciation of the Cedi markedly less than the rate of inflation, created an unsustainable balance of payments situation. Eventually, the exchange rate had to give. The interbank rate depreciated in nominal terms by over 40% during 1999, while inflation was expected to run at 12%. The real exchange rate was thus restored to a level comparable to 1995. But the high variance of the real exchange rate over the 1990s increased the risk facing both the export and import-competing sectors, and thereby reduced the incentive effect of the high real exchange rate index.

Fiscal Reforms

The Early Reforms

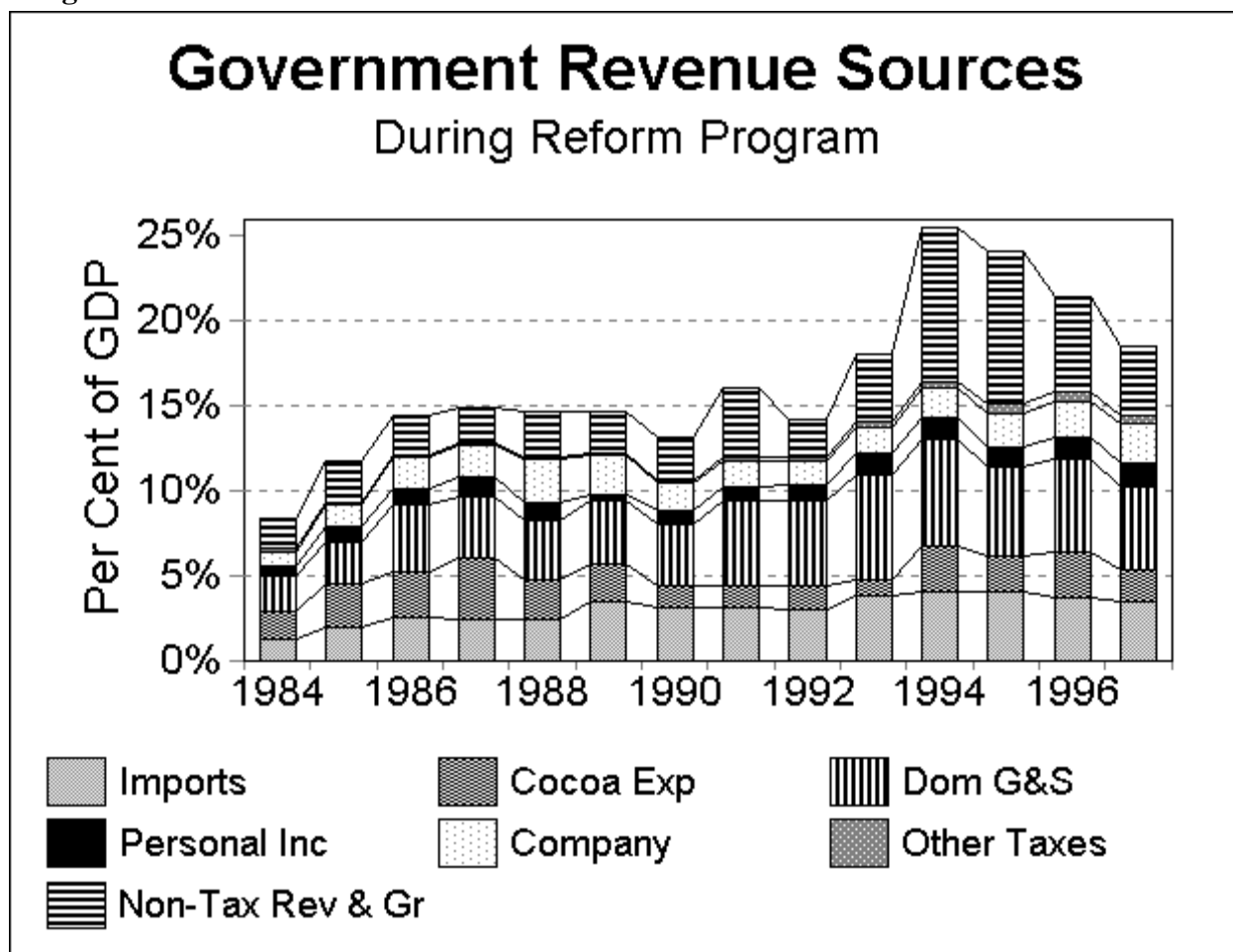
A key condition associated with IMF and World Bank support for the reform program was a balancing of the government budget. This was accomplished in relatively short order – by 1986 – largely on the basis of a substantial increase in revenues. From 5.6% of GDP in Limann's last year, revenues grew to 13.6% by 1986. This, in turn, permitted the PNDC government to expand government expenditure to over 13% of GDP (Figure 2).

The improved government revenue picture arose from a combination of exchange rate reform and tax reform. The former followed from the fact that by adjusting the exchange rate from ₵2.75/\$ in early 1983 to ₵90/\$ at the beginning of 1986, the base for all trade taxes such as import and export duties was augmented by over 30 fold, even before allowing for the effect of expanding the volume of exports and hence imports on the share of trade in the economy. Some of the reform was to reduce and simplify the customs tariff. These changes all together approximately tripled import duty collections as a % of GDP.¹

Other revenue sources were expanded dramatically by reforming tax administration (Figure 18). The Internal Revenue Service and the Customs Service were both removed from the civil service and placed under the supervision of a National Revenue Secretariat. This permitted a rationalization of the incentive system and hence recruitment of professionals. Special enforcement units were set up. Various innovative arrangements were made with associations. For example, the taxi drivers' association collects a daily tax from its members, and after deducting a commission, which it uses to finance its operations, turns over the revenues to government. The members prefer to pay daily out of their cash flow, rather than in larger lump sums, and they prefer to deal with their own collectors rather than be shaken down by bureaucrats or tax police.

¹ The exchange rate effect was not entirely positive for government, as some of its obligations were either implicitly or explicitly denominated in foreign exchange.

Figure 18



Source: Ghana Statistical service, Quarterly Digest of Statistics

Retreat From Fiscal Discipline

The major efforts made over the period from 1983 to restore fiscal and monetary discipline started to flag in 1992, with the run up to the democratic elections of that year. In early 1992 the stance of fiscal and monetary policies became decidedly expansionary. The government budget deficit jumped from a surplus of 1.6% of GDP in 1991 to a deficit of over 5% of GDP in 1992. This turn around was composed mostly of a jump in expenditure (by nearly 4% of GDP), with a drop in revenues, including a fall in receipts from privatization, accounting for the rest.

If this had been a once off event, it might have been tolerable. However, in retrospect it was a clear break in government's economic discipline, which had shown a modest budget surplus in each of the years 1986 through 1991. Government expenditures continued to grow rapidly,

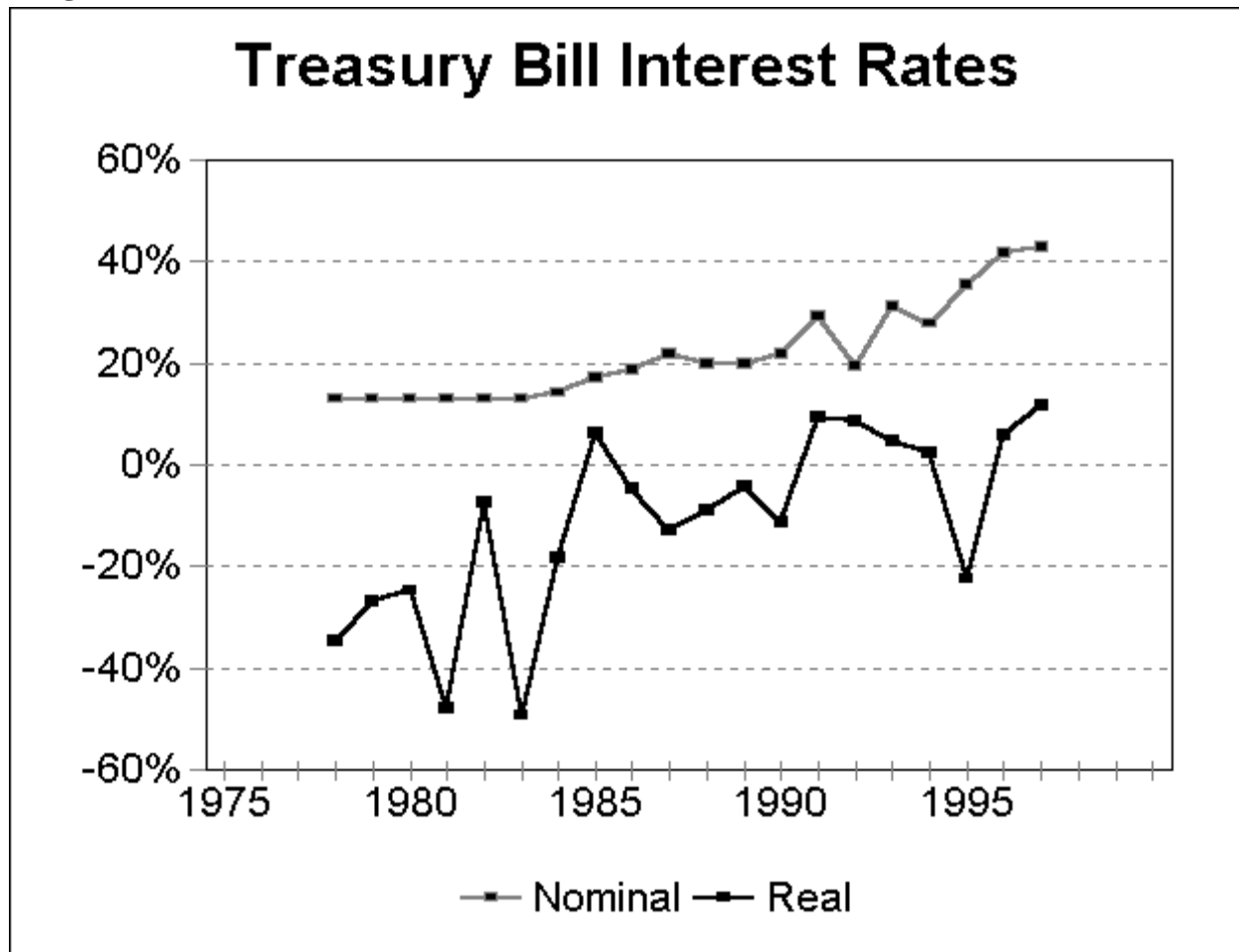
surpassing Nkrumah's most lavish year (1965 at 25.8% of GDP) in 1994, and remained above that mark. Government scrambled to find ways of financing the growing expenditure. For example, an increase in the tax on petroleum was proposed to Parliament in 1993, but was not approved.

The inability of the tax system to augment its share of GDP in line with the expenditure growth left a chronic deficit to be financed somehow. The choices for financing of the deficit boiled down to some combination of: (1) borrowing from the central bank (effectively printing money); (2) borrowing from the public; (3) borrowing from abroad; and (4) selling off state owned enterprises. Financing the deficit by borrowing from the central bank inevitably pushed up the growth of money -- from the modest growth rates hovering around 10% for 1990 and 1991 to over 50% in 1992. An increase in the central bank's discount rate was insufficient to offset the inflationary pressure: CPI inflation surged, and the current account deficit opened to 9.9% of GDP in 1993.

In subsequent years government was able to augment tax revenues, but revenues never caught up to the growing expenditures. Indeed, the anticipation of elections in late 1996 brought another surge of government expenditure and net lending, reaching one third of GDP. To help improve tax administration and to finance government's ambitious expenditure program, a value added tax (VAT) was introduced in early 1995 to replace a manufacturers' sales tax that the Nkrumah government had introduced on a much narrower base. However, the political sensitivity of parliament, and some administrative teething problems, led to a weak public education program, which doomed the tax. (See Terkper 1996.) Following several protest riots, it was withdrawn two months after it was introduced, leaving government with an even wider gap between revenue and expenditures in the coming election year, 1996, amounting to 10.4% of GDP.

After the 1996 elections, it was possible to revisit the issue of a VAT, and finally in 1998 the VAT was reintroduced. The second time round, with the opposition seated in parliament, there was wider consultation and a better education program. Further, a lower rate was set, at 10% rather than the 17.5% rate which had been attempted initially. This blunted opposition, and discouraged non-compliance. While the net effect of dropping the sales tax and introducing the VAT has not increased government revenues directly, the improved record keeping associated with the VAT appears to be enhancing compliance with the income tax.

Figure 19



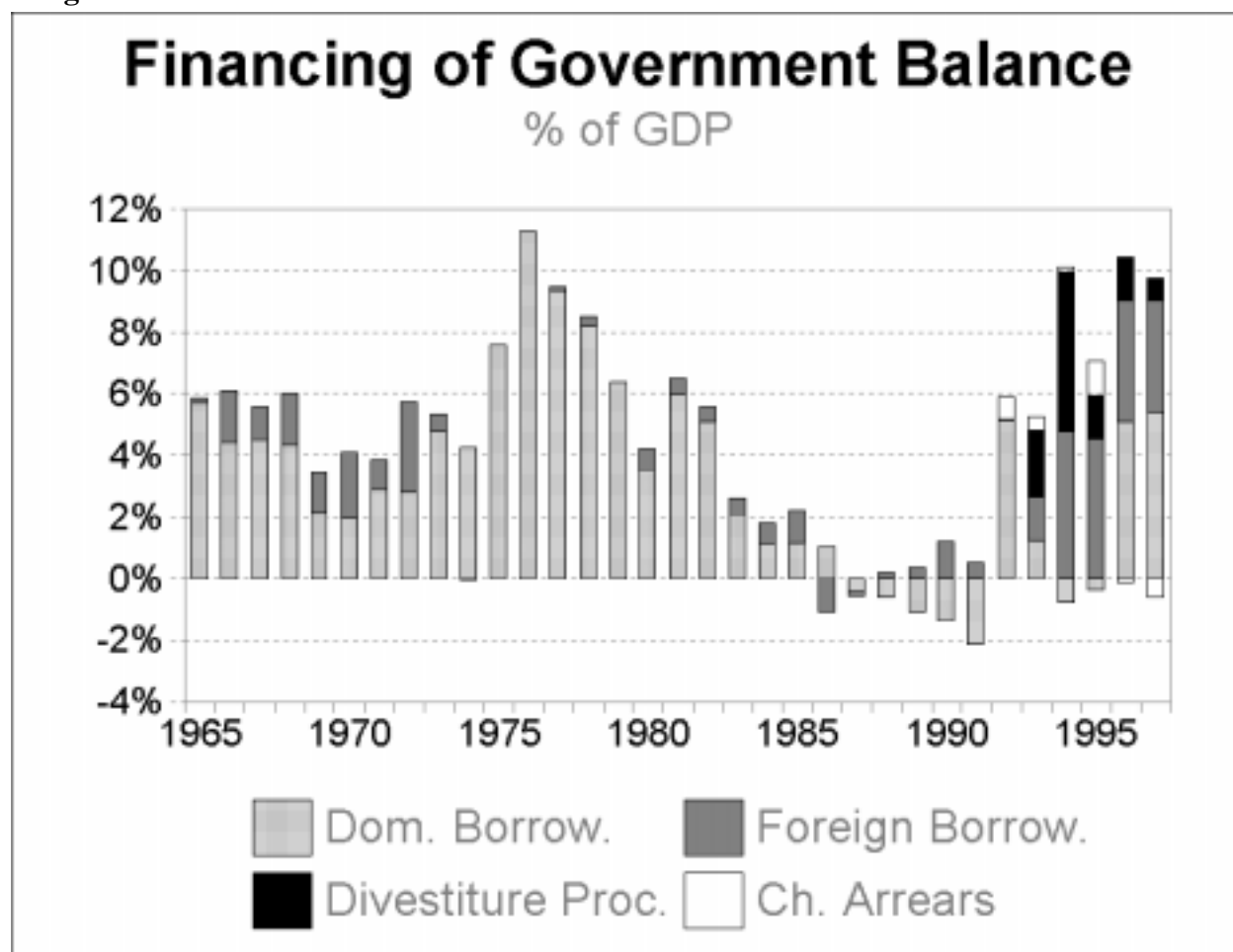
Source: International Financial Statistics

In addition to central bank financing of the deficit, government found that it had to turn increasingly to the public via Treasury bills. Real interest rates on T-bills, which had been running at modestly negative real interest rates from 1986 through 1990, became positive in 1991, and except for the inflationary spike of 1995, have remained positive ever since in order to attract the necessary funds (Figure 19). This strategy, of course, risked crowding out potential private sector borrowers of funds in the capital market.

The third possible source of financing the government budget deficit -- borrowing from abroad -- came into play in a major way from 1994 onwards. Government borrowing from abroad increased to 4.8% of GDP in 1994, and through 1997 remained well in excess of 3% (Figure 20).

This served to highlight the growing problem of the build up of external debt, and the associated cost of servicing it. (See discussion of debt below.)

Figure 20



Source: International Financial Statistics

In addition to the traditional avenues of formally borrowing funds, government began to run up arrears in payment of some of its bills internally. Although not substantial relative to other sources, such a practice was indicative of a lack of internal financial controls. More important quantitatively, government received significant funds from the divestiture of state-owned enterprises, starting in 1993 at 2.2% of GDP, jumping to 5.2% in 1994, and falling back to 1.4% in each of 1995 and 1996.² Had these assets not been sold, the size of the government deficit to

² The data on divestiture proceeds and changes in arrears cover the period from 1990 only. Although a few state owned enterprises were disposed of in the years following the overthrow of Nkrumah, there are no systematic data covering the proceeds from such sales.

be covered by borrowing, either internally or externally, would have averaged close to 10% of GDP during 1994 through 1997. This gap between government spending and taxation revenue was similar to the average during Acheampong's most profligate years. Clearly the unwillingness to limit government spending to **ifs** taxation and grant revenues was unsustainable, placing the entire reform program in jeopardy.

Foreign Debt

Rawlings had inherited an economy in shambles, but an excessive foreign debt was not one of the problems. Nkrumah had drawn down the accumulated foreign exchange reserves, and borrowed both long term to finance the massive Volta River project, and short term to cover a growing shortage of foreign exchange. After a series of rescheduling, one of which had a substantial grant element (see Chapter 1), the debt was brought to a moderate level where it remained during the rule of Acheampong. It was only after the departure of Acheampong that the military government took on additional debt.

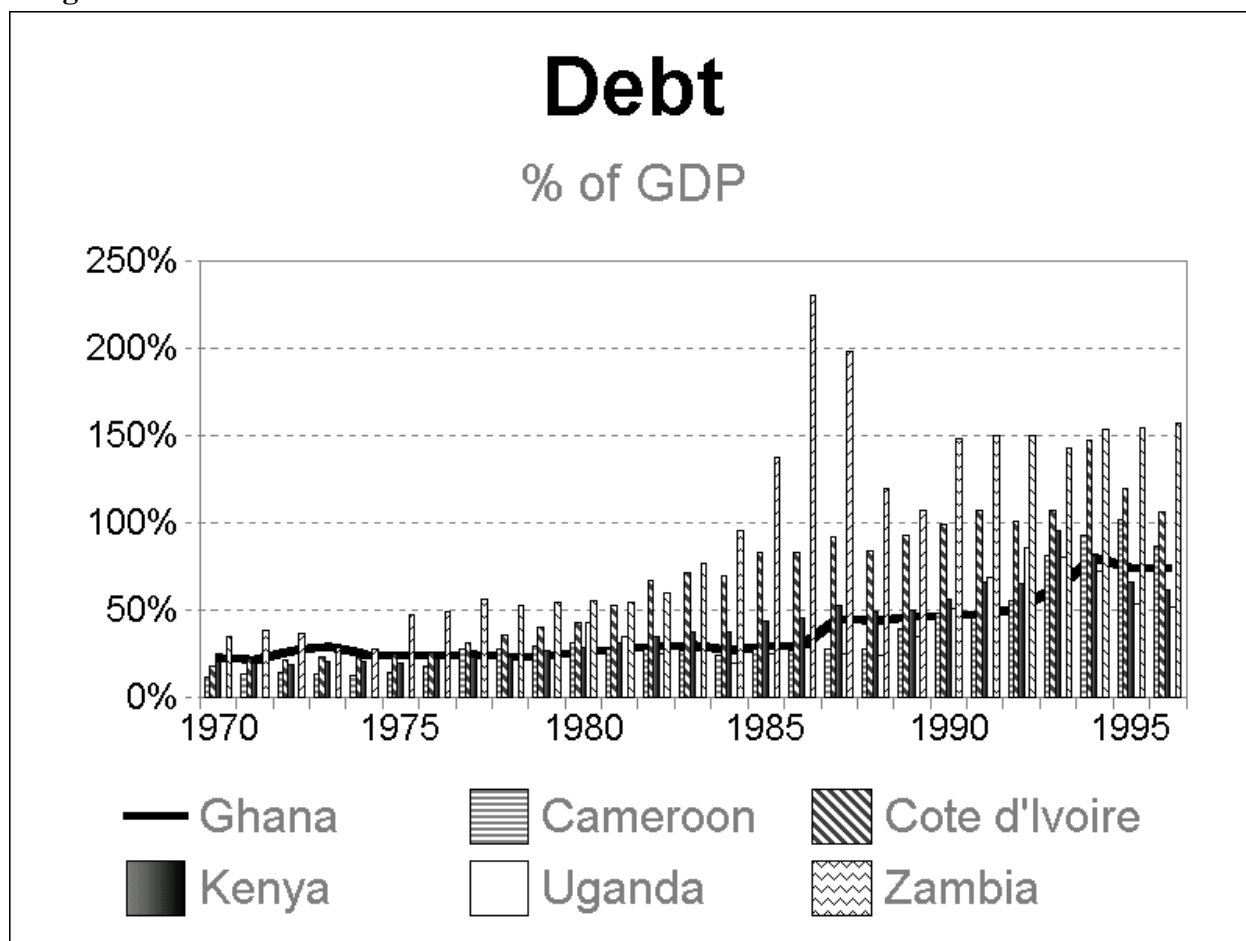
Initially Rawlings did not increase the debt. This is scarcely surprising, given the radical populist stance of the PNDC in **ifs** first year in office, which would not have endeared the government to potential lenders. However, as part of the reform program the PNDC government took on additional foreign debt. Foreign governments and in particular multilateral agencies were ready to finance new projects in Ghana. As Table 1 shows, the share of multilateral debt to total debt increased from just over 20 per cent at the outset of the ERP to over half in 1997. From the launch of the reform program in 1983 to the end of 1997, the external debt almost quadrupled in dollar terms.

Table 1:
Debt Statistics Since Launch of ERP

	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
Total debt stocks (US\$ million)	1,666	1,963	2,257	2,767	3,313	3,128	3,397	3,873	4,371	4,499	4,878	5,459	5,857	6,136	5,982
Debt reduction (US\$ million)	NA	NA	NA	NA	NA	NA	(44)	(102)	(116)	0	0	(12)	(1)	0	0
Rescheduling (US\$ million)	0	0	0	0	0	42	3	0	0	40	0	0	0	74	0
Arrears, total (US\$ million)	18	30	44	54	76	78	112	133	113	122	159	150	117	37	27
Concessional/Total debt (%)	49.5	41.8	41.1	44.5	49.0	52.0	53.8	54.8	54.5	57.2	59.3	61.2	63.6	63.9	66.5
Multilateral/Total debt (%)	22.5	20.2	23.3	28.3	34.4	42.1	43.5	47.5	47.6	48.9	49.3	49.5	50.7	50.8	53.1
Debt service/Exports (%)	30.4	21.6	23.6	28.3	45.8	56.6	50.4	37.0	27.1	28.4	25.0	26.1	25.2	26.9	29.5
Total debt/Exports (%)	348.6	318.6	333.6	343.6	365.3	324.2	377.4	388.8	392.3	400.8	396.6	386.4	363.1	345.0	349.4
Total debt/GNP (%)	41.4	45.0	51.0	49.4	67.1	61.8	66.2	67.1	67.5	71.3	83.3	102.4	92.5	90.4	88.6

Source: Global Development Finance 1999 CD-ROM

Figure 21

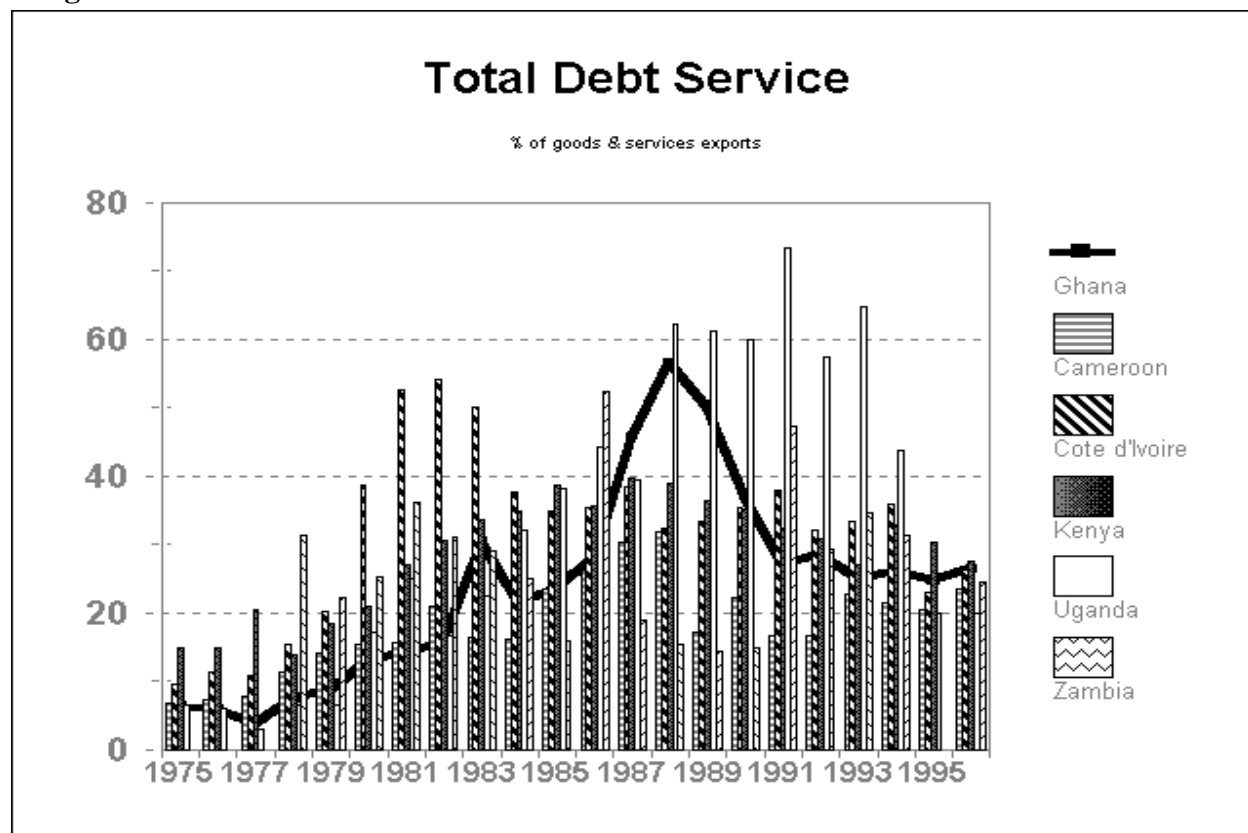


Source: World Development Indicators

Given the relatively low level of debt to begin with, and the desperate need to restore essential infrastructure, the initial increases in the debt were amply justified. Nevertheless, the increase in the debt to GNP ratio from 41 percent in 1983 to 89 percent in 1997 is a cause for concern. Relative to some of the seriously indebted African countries, such as neighboring Côte d'Ivoire or Zambia, this may still not be in the excessive category (Figure 21). Yet annual debt service has become a significant first claim on export earnings. Debt service as a ratio of exports increased rapidly from less than 10 percent in the 1970s to over half at the end of the 1980s (Figures 22 and 23). A large part of this was due to the fact that substantial amounts of relatively short term IMF loans taken at the beginning of the ERP fell due. IMF repurchases and charges represented over 50 per cent of total debt service in 1987-89. This number subsequently fell, bringing down the debt service to exports ratio significantly. This was further helped by three reschedulings in 1987,

1991 and 1996. Annual debt service is now running between 25% and 30% of exports of goods and services.¹

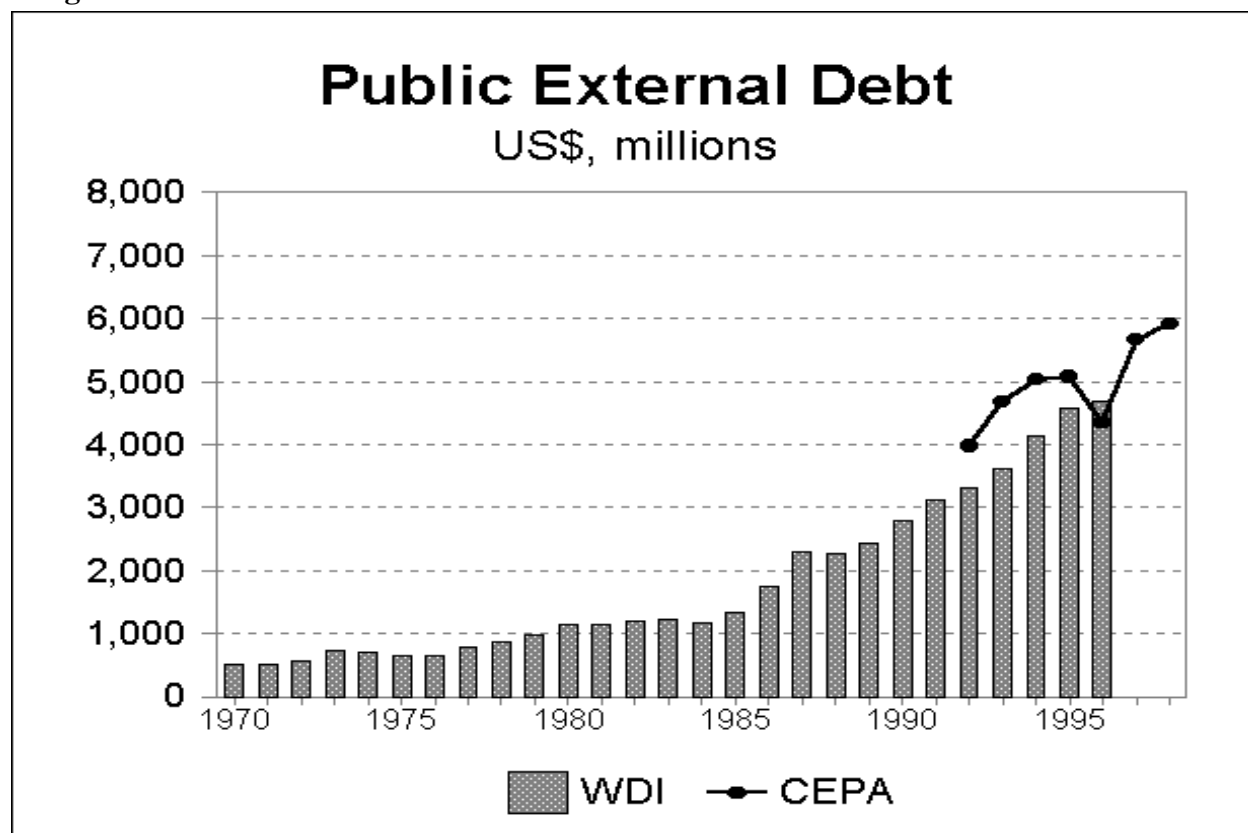
Figure 22



Source: World Development Indicators

¹ Different sources of data on debt report different numbers. The longest time series is available from the World Bank's *World Development Indicators*. However, the IMF 1999 and CEPA 1999 both report higher figures. The data reported by CEPA 1999 are also shown in Figure 23.

Figure 23



Sources: World Development Indicators and Centre for Policy Analysis (CEPA)

This improvement notwithstanding, such a level of debt service to exports is still considerable – to the point that it is highly questionable whether it can be maintained in the long run. Ghana did not qualify for the initial Highly Indebted Poor Country (HIPC) initiative in 1996, as the country was not considered to have an unsustainable debt burden according to the criteria defined by that initiative. However, as the criteria were relaxed at the Cologne summit in 1999, Ghana’s debt did fall into the unsustainable category (Table 2).¹ Note also that on the basis of the debt service to export ratio alone, Ghana would have qualified already for the initial HIPC initiative. The fact that Ghana’s debt is regarded as unsustainable by such widely accepted criteria as the ones set out by the Cologne initiative indicates that debt is becoming a matter of serious concern for the country.

Table 2:
Measures of Debt Sustainability

	NPV Debt/Exports (%, in 1999) ¹	Debt Service/Exports (%, in 1997) ²
Level in Ghana	175	29.5
Sustainable level according to initial HIPC	200-250	20-25
Sustainable level according to Cologne initiative	150	unchanged

Source: Joseph (1999b).

Notes:

¹1999 corresponds to Ghana’s point of decision.

²Last available.

NPV is Net Present Value.

¹ See Joseph 1999b, or Andrews *et al.* 2000, for more information on the HIPC and the Cologne initiative.

Monetary and Financial System Reforms

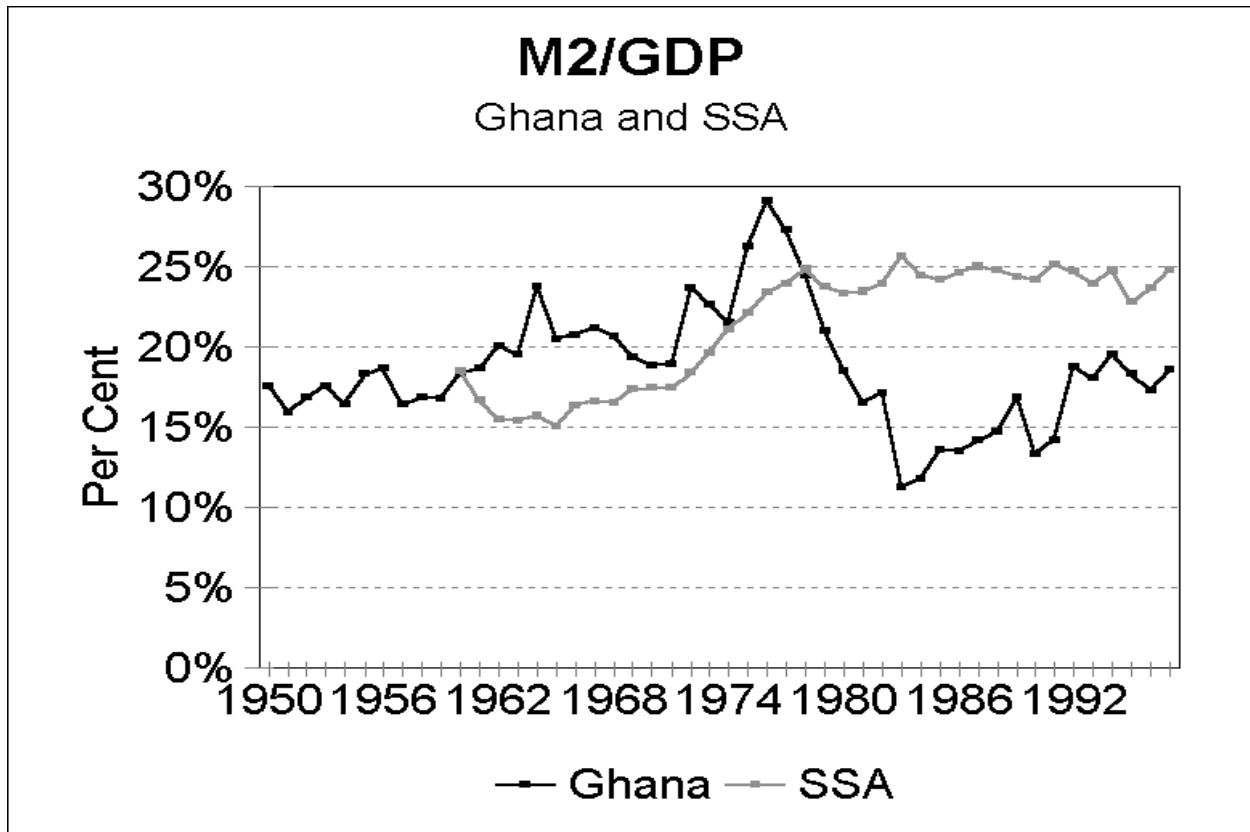
Money and Inflation

It proved to be even more difficult to achieve monetary stability than fiscal balance. Several elements were involved. The public's willingness to hold money had been sharply reduced first by the previous decade's inflation, and then by the arbitrary confiscations of monetary assets of 1979 and 1982. Although the money to GDP ratio did show a modest rising trend after 1983, the public remained leery of holding substantially larger balances in either cash or bank deposits, for fear of a repeat of past experience (Figure 8). A similar picture is evident when looking at the M2/GDP ratio (Figure 24). Moreover, although the ratio has improved since the mid 1980s – contrary to trend of the Sub-Saharan average – it remains more than five percentage points below the average for the continent. And, a high ratio of narrow to broad money persisted. In 1984, M1 accounted for 84 per cent of broad money.

These numbers suggests that the public would hold money only as necessary to finance transactions, and not as a store of value. Indeed, inflation continued at unacceptable rates for most of the rest of the decade: after the 122% rate in 1983, CPI inflation ran between 20% and 40% in every year except 1985, when good crops kept the CPI inflation to 10%.¹

¹ See Sowa (1996) re the sources of inflation during the early years of the reform program.

Figure 24



Source: International Financial Statistics

Note: Data for Sub-Saharan Africa are unweighted averages

Over the first few years of the ERP, monetary growth was kept in check largely because government was no longer drawing large volumes of credit from the monetary system. At the same time foreign monetary assets were drawn down, while growth of credit to the private and parastatal sector was kept in check by credit ceilings (Figure 4). Various quantitative regulations were gradually abandoned during the late 1980s, but the monetary authorities had not yet developed market based systems to replace the regulations. This made it difficult to sterilize the inflow of foreign assistance, leaving renewed evidence of excess demand in 1989 and 1990 (Figure 3). From late 1989 on, the Bank of Ghana started to actively absorb excess liquidity by open market operations. Eventually this had the desired effect, reducing inflation in both 1991 and 1992 (to about 10%). However, the central bank's own discount rate, which had been raised steadily from 10% in 1982 to over 30% in 1990, was not kept in line with inflation, and thus

remained strongly negative in real terms.¹

Financial Institutions at the Launch of the ERP

The financial institutions themselves were not in a healthy state. The heavy influence of the government had resulted in a financial system which was characterised by its shallowness, inefficiency, lack of competition, and a high proportion of non-performing loans. This meant that the financial sector was not playing the critical roles of mobilizing savings, evaluating innovations, and channelling additional resources to profitable new activities.

The structure and level of nominal interest rates were entirely determined by regulation. The Bank of Ghana (BOG) employed a system of minimum savings rates, combined with maximum and differentiated sectoral lending rates. The priority sectors -- agriculture, manufacturing and exports -- received credits at lower interest rates. In some cases, lending rates to priority sectors were lower than the minimum rates on savings deposits. Moreover, no concern was shown for risk, with preferential rates being accorded to such risky sectors as agriculture. In addition to the *dirigiste* stance on levels of interest rates, the BOG had guidelines for credit allocation according to sector, directing credits towards priority sectors. This bias of credits towards high risk sectors was further compounded by loans being directed towards SOEs within sectors.

Sectoral credit ceilings and the differentiated sectoral interest rates left the banks holding excess liquidity. Rather than lend to high risk sectors such as agriculture, the banks responded to the minimum lending requirements by holding funds in liquid assets that far exceeded their liquid asset requirements. Occasionally, banks even turned away potential depositors or refused to pay interest on deposits over a certain amount. Savings were also discouraged by nominal interest rates consistently falling below the level of inflation. Figure 19 shows that real interest rates for savings deposits have been highly volatile and negative since 1975 with the only exceptions of four non consecutive years.

From the days of Acheampong, the commercial banks all had a substantial state shareholding, and the bulk of their loan books were to state-owned enterprises, many of which were effectively bankrupt -- some before the reform program, and many more after its launch. The heavy state-control had implied that banks to a large extent had become instruments for channelling funds to

¹ See Kapur *et al.* re the fiscal and monetary reforms to 1991.

highly inefficient and corrupt state-owned enterprises, and to some extent – prior to Rawlings' entry on the scene – to private companies with ties to the government. During the Acheampong regime, loans were granted by military officers and the banks had no choice other than to comply. Government intervention continued after the fall of the military. In 1982, 92 per cent of bank credits outstanding were to the public sector (Sheng and Tannor, 1996). In other words, the bulk of loans had been extended on political grounds and not on any business criteria.

The financial sector was not performing its fundamental functions of mobilizing savings, evaluating investment opportunities, and facilitating the reallocation of resources from low productivity activities to higher productivity ones. Indeed, rather than adding value, the system was subtracting value, as funds that were repeatedly allocated to activities that could not service their loans. Non performing assets accumulated, amounting to as much as 41 per cent of total credit in 1989 (IMF, 1999).

The reforms and transformation of the formal financial sector

The reforms of the financial sector were not part of the initial efforts to restore the economy in Ghana in the 1980s. Before embarking on a project to clean up the financial system, the macroeconomic situation -- in particular with regard to the weak discipline of the fiscal and monetary policies -- had to be improved. However, during the 1983-88 period, the banks' balance sheets continued to deteriorate, with mounting non-performing assets (NPAs) and weak mobilization of deposits rendering all public banks insolvent. The banking system was in crisis and jeopardizing the economic recovery triggered by the ERP.

The financial sector reforms were carried out in three phases:¹ liberalization of interest rates and credit allocation (1987-88), prudential regulations and a major clean-up of the bank's balance sheets, in particular with regard to non performing assets (1989-91), and finally attempts to promote structural change through divestiture and other incentives to bring in private capital (1992-present).

In 1987 the Ghanaian authorities began the financial reforms by gradually liberalizing interest rates. Sectoral credit ceilings were removed the following year. This was accompanied by the

¹ In reality, the phases overlap somewhat. In particular, the improvements of banking regulations still continue.

liberalization of the foreign exchange market and the establishment of forex bureaux. In 1989, a far-reaching Financial Sector Adjustment Program (FINSAP) was initiated, financed by the World Bank and the IMF with co-financing from Japan and Switzerland among others. The FINSAP was divided into three programs: FINSAP-1 (1989-91) aimed at reviewing the legal and regulatory environment in the banking sector, restructuring banks in order to make them viable and more efficient and revitalizing the financial sector in general. FINSAP-2 (1992-95) and FINSAP-3 (beginning in 1995) sought to continue and reinforce the restructuring by creating new institutions and decreasing the role of government in the financial sector. Financing for further reform will in part fall under the more general ESAF loan, approved for 1999-2001.

One of the main features of FINSAP-1, was the amendment of banking acts and laws. Prior to the reforms, there were no uniform guidelines as to how to account for non-performing loans, making it difficult to properly assess the balance sheets of banks. Moreover, the Banking Act of 1970 did not provide for any capital adequacy ratio and allowed for high concentration of portfolio risks. Penalties for infringing the banking laws had not been adjusted for inflation, which severely limited its deterring effect. Furthermore, the BOG had concentrated its supervision efforts on ensuring compliance with credit ceilings rather than on the quality of the banks' assets. The Bank Examination Department (BED) of the BOG was understaffed and poorly trained. The 1989 Banking Act gave the BOG powers to request information, set rules for liquidity requirements, impose lending policies and to levy fines for banks not complying with the law. In addition, a major training program was implemented for bank supervisors and material resources as well as personnel were increased. In 1992, the Bank of Ghana Law was revised and implemented, giving the central bank increased powers in terms of banking supervision. The BOG is now in a position to act strongly and swiftly to deal with distressed banks. The commercial banks now work closely with the BOG on supervision issues and several interviewees considered the banking supervision to function well.

As long as credit was allocated by decree, and not by evaluation of creditworthiness of borrowers and their projects, the banks could subsist despite substantial amounts of virtually useless assets. But as the deregulation of credit and interest rates proceeded, the weaknesses of the banking system became evident. Following an audit of nine troubled banks, an estimated 62 billion Cedis (US\$222 million at that time) of NPAs were identified. These assets weighed heavily on the capital adequacy ratio, and the banks were consequently barred from expanding credit to other, more promising activities, which were responding to the new incentives created

by the reform program. To solve this bottleneck, in 1990 the World Bank's IDA concessional loan window provided funding to set up the Non-Performing Assets Recovery Trust (NPART). Assets transferred to NPART were either offset against liabilities of the bank to the BOG or transformed into BOG bonds. This permitted the banks to offload their non-performing loan book, making it possible to sell off government's shares in some financial institutions, and to permit all to focus on profitable loan opportunities.

The rural banks, accounting for around 7 per cent of total deposits in the banking system (Sheng and Tannor, 1996), accumulated substantial amounts of non-performing assets during the 1980s but have only recently been subject to major restructuring. Of the 133 rural banks that were in operation in 1998, 23 had their licenses withdrawn in late 1998 for not fulfilling the prudential requirements, which are the same as for commercial banks. The BOG intends to create what they call an apex institution for the development of a network of sound rural banks. Once this is in operation, the BOG may continue its support by providing funds to hire outside auditors, or through training. According to one of our interviewees, lack of human capital remains one of the main problems to rural banks. As a result, book keeping is still often poor and rural banks continue to accumulate bad debts. In the 1990s, a rural bank association was set up with the aim to provide training and basic equipment. The BOG itself administers a number of specialized credit lines, which are funnelled through the rural banks. Examples are funds to help smallholders market their product, funds for land conservation and construction of irrigation and a special fund for women. There is also a community bank refinance scheme which aims at improving the balance sheets of rural banks.

Efforts have also been made to promote Non Banking Financial Institutions (NBFIs) to fill some of the gaps left by the banks. In 1993, a law specifically dealing with NBFIs was introduced. There are currently 2 discount houses, 7 savings and loans companies (IMF, 1999) and 11 brokerage firms in Ghana (GSE, 1999) among the NBFIs. The SSNIT, a social benefit fund, is the largest financial institution in Ghana.

The Ghana Stock Exchange (GSE) came into operation in 1990 with 11 listed companies and a market capitalization equivalent to less than one per cent of GDP. The number of listed companies has grown to 21 (GSE, 1999) and market capitalization is currently nearly a third of GDP (Kenny and Moss, 1998). This rapid growth notwithstanding, the GSE remains rather

marginal as a source for funds for corporations.¹ As an example, the market capitalization can be compared to the 200 per cent of GDP ratio for the South African bourse. Furthermore, this rather rapid growth of the GSE is mainly the result of the listing of Ashanti Goldfields Corporation (AGS) in 1994. AGS account for approximately 90 per cent of total GSE market value.

As part of the program to revitalize the financial sector, and to give a larger weight to private capital, in 1992 the government announced a strategy to divest its equity in commercial banks. The largest commercial bank, Ghana Commercial Bank, now has a significant share of its equity held by the public, while the two major expatriate banks are again completely or almost completely in private hands. (See Divestiture below.) These changes have begun to have a significant impact on the role and mode of operation of the financial sector.

The current state of the banking system

The restructuring efforts have been under way for more than a decade and remain a priority in Ghana's economic program. There is no doubt that the reforms have had a positive impact on the effectiveness of the financial system in the country, which in turn has contributed to the economic recovery.

One major concern for the sustainability of economic growth in Ghana is the lack of private funds for long term investment. The country has derived most of its modest growth of income per capita since the beginning of the reform program from enhanced productivity, while the contribution of gross fixed investment has been trailing (see growth accounting below). An important reason for this low level of investment may be a lack of credit to finance new fixed capital.²

A major explanation for the lack of long term credit is that Ghana continues to be a very risky environment for investors. Inflation is still high and volatile, adding substantial uncertainty to

¹ This situation is not uncommon in emerging economies, where only the well established firms meet the listing requirements.

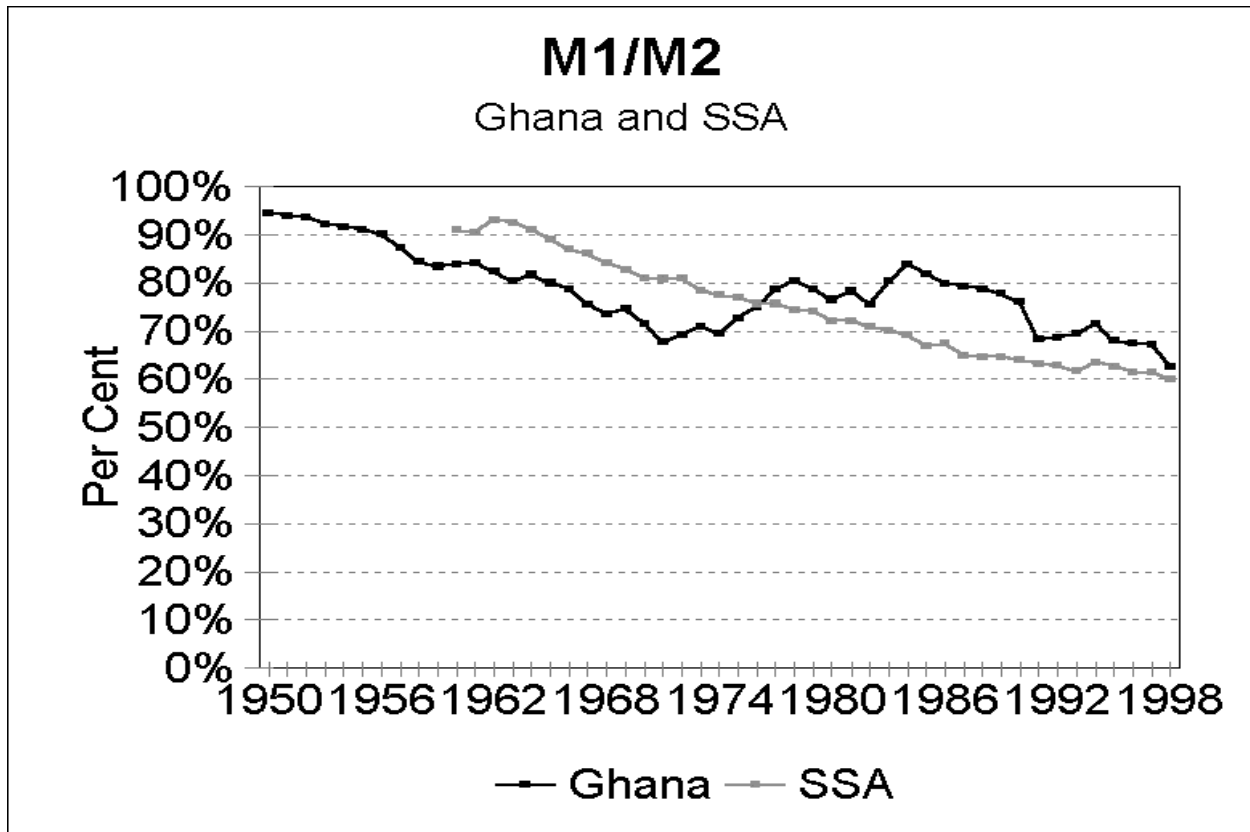
² One must be careful, however, not to exaggerate the potential benefits of improved access to credit. There appears to be a significant misconception about what increased supply of credit would actually achieve, not the least among the agents demanding such increases themselves (see, e.g., Buckley 1997).

the real value of financial assets. Suppliers of credit are reluctant to lock up funds for long periods. Banks, for example, are hesitant to commit funds for periods exceeding 3 to 6 months.

In addition to the detrimental effect of inflation on the supply of long term credit, the government's demand for funds crowds out credit to the private sector. The substantial and persistent budget deficits have induced repeated drawing of funds from the public. To finance its deficits, the government issues treasury bills at competitive interest rates. The T-bill rates have consistently been at about the same level as lending rates since the beginning of the 1990s (Figure 19). Moreover, risk averse banks and individuals often find T-bills more attractive than private projects.

The unwillingness of banks to provide long-term capital also stems from the short-term characteristics of deposits. Nearly 50 per cent of total deposits are demand deposits (see Figure 25) although the share of time deposits has been increasing throughout the 1990s. Moreover, the soundness of clients is often difficult to assess due to lack of a track record in the form of financial statements. This risky situation is often further compounded by the lack of proper collateral, in particular for small and medium-sized firms.

Figure 25



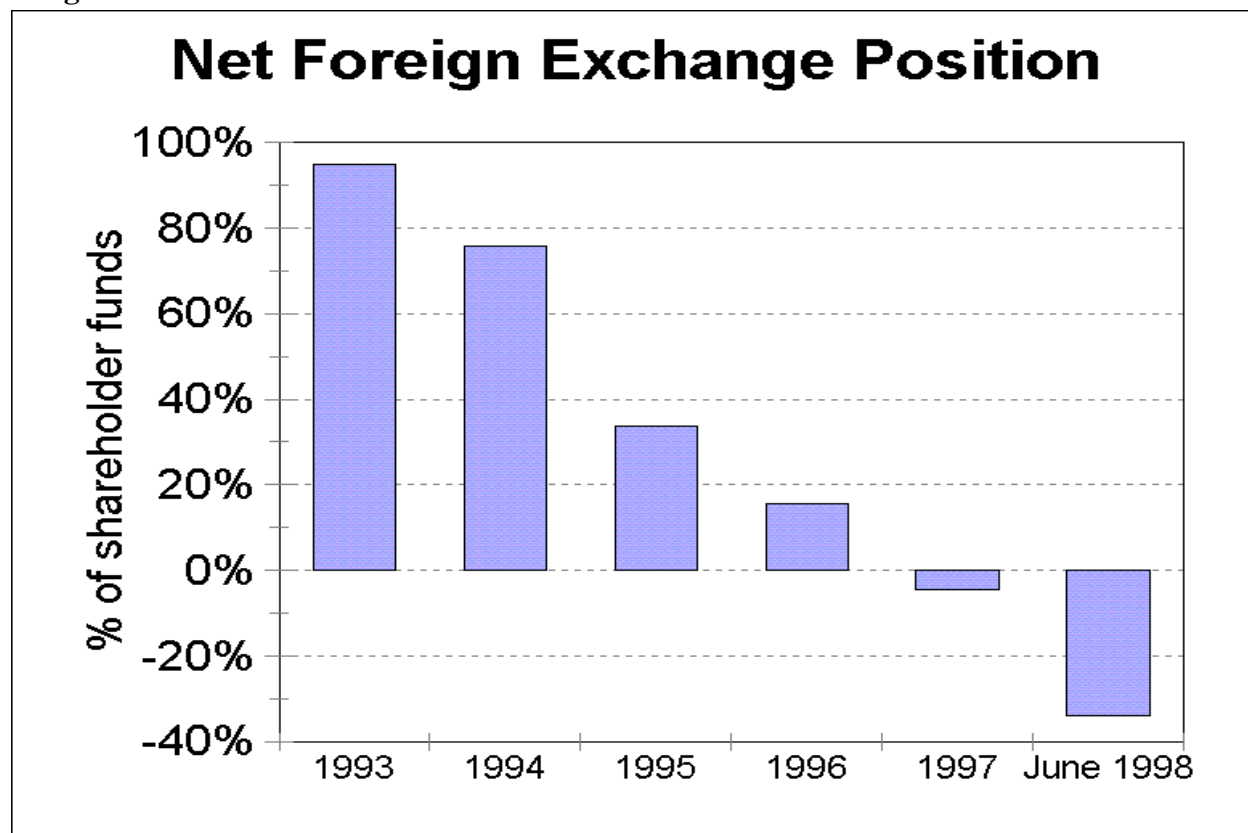
Source: International Financial Statistics

Note: Data for Sub-Saharan Africa are unweighted averages

Another characteristic of the current financial system in Ghana is the increasing dollarisation. Ghanaians are allowed to hold accounts in banks abroad as well as foreign denominated accounts in Ghana, with some restrictions. Foreign denominated loans are also permitted. The high domestic interest rates, in combination with a real appreciation of the Cedi from 1995 through late 1999, resulted in an increase in foreign denominated debt, since credit appeared substantially cheaper abroad. The Banking Act of 1989 did not establish any limits regarding foreign exchange exposure. However, as banks became more transparent, it soon became clear that foreign denominated debt was an issue that had to be reckoned with. In response to the increased urgency to regulate foreign exchange exposure of banks, a new law was introduced in December 1998. According to this new regulation, effective mid 1999, the net exposure shall not be more than 15 percent of the net worth of a bank for one single currency, while the total exposure limit is 30 percent. Given these limitations to foreign exchange exposure, the BOG does not appear to

be overly concerned with the risk stemming from foreign exchange exposure. Nevertheless, as Figure 26 shows, the foreign exchange position of banks, i.e. the difference between foreign liabilities and foreign assets as a ratio of total shareholders funds, has deteriorated substantially during the 1990s rendering the banks vulnerable to changes in the exchange rate. Also of concern, but more difficult to measure, may be the exposure of the customers of banks, although several interviewees claimed that they only extended foreign denominated credits to companies generating foreign exchange revenues.

Figure 26



Source: Ghana Quarterly Digest of Statistics

Note: Net foreign exchange position is defined as $(\text{foreign assets} - \text{foreign liabilities}) / (\text{total shareholder funds for commercial banks and secondary banks})$.

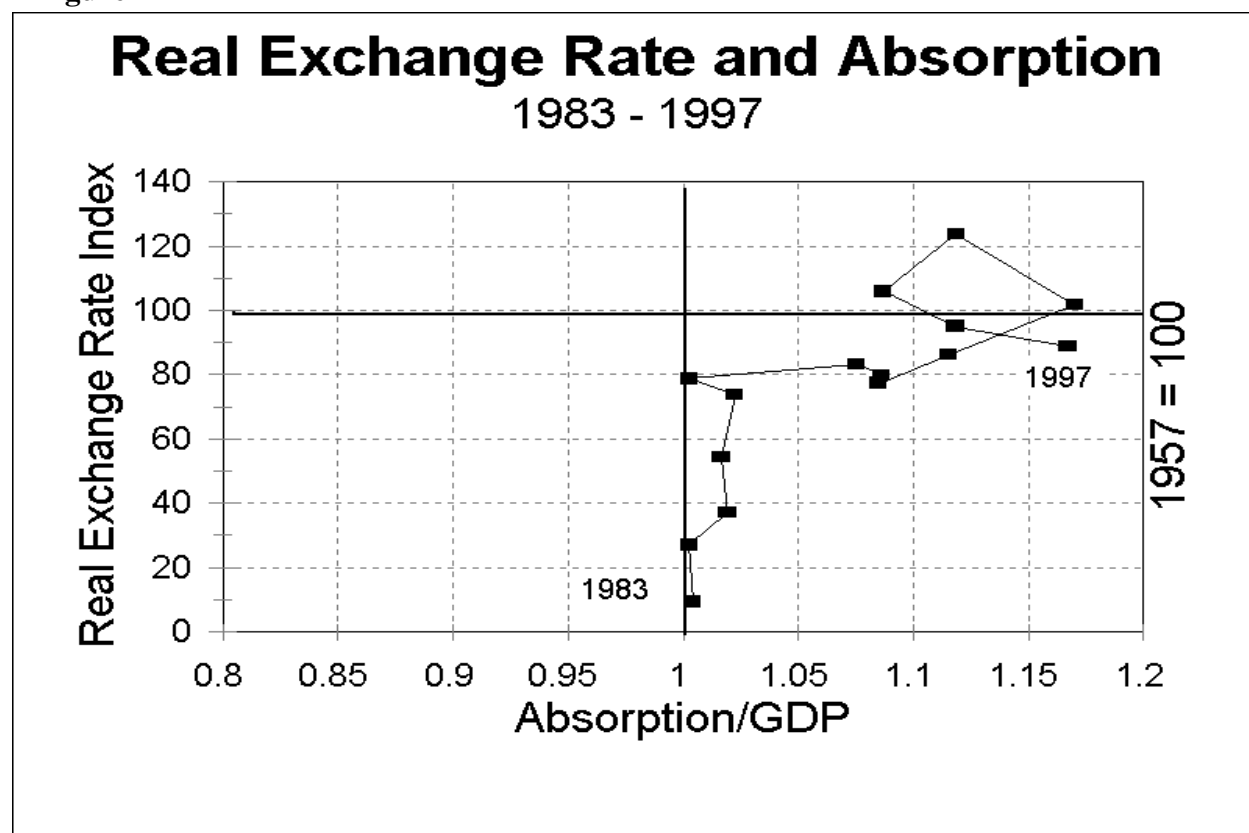
Internal and External Balance

A useful way of summing up the macroeconomic effects of the economic reform program is to consider the experience from the perspective of the internal-external balance type of model, first developed by Swan (1956). This approach maps the real exchange rate on the vertical axis, and

absorption on the horizontal axis. Each of the four quadrants has an appropriate policy stance, representing combinations of exchange rate and absorption policies. If, for example, the actual situation falls in the southeast quadrant, this would call for macroeconomic expenditure restraint combined with real depreciation of the currency.

The actual combinations of real exchange rate and absorption (relative to GDP) from 1983 through 1997 are mapped in sequence in Figure 27.¹ At the launch of the reform program in

Figure 27



1983, the principal problem was the vastly overvalued currency, reflected in the extremely low real exchange rate index. The effects of exchange rate reform while fiscal restraint was maintained are shown as the annual observations moved upwards dramatically without straying

¹ Absorption is mapped relative to GDP to facilitate easy comparison of the balance between absorption and income. For long run sustainability, absorption and income must balance.

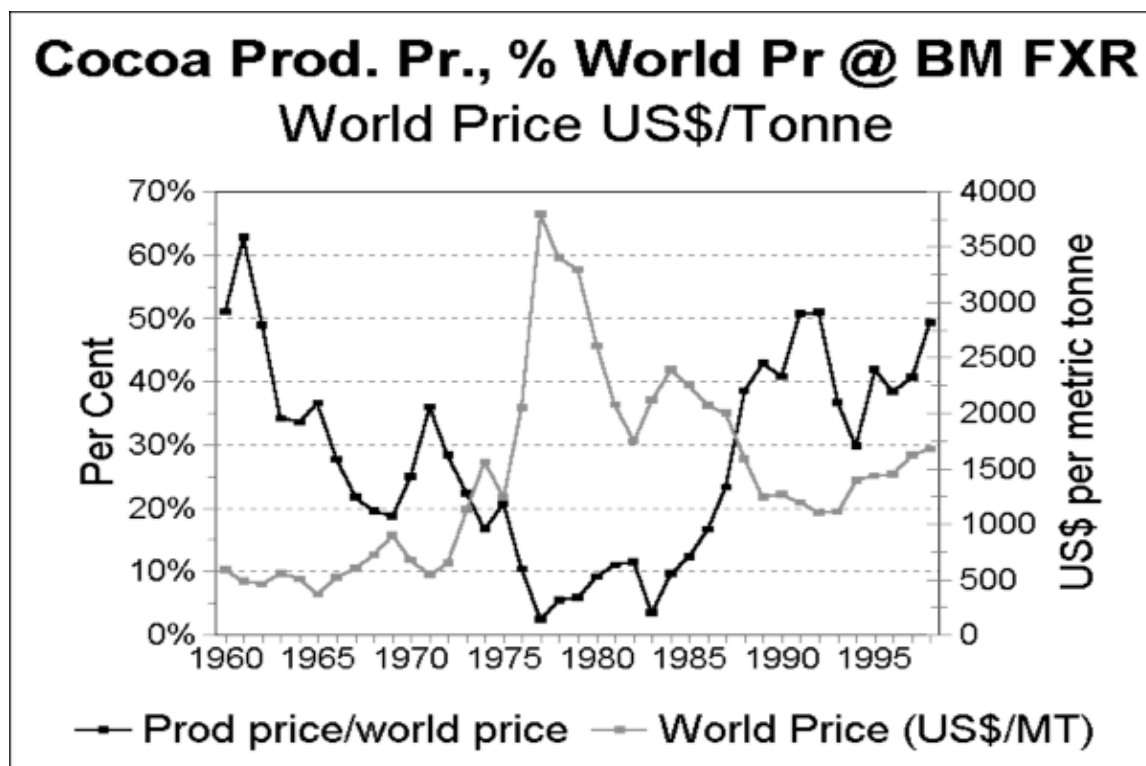
significantly to the right. However, before the real exchange rate had returned to its level at independence, the availability of foreign finance enabled domestic absorption relative to GDP to rise dramatically. From the cluster of observations for 1989, 1990 and 1991 at a real exchange rate index of about 80 and absorption of 1.07 to 1.08, the appropriate policy mix would have been further real depreciation of the currency accompanied by reduced absorption. Instead, we observe the launch of a circular sequence associated with the electoral cycle. In 1992 and 1993 absorption expanded, with some real depreciation. By 1994 the appropriate balance of policies was reduction of both absorption and the real exchange rate – which is what was done. However, the 1996 election and its aftermath saw real appreciation of the currency and expanded absorption.

In brief, of the two policy stances identified in this framework, the fundamental problem of getting the real exchange rate back in line was dealt with relatively successfully by the reform program, but achievement of a sustainable balance between absorption and income was not.

Cocoa

At independence cocoa was Ghana's principal export, providing a source of foreign exchange earnings, a source of income for peasant farmers in many parts of the country, and a source of government revenue. The deterioration of the cocoa sector prior to the reform program was thus a disaster on many fronts.

Figure 28



Sources: International Financial Statistics, Stryker et al., and Ghana Cocoa Board

Note: Producer prices are converted to current dollars at the black market exchange rate.

The reform program brought about a rapid increase in the real price of foreign exchange through 1987. This permitted the Cocoa Board to triple the real producer price by the 1987/88 crop year (Figure 10). The real producer price increase had the desired effect of reversing the decline of Cocoa Board purchases and export volumes.

Part of the recovery was undoubtedly a reduction of outward smuggling of Ghanaian produced beans to neighboring Cote d'Ivoire and Togo, for the producer price as a fraction of the world price at the black market exchange rate had also recovered rapidly under the reform program. (See Figure 28.) The reduction of smuggling was a real gain to the economy, eliminating the waste of resources used in inefficient transportation of the beans across borders.

Unfortunately for Ghana, the world price of cocoa declined in real terms during early years of the ERP. (See Figure 11.) This made it difficult for the Cocoa Board to keep the real producer price in Cedis at the level achieved for the 1987/88 crop year. However, more than simply passing through of the improved exchange rate was required to achieve full recovery for this important sector. The Cocoa Board was a bloated organization, with excessive staffing. It was slow to reform itself, for the same factors affecting the SOEs in general applied to the Cocoa Board.

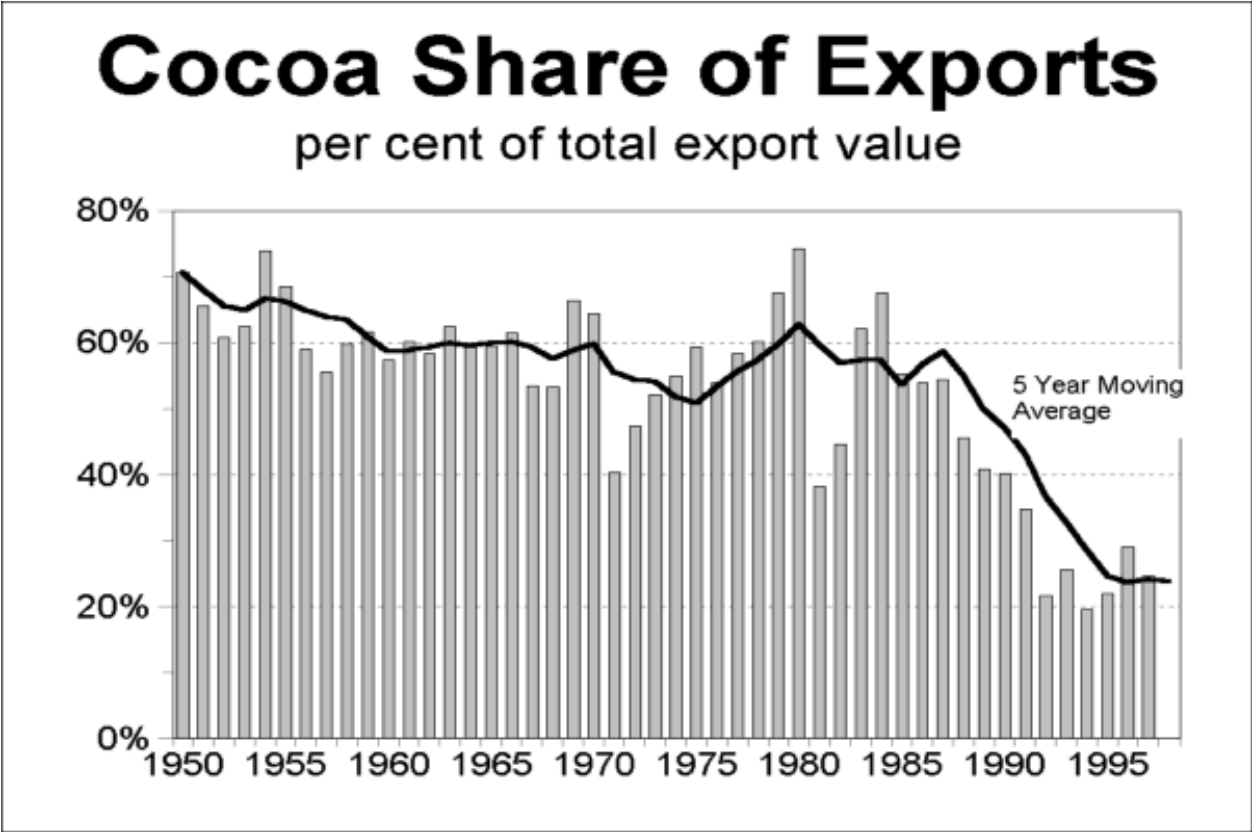
The apparent recovery of export volume from the depths of 1983 through 1985 stalled by 1990. For the next eight years the average export volume index was slightly less than the average of 1989 and 1990. This was scarcely surprising in light of the fact that the real producer price index in the 1990s declined by about 40% from its post-reform peak in 1987/88 to a trough in 1992/93 and 1993/94. It then only gradually moved back towards the post-reform peak in 1997/98.

The Cocoa Board's ability to increase the real producer price was constrained by low world prices, which in the early 1990s hovered at levels, in real terms, similar to the post independence trough of 1965. Then, just as there was some recovery in the world price, the real exchange rate of the Cedi appreciated, squeezing the real local currency margin which the Cocoa Board had to work with.

Yet something more fundamental was at work. There are many more interests and individuals involved in the cocoa sector than in other important sectors such as the minerals sector. These interests included not only the farmers (large and small), but also those engaged in the purchasing of the beans and transportation to the harbors, the research and extension services, the provision of infrastructure, the furnishing of finance, the marketing, and local processing. The PNDC government had found it difficult to achieve more than a pass through of the improved real exchange rate to the producers, and elimination of hoards of ghost employees. The elected NDC government found it even more difficult to reconcile the various competing interests in a democratic society, including its own desperate need for revenues. The inability to reconcile the competing

interests in the cocoa sector meant that recovery elsewhere in the economy left cocoa with a declining share of total exports (Figure 29).

Figure 29



Source: Leith (1974) and Ghana Quarterly Digest of Statistics

It was not until long after the 1992 transition to an elected government that the process of reforming the Cocoa Board itself gained momentum. After many years of dithering and repeated failure to reduce high costs in the cocoa sector, a comprehensive consultative process was undertaken in the 1990s, leading to the approval of a Cocoa Sector Development Strategy in 1999. It envisions:

- a doubling of cocoa production in a decade;
- building of new feeder roads and warehouses;
- better credit and payment facilities for the farmers;
- reliance on private buying of cocoa within the country;
- partial liberalization of the Cocoa Board's monopoly on external sales;
- elimination of the price discount given to local processors; and
- reduction of government's share to 15% of the fob Ghana price.

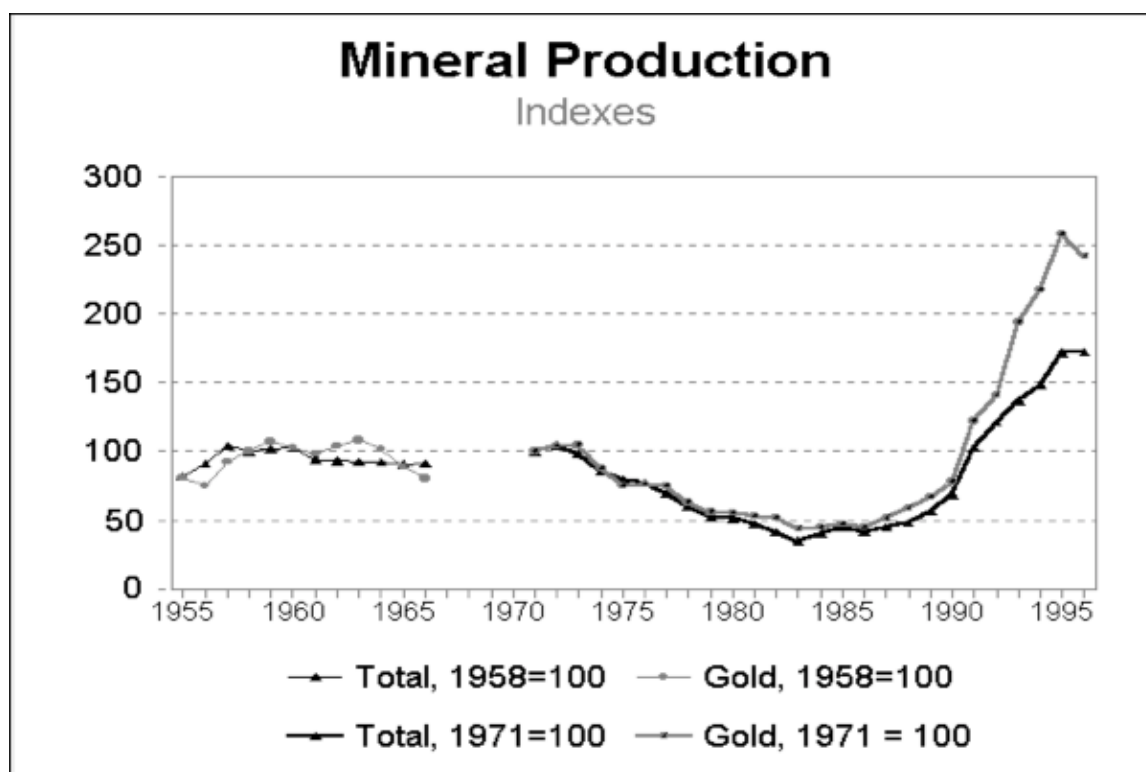
The production objective for the crop year 2009/10 is 700,000 tonnes, which is 30% more than the peak year of 1964/65 and 67% more than the average of 1960/61 through 1963/64. To achieve this ambitious objective will certainly require successful implementation of the targets noted. It will also depress the world price of cocoa, as Ghana's share of the world market at about 12% can still affect the world price. However, given a long run world demand elasticity that is smaller than -0.5, the demand facing Ghana is elastic, and therefore total revenue would rise.¹

¹ Blomqvist and Haessel (1972) estimate the long-run world demand elasticity to be -0.436. If we assume that there is no reduction of production in the rest of the world from a price reduction, then the elasticity of demand facing Ghana is $-(.436/.12) = -3.63$.

Minerals

Ghana's second most important export category had long been minerals, particularly gold, but also including bauxite, diamonds, and manganese. Mineral exports had been adversely affected by both the exchange rate and state ownership. Throughout the NRC/SMC government, the Limann government, and to 1983 under the PNDC, minerals production had declined, to the point that in 1983 it was less than 50% of Busia's last year in power, 1971. (Figure 30).

Figure 30



Source: Ghana Quarterly Digest of Statistics

In contrast with the erratic recuperation of the cocoa sector, the successful resuscitation of the minerals sector has been consistent and sustained. Exchange rate reform was important for the recovery of the sector, for virtually 100% of the improvement in the real exchange rate was passed through to the producers. However, in addition, an imaginative approach to institutional reform was critical. A Minerals Commission was set up in 1986, whose purpose was to promote the development of the sector. Some existing state-owned mineral enterprises were sold off, mostly to foreign investors. Taking a cue from other successful mineral based export economies, the Minerals Commission was able to negotiate arrangements with foreign investors that shared the returns

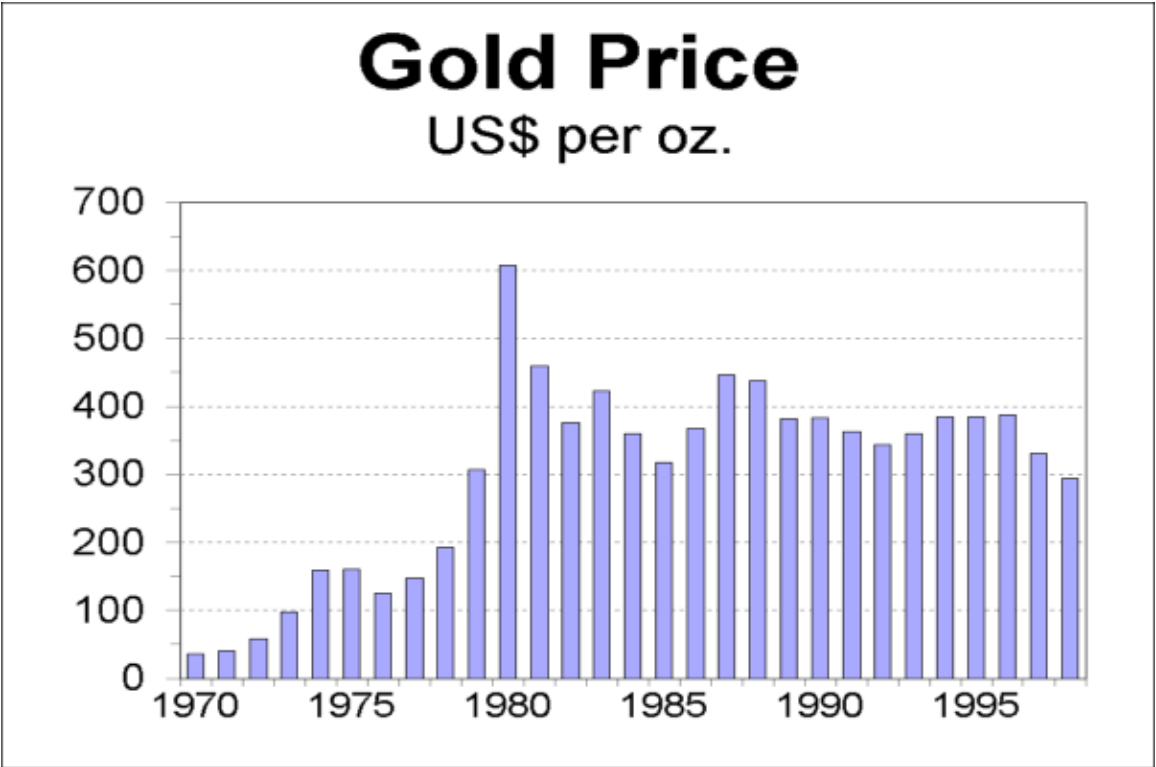
between the investors and Ghana. The overall result was dramatic.

The combination of exchange rate reform, privatization, and realistic royalty rates did wonders for recovery of the minerals sector under the PNDC. By 1992 total production in the sector, led by gold, had reached levels that exceeded those of the early 1970s. By 1991 gold production had more than recovered the level of two decades earlier, and in 1992 the value of gold exports exceeded cocoa exports, where it has remained since. The change-over to the NDC government did not halt the momentum of mineral sector growth to new output records. As the real exchange rate continued to appreciate through 1995, so too did mineral output and exports grow. Gold production in 1995 reached 2.5 times that of Busia's last year, and 6 times that of 1983. (Figure 30).

The world price has had an important impact on the gold sector. As the rehabilitation of the state-owned gold mines was gathering momentum in the second half of the 1980s, the world gold price began to recover from a relatively sharp drop during the first half of the 1980s. This undoubtedly contributed to the increased profitability of the sector (Figure 31).

Mineral production, once capacity is in place, typically has relatively low short-run marginal costs, because the cost of opening up the deposit has already been sunk (much of it literally sunk in the form of a mine shaft that has no alternative use). This makes it feasible to continue production at or near capacity for extended periods, as long as marginal costs are covered. With the real exchange rate reversing direction in 1996, and the fall in the world gold price beginning in 1997, the rapid growth phase of mineral recovery came to an end. The growth rate leveled off, but the sector did not shrink.

Figure 31



Source: International Financial Statistics

State-Owned Enterprises

The Background

Nkrumah had sought to modernize the economy and promote socialism via state-owned enterprises. He had added to an already important state presence in the modern sector which had begun in the 1920s as the colonial government had used the state to establish modern facilities ranging from railways to postal and telecommunications services. By the mid 1960s state owned enterprises were involved in a wide range of activities: from the production of boats, bricks, fibre bags, liquor, marble, paint, paper, steel, and sugar, to the running of enterprises engaged in farming, fishing, construction, gold mining, hotels, airway services, and wholesale and retail trade. The National Liberation Council (1966-69) had attempted to divest some of the enterprises, but in doing so left itself open to the charges, which still persist today, that it did not do so in a way that protected the public interest.² In the end only a small dent was made in the size of the sector. Busia's timid attempts at privatization had also drawn criticism, while Acheampong had further extended the role of the state in nationalizing various foreign owned companies during his early years, and Limann had done little to turn the tide.

Divestiture

Transformation of the state-owned enterprise (SOE) sector was a critical area for reform, if for no other reason than the sheer size of the enterprises and their low productivity. More than half of the value added and employment in the industrial sector (including mining) was reported to be in SOEs for 1987. (See Industrial Census 1987.) A similarly large presence of SOEs was evident in the

² See, for example, E.A. Agbodo, (Executive Secretary, Divestiture Implementation Committee):

"In our particular case, the established procedures have been designed to create such a high level of transparency as to avoid some of the accusations levelled against the implementation of the first divestiture program of 1966/67. ... Our search since 1992 to obtain particulars of those divestments has not yielded any positive results. We still do not know how the companies were valued, how many proposals or bids were received, how those bids were evaluated and above all, how much the companies were sold for."

"Divestiture Implementation Process in Ghana: Situational Context and the Way Forward," in Divestiture Implementation Committee, 1997, p. 24.

agricultural and service sectors, including banking. And, since state-owned banks owned significant shares of SOE equity, the state indirectly owned even more than the direct ownership figures suggested.

It was widely acknowledged that the only solution was divestiture. Yet despite the emphasis of the reform program on freeing up markets, divestiture of SOEs lagged behind other reforms. The reasons for the slowness in divestiture were many. Beginning with Nkrumah, the poor performance of the state-owned enterprises had been attributed to factors such as corruption and poor management, and not to the fundamental strategy itself. Hence, in this view, as long as corruption was under control, there was no sense that divestiture was central to achieving a vibrant economy.

Several specific reasons should also be noted. First of all, because of the overhang of the controversy associated with the immediate post-Nkrumah divestiture efforts, the PNDC felt it crucial to ensure that each enterprise would be properly valued before it was put up for sale (rather than rely on the willingness of purchasers to pay). This made the entire process far more complex than exchange rate reform, requiring large numbers of accountants and administrators to sift through the detail concerning the assets and liabilities about each company. Second, many SOEs in the past had promised generous termination benefits to their employees, but had not funded the liability implicit in that promise. Third, it did not appear possible for an SOE to declare bankruptcy even if it were effectively in such a position. Many worthless moribund companies simply remained on the books of the state. Fourth, the political dimension was never far from the surface. The PNDC itself was reported to be split on the extent of the divestiture, for the sales of SOEs would be either to local entrepreneurs who had enriched themselves under the old regime, or to foreigners. Finally, the very process of privatization constrains government's subsequent intervention in the economy. While the private sector would regard this as a plus, politicians would not necessarily do so. These various factors led to lengthy delays in deciding important issues such as how to proceed, and which enterprises should be retained.

A Divestiture Secretariat was eventually set up in 1987, but it was not until 1990 that sales were actually made. During the period 1990 through 1992 a total of 49 SOEs were sold. A further 26 were liquidated during the latter part of the PNDC rule.

The divestiture process quickened under the elected NDC government. In its first year (1993), the status of the Divestiture Implementation Committee (DIC) was formalized with the passage

of a law governing its mandate. The volumes of the different types of divestitures handled by the DIC are spelt out in Table 3 below. Payment for the acquisitions were not always 100% cash, and on a few occasions the purchaser defaulted on the installments and repossession occurred. Many of the enterprises divested had liabilities outstanding at the time of sale, particularly severance pay to workers. The proceeds of divestiture by the DIC were used first to discharge those liabilities, and then make payments to government. Most of these divestitures yielded only modest amounts to Government, cumulating to US\$172 million by the end of 1998, which amounted to less than ten per cent of exports for the single year of 1998.

Table 3:
Divestiture Results

(numbers of enterprises)

Mode/Year	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	Totals
Sale of assets				4	3	30	19	18	15	6	95
Sale of shares*				5	2	2	6	1	2	16	34
Joint venture				3	1	4	0	4	1	1	14
Lease		2	1	1	0	1	0	0	1	0	6
Sale- unspecified		16	17								33
Liquidation	12	10	2	2	5	5	6			2	44
Total	12	28	20	15	11	42	31	23	19	25	226
Total proceeds		14.5	32.5	28.4	5.7	47.3	6.1	21.9	7.2	8.5	172

(US\$ millions)

Source: Divestiture Implementation Committee

Note: * includes outright sale of companies

In addition to the divestitures handled by the DIC, there were a few major ones handled by government directly. These were: the substantial floatation of Ashanti Goldfields for US\$293.7 million to foreign investors plus 61 billion to Ghanaian investors; the sale of Ghana Telecoms for US\$38 million to foreign investors; and the sale of part of the government's shares in Ghana Commercial Bank and the Social Security Bank to the public for US\$16.6 million plus 44.1billion. The rehabilitation of each of these companies was essential for other elements of the recovery program -- the mineral sector, infrastructure renewal, and the financial sector reform, respectively.

The divestiture of the state-owned banks attracted substantial initial interest, but subsequently stalled, essentially due to the poor quality of some of the state-owned banks. (See Table 4 for the current structure of ownership of banks.) The partial privatization of GCB in 1996 was initially intended to include only 30 per cent of the shares, but strong public interest induced the government to increase its offer to 41%. The government has committed to sell off at least an additional 40 per cent, hence leaving 19 per cent of the shares with the state. Under Acheampong the government of Ghana had acquired 40 per cent of the shares in Standard Chartered and Barclays. All of these shares have been divested from Standard Chartered and in 1998 the government sold three quarters of its 40 per cent stake in Barclays. Plans are made to sell off a substantial part of the National Investment Bank, while the Agricultural Development Bank will remain fully in government hands.

Table 4:

Current Structure of Banking Sector

	Share of total			GOG/BOG ownership (%)	Proposed divestment
	Assets	Deposits	Employees		
Ghana Commercial Bank (GCB)	25.2	26.4	36	59.1	40
Social Security Bank (SSB)	13.6	14.3	15.2	5.3	
Standard Chartered Bank (SCB)	12.6	14.2	6.2	0	
Barclays Bank Ghana (BBG)	12.2	14.7	10.1	10	
Agricultural Development Bank (ADB)	9.4	5.2	9.1	100	0
Bank for Housing and Construction (BHC)	4.7	3.0	9.1	60	Liquidated
National Investment Bank (NIB)	4.5	3.0	5.3	30	30
Other	17.8	19.2	9		
Total	100	100	100		

Source: Market shares, refers to end of 1996 - Standard Chartered (1997). Ownership – Standard Chartered (1997), IMF (1999) and Letter of intent to the IMF, (1999)

Note: the GOG/BOG ownership only refers to direct ownership and ignores shares held by the SSNIT.

One of the major criticisms from institutions such as the IMF is that the divestiture of state owned banks, and the liquidation of weak banks, has not progressed rapidly enough. The Ghanaian government does maintain that it is committed to remedying this shortcoming. In its letter of intent to the IMF (1999), the government stated that it intended to divest all remaining shares in financial institutions other than the ADB, without giving a precise time frame. Moreover, shares in banks

owned by the BOG are to be divested before the end of 1999.³ In addition, all banks not satisfying the capital adequacy ratios would have their licenses withdrawn.

At the same time, it is worth noting that certain state-owned enterprises have been reserved from divestiture because of their “strategic” importance. Some observers interpret this as political patronage, noting that officials who manage these institutions know that their tenure depends on the NDC party, and act accordingly. (See Gyimah-Boadi 1999.)

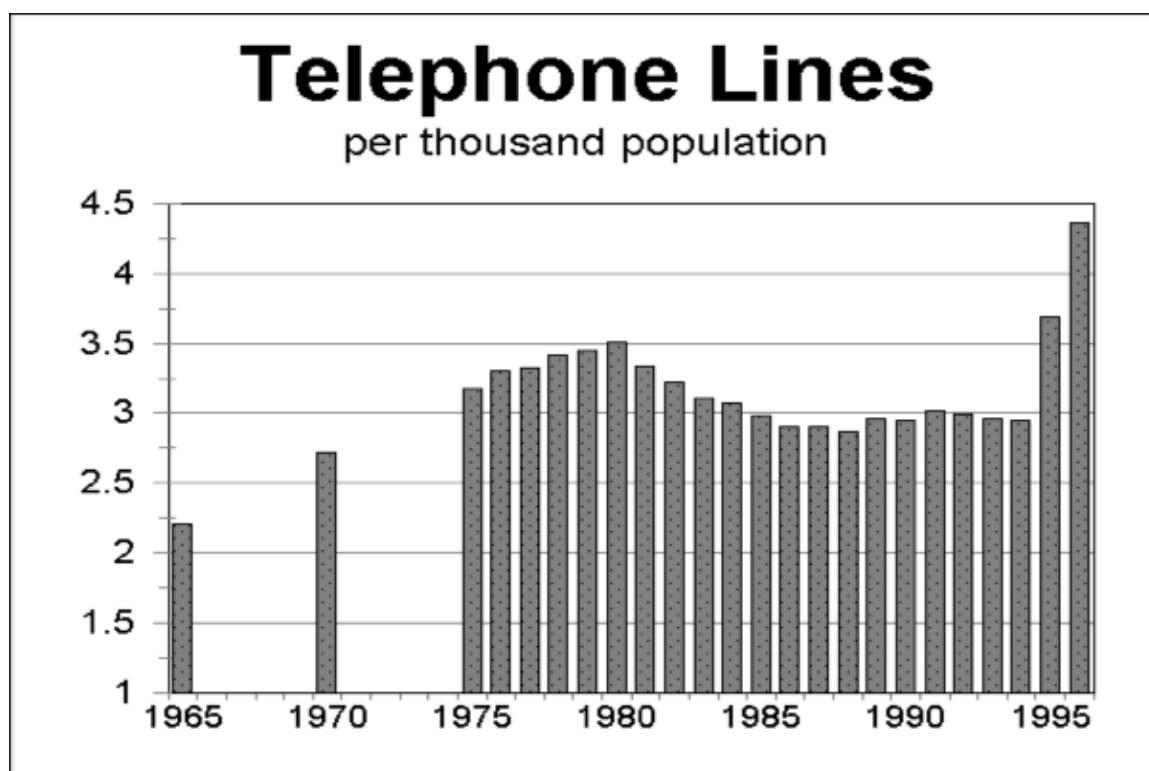
In sum, while slow to gather momentum, the divestiture program finally moved forward under the NDC government. The DIC is remarkably open about the details of the procedures and results of sales. The mode of sale, the purchaser, the purchase price, and any balance owing are all public information. A seminar for members of the parliamentary committees of finance and public accounts was held in late 1997, and the proceedings have been published. (See DIC 1997.) While questions remain about some details (see, for example, Ayee 1998), there are now several stories for the DIC to tell of successful former state owned enterprises.

³ The anomalous nature of this situation was, of course, recognized by the government and the central bank. But with so many items on the agenda for financial sector reform, this matter had not reached the top of the pile on its own.

Social Infrastructure

A significant element in the economic recovery was the restoration of the social overhead capital. While data documenting the deterioration of the social infrastructure are scarce, the anecdotal evidence is overwhelming. Prior to the recovery program the road and rail transport system had become so decrepit that it would take days either to move the limited imported goods inland or to get agricultural produce to market. Roads might be recorded in the ministry as paved and in good condition, but they were virtually impassible. The railway tracks and rolling stock had all but broken down. Similarly, the telecommunications system was no longer functioning. Telephone instruments and lines, while recorded on the books of the telephone company, no longer worked. The officially recorded data on telephones and rail traffic prior to the launching of the ERP in 1983 are reported in Figures 32 and 33

Figure 32

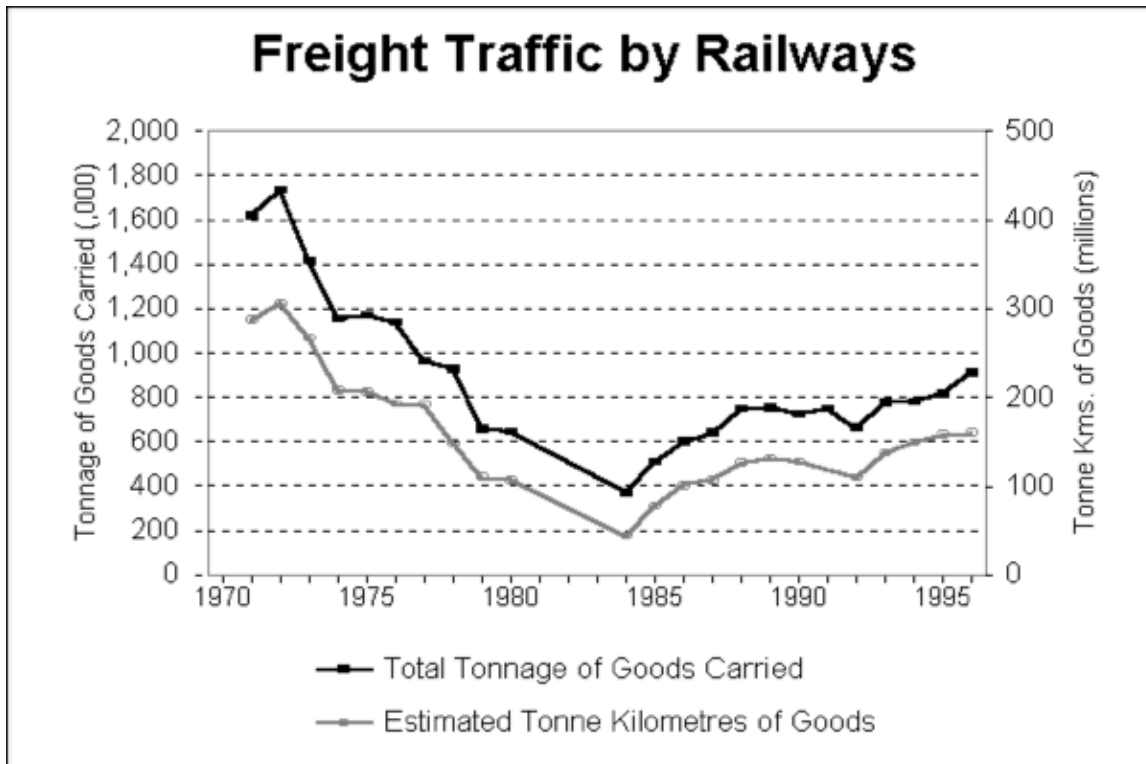


Source: Ghana Quarterly Digest of Statistics

The reform program was instrumental in turning these around. Roads were rebuilt, and many repaved. Rail lines were rehabilitated, and the rolling stock renewed. Telephones that work are

now widely available. The national electricity grid has been extended to many areas of the country that were formerly not served. In light of the true situation prior to 1983, the rehabilitation of the social overhead capital since then has been far more dramatic than the official data suggest.

Figure 33



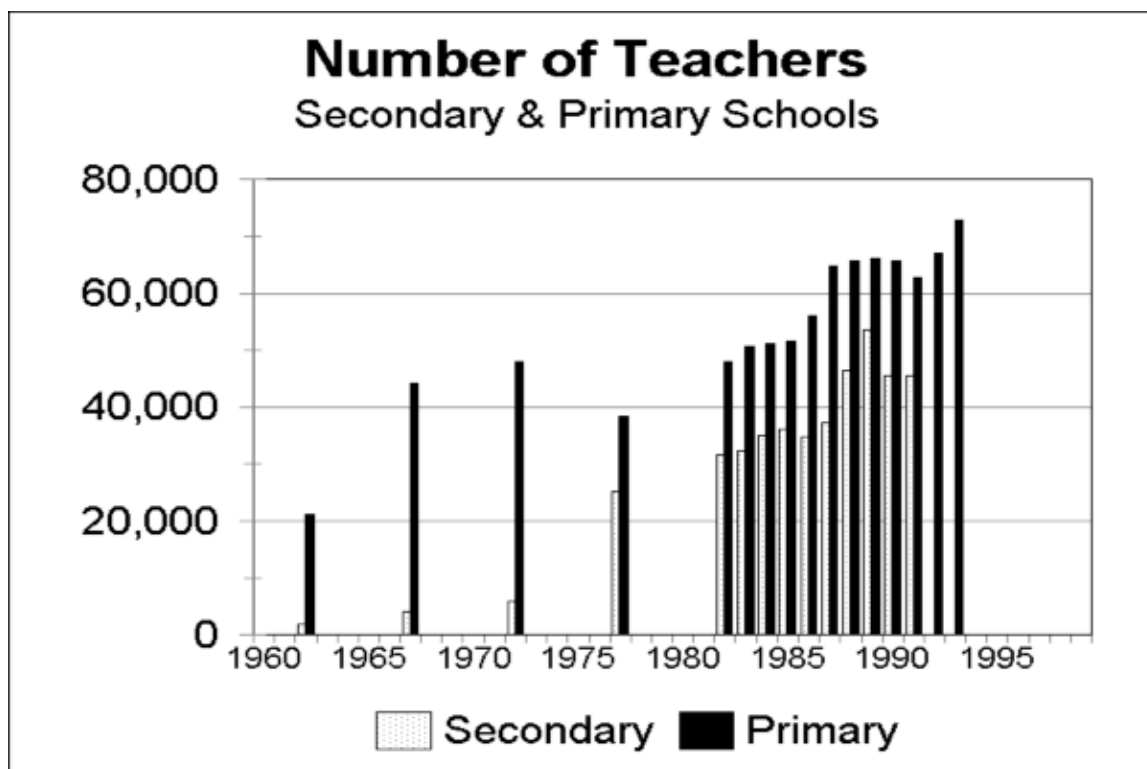
Source: Ghana Quarterly Digest of Statistics

Human Development & Income Distribution

The reforms also had major implications for income distribution as well the public provision of services such as education and health care, primarily through the availability of more funds, including foreign capital. Data is very scant, in particular regarding poverty and health and our assessment will accordingly be somewhat impressionistic. Data on education suffers much of the same weaknesses as the data on infrastructure referred to above. While enrolment rates may have continued at levels indicated by the available data even during the worst years of economic decline, it is beyond doubt that the deterioration of the quality of education was severe, due to lack of teachers, books and other materials. Moreover, even if the quality aspect of education in Ghana could be accounted for, the enrolment rates would still not correctly reflect their impact on the stock of human capital, inasmuch as many educated Ghanaians – including teachers - left the country. This is not to say that the data on school enrolment are without value, only that they should be interpreted with much care. This is probably particularly true in the case of Ghana.

The general rise in government expenditure made possible by the economic recovery in the 1980s and the inflow of aid, did not exclude social spending on education, health and social welfare. According to Roe and Schneider (1992), spending on social functions increased from 30 per cent of total recurrent expenditure in 1983 to 48 percent in 1989. Spending per primary school pupil more than doubled from 1984 to 1990 (WDI, 1999). Undoubtedly, given the fact that lack of funds was the main reason for the deterioration of health and educational services prior to the reforms, this increase in spending has helped improve quality in both areas. The number of teachers increased during the 1980s, both for primary and secondary school (Figure 34). Meanwhile, recorded enrolment rates both in primary and secondary school were stagnant or even declining during the 1980s. (See Figures 35 and 36).

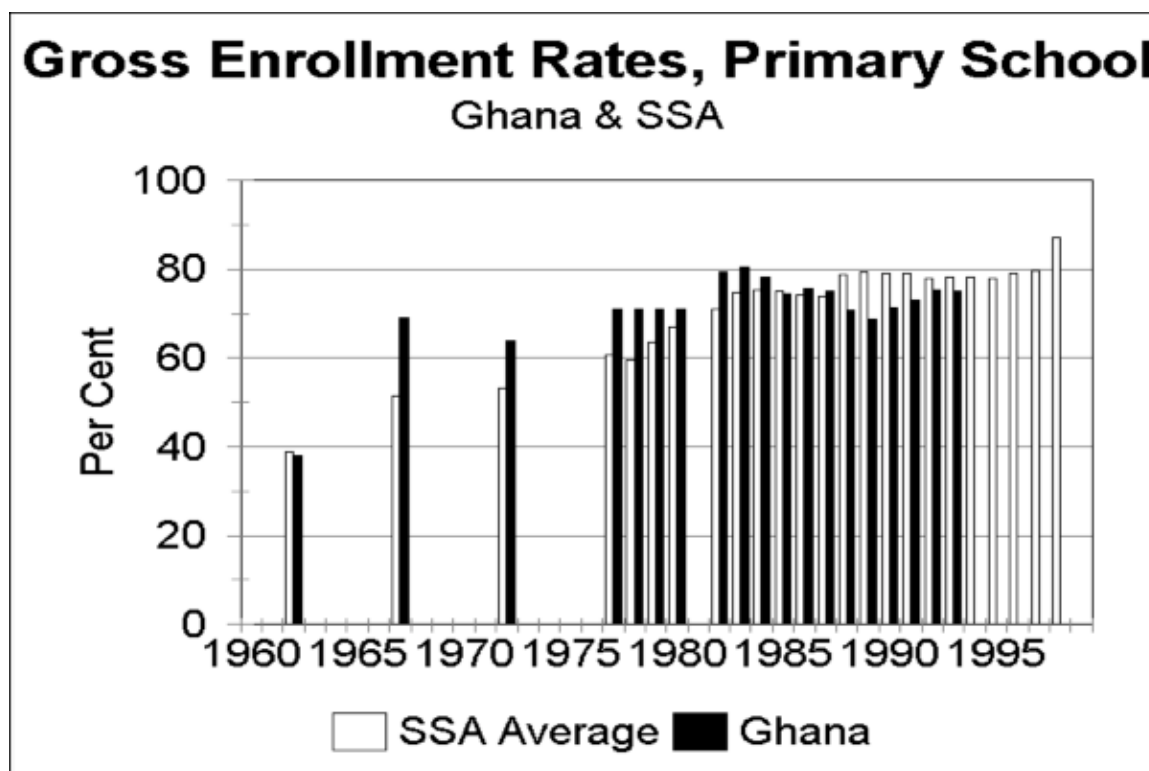
Figure34



Source: World development Indicators

Education during the period after 1990 is more difficult to assess due to lack of data. Concerns about the quality of education continue to be raised, notably by the UNDP Ghana Human Development Report (1997). According to the latter, only a small fraction of primary school pupils met certain criteria regarding literacy and numerical skills as measured by tests carried annually since 1993, although the results have shown a moderately improving trend since. Not surprisingly, the rural areas scored worse than the urban areas. These type of tests are inherently subjective, and the short time span covered only allows us to draw tentative conclusions regarding the modest improvement of educational quality during the 1990s. The Core Welfare Indicators Questionnaire (CWIQ) survey from 1997, indicates that lack of teachers and books are still the most important reasons for dissatisfaction with primary education, in particular among the rural poor. During the same period, spending on health has largely been stagnant as a share of GDP (see Figure 37).

Figure 35

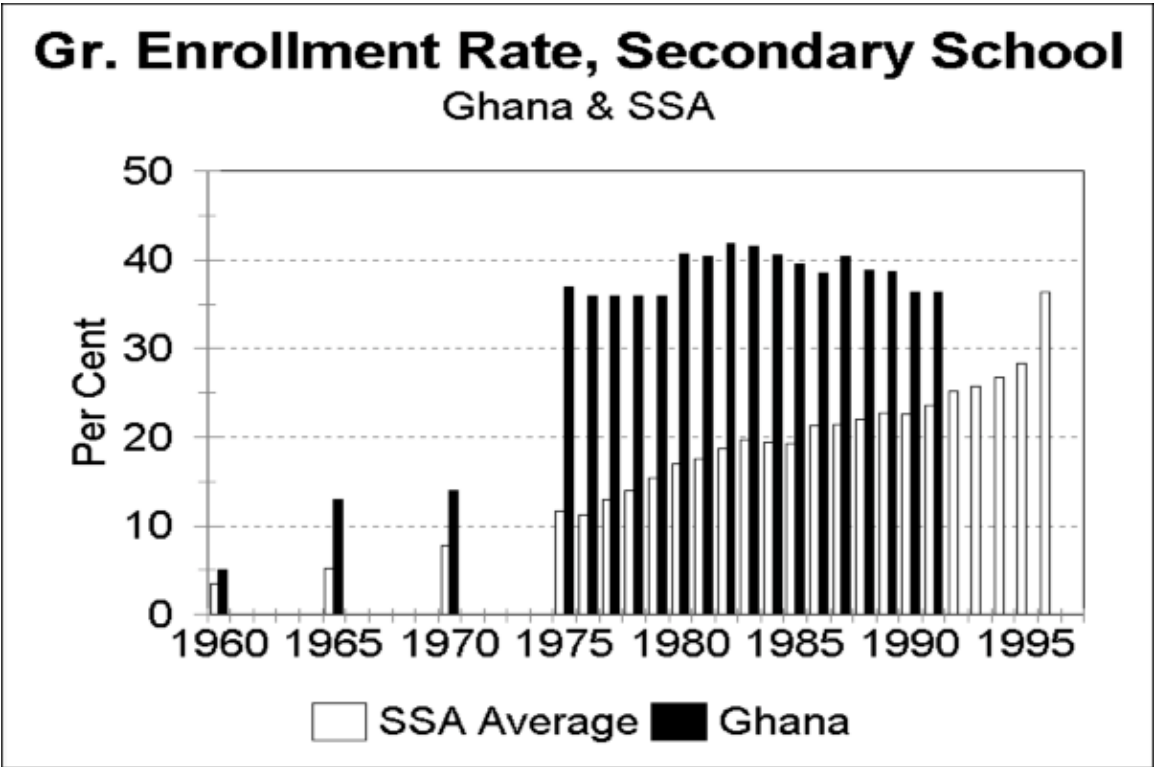


Source: World Development Indicators

The macroeconomic policies before the reforms had important distributional implications. The high inflation made it extremely costly to hold cash. In addition, the shallow and distorted financial system did not provide any investment opportunities by agents relying on occasional receipts of cash. As an example, cocoa farmers sold their annual crops for cash, which they had to rely on to support themselves with until the next annual harvest. By consequence, they and other heavy holders of cash became very vulnerable to the impact of inflation eroding their income with time. The population depending on cash in this manner was predominantly the rural poor. Hence, the malfunctioning of the financial system in conjunction with the high inflation had severely negative effects on income distribution, hitting the poor the most. For the cocoa producers, this effect was added to the effect of being heavily taxed through low producer prices and the overvalued currency. These considerations have been mitigated, albeit not eliminated, by the reforms. Inflation has been brought down, temporary spurts notwithstanding. The possibilities to use the financial system as protection from inflation are still limited however, due to the generally poor state of the rural banks. Further, since the rents attributable to the control system essentially benefited the urban privileged groups, it is reasonable to assume that the elimination of these rents has worked in favour of more

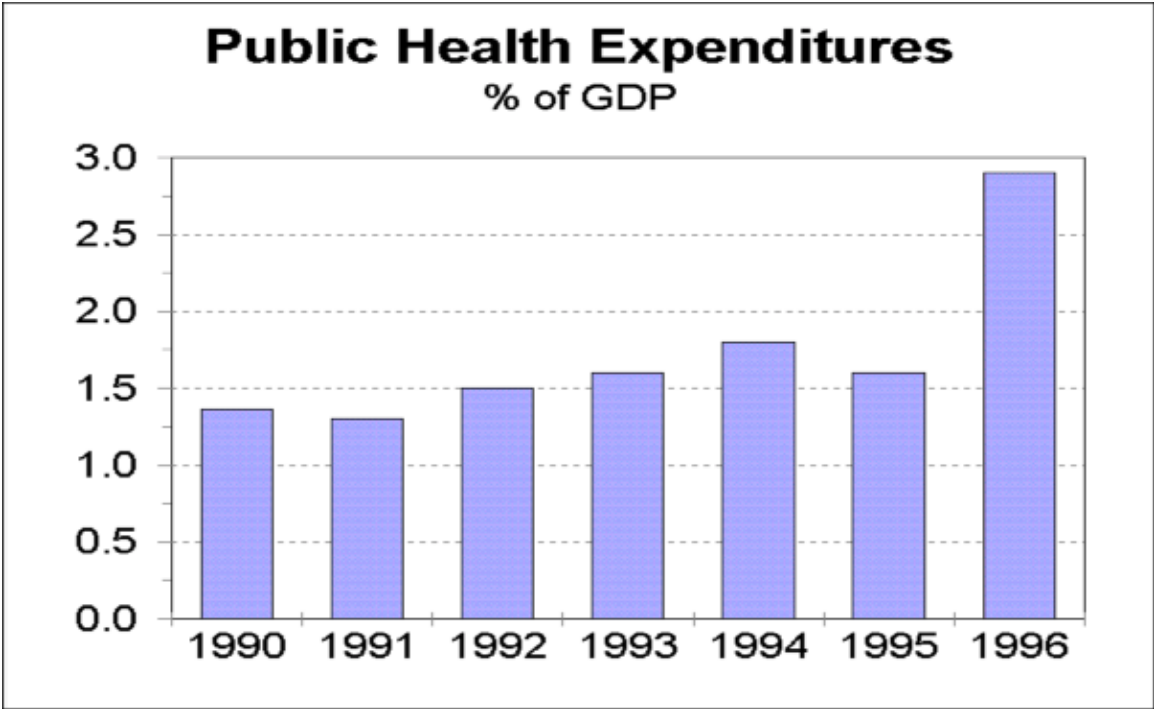
equitable distribution.

Figure 36



Source: World Development Indicators

Figure 37



Measuring the Reform Program's Success

The reform program stopped the slide of the economy. Using the most common measure, GDP per capita, the nadir was reached in 1983, with the economy on a recovery path since. Yet that recovery has been relatively modest, for per capita GDP in Ghana today is no better than it was in the early 1950s, and is still significantly below that of the early 1970s, before the downward spiral began. Why has there not been more progress?

A useful way of looking at the issue is to consider an aggregate production function, where inputs of capital and labour produce real GDP. In this framework, growth of GDP per worker arises either from increases in capital per worker or from increases in total factor productivity. Thus, there are two potential reasons for the failure to return to former income levels.¹ One is that investment in the economy has not restored capital per worker to its former level, and the other is that total factor productivity has not fully recovered to the levels achieved in the earlier periods. The division between these two can be sorted out by carrying out a growth accounting exercise, which follows.

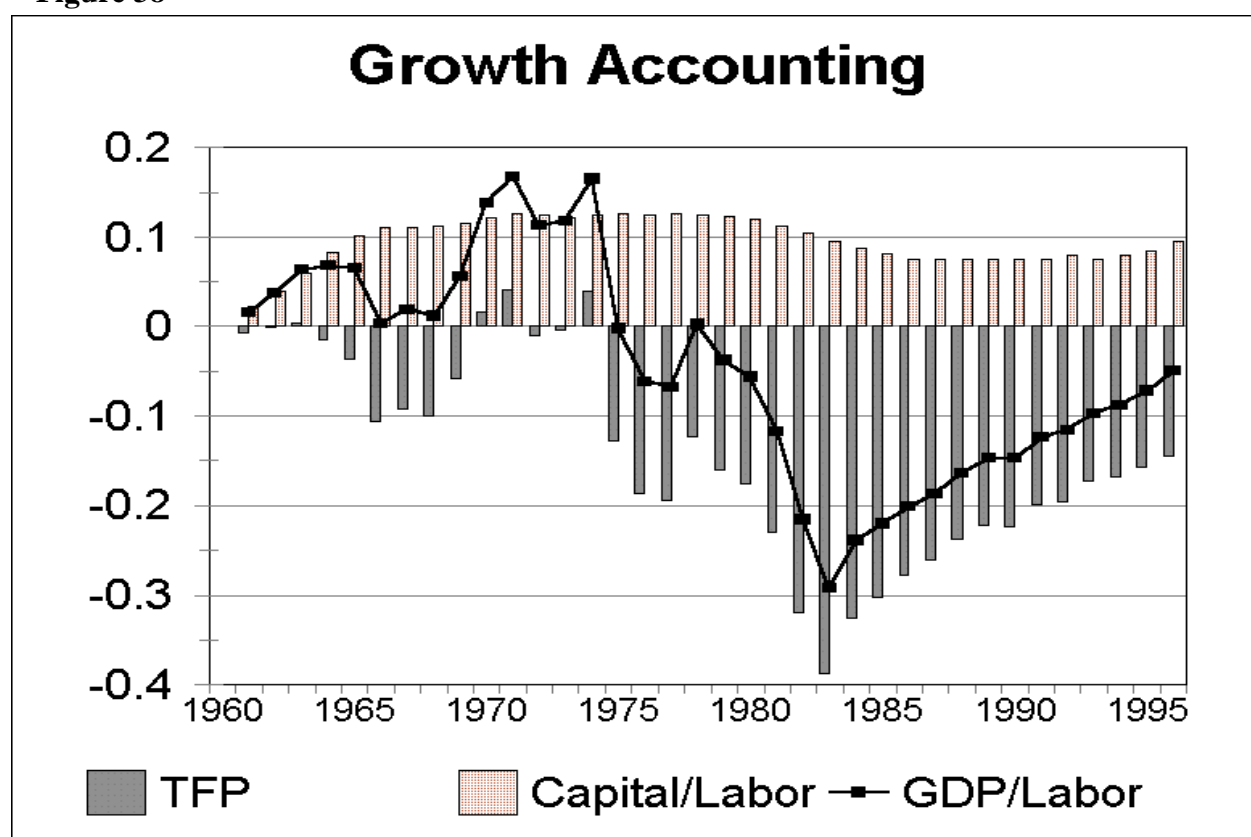
Growth Accounting

Several approaches to growth accounting are conceivable. One is to estimate an aggregate production function for the economy of Ghana, and apply the estimated coefficients for capital, labour (and any other factors of production), to compare the growth of factor inputs against the growth of output. This proved impossible, due to the weak statistical significance as a result of the limited degrees of freedom. A second option is to employ a panel consisting of various countries in a time series regression. This method has the advantage of allowing for inclusion of more explanatory variables without compromising their statistical significance. Moreover, it provides a good framework for simulations of future growth scenarios. This was the method employed by Berthélemy and Söderling (1999). The obvious drawback, however, is that the production function estimated for the panel of countries, even after accounting for country specific trends and dummies, may not be an appropriate representation of a single country's aggregate production function.

¹ It should be noted that output per worker and output per capita are not exactly the same thing. If the population growth is faster than the number of workers, then per capita GDP will not grow as fast as output per worker.

In order to avoid possible bias from other countries, we opted for a simpler, less detailed method, distinguishing only between capital deepening and total factor productivity growth to explain changes in the GDP/labour ratio. For this purpose we assume a Cobb-Douglas production function in the two production factors capital and labour. We further assume constant returns to scale. The capital coefficient is then given by factor shares. The labour share is the average labour income as a ratio of GDP between the years 1956 and 1969. During this period trade restrictions were relatively modest (with the exception of 1964-67) and bias from lack of foreign exchange is therefore limited. Data were drawn from Brown (1972), for which the labour share was 0.77, implying a capital coefficient of 0.23. This rather low capital coefficient may be explained by excess capacity, including SOEs and mining facilities.

Figure 38



Source: Authors' calculations. Capital stock and real GDP drawn from Nehru and Dharehwar (1993), extended after 1990 by investment series from WDI. Labor force from African Development Indicators.

The growth accounting results are displayed in cumulative form in Figure 38. The evolution of the GDP/labor, indexed on the 1961 level, is shown as the solid line. The two bars represent the determinants of growth: (1) capital deepening, and (2) total factor productivity. Capital deepening is measured as the capital to labor ratio, also indexed on the 1961 level and multiplied by the estimated capital coefficient (0.23). Total factor productivity is calculated as a residual. The height of a particular bar represents its cumulative contribution to real GDP/labor growth since 1961.

The economic decline to 1983 is clearly detectable from Figure 38. Moreover, although growth has been impressive since 1983 real GDP per worker was still below its 1961 level in 1996, and well below its peak at the beginning of the 1970s. The low rate of net investment since the beginning of the 1970s is evident from Figure 38. The ratio of capital to labor was stagnant during the 1970s, indicating that the capital stock was merely keeping up with growth of labor. In the early 1980s, as a result of the investment rate reaching a level as low as four per cent of GDP in 1982 (Figure 12), the capital/labor ratio declined.

Despite the elimination of some of the extreme distortions, such as the foreign exchange black market premium, in the 1990s investment remained relatively low (Figure 12). Further, a substantial portion of the investment that did occur appears to have been financed by foreign assistance, some of which was grant money and soft loans. Private domestic investment remains low, apparently hampered by the lack of long term credit facilities and the unstable macroeconomic environment.

The efficiency of the economy, or the amount of output generated per unit of factor inputs, has still not caught up with its level at the beginning of the 1960s. This is seen by the accumulated change in total factor productivity, which was still negative at the end of the series. In sum, the reform program was able to yield a small increase in the capital/labour ratio, and a larger increase in total factor productivity. Together, these two outcomes of the reform program have generated a modest increase in GDP per worker.

Much of this growth record can be explained by the waxing and waning of market distortions and macroeconomic uncertainty. These had both a direct impact on Ghana's economic performance, and no doubt contributed to the low level of investment in the country. In light of this, the deterioration of the fiscal balance from 1992 onwards, leading to macroeconomic instability and

real exchange rate appreciation, suggest that one of the major reasons for the slowing of total factor productivity growth in recent years is the reappearance of distortions. Even though the extremes of the foreign exchange black market premium were down to single digit levels for the first time since 1961, other distortions remain. Both labour market and financial market distortions are significant, but are more difficult to tackle. In this sense the easier work has been done and future growth will be more difficult to achieve.

3. Conclusion

Ghana's turbulent economic and political history contrasts sharply with the great potential that the country exhibited at independence. What went wrong? With over forty years of experience, scholars today are in a position to begin providing an answer that question. Inevitably, the answer has many dimensions -- cultural, economic, political, and social -- and within each dimension there were numerous complexities, all of which were interacting with each other. To contribute to a better understanding of the economic dimension, this study has focused on the determinants of Ghana's long-term economic growth performance. The principal purpose of this chapter, then, is to sum up what we have learned about the determinants of Ghana's long term growth.

At the most basic level, Ghana's economic atrophy to 1983, and modest recovery since the launching of the reform program, are attributable to the combination of weak investment and low productivity. This was spelt out in the growth accounting analysis contained in Chapter 2. The low investment rates, in the presence of rapid labor force growth, have meant that the capital/labor ratio today is only on a par with that achieved at the time of Nkrumah's overthrow in 1966. Further, the productivity of labor and capital continue to lag substantially behind the levels achieved in the early years of independence.

But why have investment rates and productivity been low? The answer to that question is much more complex. It involves economic policy failures and political failures. In what follows, we trace various economic and political themes which, with their variations, repeated throughout the story of modern Ghana, help explain the economic performance.

With a clearer understanding of the economic and political past, and expectations concerning the nature of the political regime emerging in the year 2000, it is possible to contemplate what the future might hold. One way of doing that is to project various potential future scenarios, based on plausible values for key economic variables. This permits us to examine the feasibility of various future scenarios that have been proposed, such as Ghana's official Vision 2020, and to identify the policy thrusts that would achieve sustained high growth for Ghana.

Economic Policy Themes

There are four major policy themes that run through the last half century of Ghana's modern history: excess demand, currency overvaluation, and anti-export bias, and financial repression. Each has had a major impact on the outcome.

Excess Demand

The first theme is excess demand. Repeatedly, from the days of Nkrumah onwards, fiscal and monetary policies failed to control excess demand. Some bouts were worse than others, and there were some periods of restraint, such as under the NLC following Nkrumah's overthrow. But the overwhelming effect for several decades has been that no Ghanaian has been able to count on a stable macroeconomic environment beyond the immediate horizon.

The principal source of excess demand was the government budget. Prior to independence, government expenditures were kept at a steady share of just under 10% of GDP, while fluctuations in government revenues, due mostly to variation in cocoa tax receipts, were simply absorbed by the government's bank balances. But from independence on, control over government's expenditure and net lending evaporated. This changed briefly during the first few years of the reform program, but today remains the central problem. In the meantime, from the early 1960s onwards, government revenues were stuck at considerably less than expenditures. As overvaluation of the currency became more serious, the tax revenue base was badly eroded. This occurred in the late Nkrumah era, and even more seriously from the mid-1970s until the mid 1980s.

The investment rate was generally negatively related to the government budget deficit. The channels for this relationship were many, but the most important were the following:

- (1) The unstable macroeconomic environment generated uncertainty, adversely affecting the private investment climate and the profitability of investments once made.
- (2) Government's own investment was curtailed by its shrinking ability to raise revenue, either by taxes or foreign borrowing.
- (3) The lack of essential infrastructure and services normally provided by government, such as roads and schools, further constricted the economy and government's revenue.

Monetary policy was seldom used to restore macroeconomic balance. Rather, the government budget deficit was frequently financed by credit from the banking system, with consequent high money growth rates, inflation, and inflation tax. Until the reform program was launched, real interest rates were seldom positive, and often highly negative. Even with the reform program, real interest rates have not remained consistently positive.

Currency Overvaluation

The second explanatory theme is exchange rate policy. Excess aggregate demand interacted with a fixed exchange rate to create excess demand for foreign exchange. When the reserves were depleted, the resort to controls in 1961 set in motion the first round of currency overvaluation, shrinking exports, declining imports, and falling government revenues. The overvaluation of the Cedi was reversed only temporarily by devaluations in 1967 and 1971. The cycle repeated itself in more extreme form during the 1970s. The reform program brought a major reversal, finally restoring the real exchange rate to its level at independence in the early 1990s. However, this proved only temporary, as the real exchange rate fell back dramatically in the 1990s, eventually recovering in late 1999.

The level of the real exchange rate clearly affected the real economy, both by directly affecting the volume of international trade and indirectly through the government revenue received from taxes on international trade, and hence the budget deficit. The considerable instability of the real exchange rate also played an important part. Export and import competing producers have both faced substantial uncertainty about their real returns throughout Ghana's modern history. That uncertainty has remained in the 1990s, which reduced the gains from reopening the economy to international trade. The potential of the tradeables sector to serve as an engine of growth was thus diminished.

The interaction between the real exchange rate and government revenue merits special emphasis. The base for much of government's revenue was denominated in foreign exchange at the official exchange rate. Import duties and the cocoa export tax accounted for well over 50% of government revenue into the 1960s. Excise duties were augmented substantially in the 1960s, but these were levied almost exclusively on importables. These three together thus accounted for over two thirds of government revenues in almost every year until the reform program was launched. The failure to maintain the real exchange rate at a competitive level meant not only that the volume of exports and thus imports was restricted, but that the valuation for tax purposes was

vastly understated. It is no wonder, therefore, that until the late 1980s government revenues paralleled the real exchange rate.

Bias Against Major Export Sectors

Third, over the decades Ghanaian policy ignored the potential gain from focusing on the nation's comparative advantage in its traditional export sectors. These sectors suffered not only from overvaluation of the currency, but also from various elements that have systematically discriminated against them.

The best known is cocoa, where the real producer price, even fifteen years after the launching of the reform program, has not recovered to the levels of the early 1960s. The cocoa export tax has always been much higher than optimal in light of Ghana's limited power in the world market. This, in turn, contributed to a substantial reduction of market share and hence a diminution of that market power. Reinvestment in research and development, and infrastructure in support of the sector has been inadequate. Inflation and financial repression were especially hard on the sector, and government's insistence on state involvement in the collection and marketing of cocoa absorbed a large share of the potential profit. The length of time it took to reach a consensus on a cocoa sector development strategy, finally launched in 1999, is indicative of the ambivalent attitude towards the sector.

The minerals sector has done better under the reform program, but was the victim of systematic discrimination before. In addition to currency overvaluation, state ownership of many of the mines, neglect of infrastructure, demands for costly local processing, and lack of geological survey information all kept the sector from achieving its potential as an engine of growth.

Traditional exports have also been victims of some considerable variation in the world prices, with prices falling, sometimes at inopportune times. The world price of cocoa in the late 1990s was half what it had been in real terms when the reform program was launched. The world gold price has also dropped by more than 25% over the same period.

Financial Repression

The fourth major theme is financial repression. The potential for the financial sector to support the growth of the real sector was systematically suppressed. The devices were many, ranging from administered interest rates and credit allocation, to state ownership of financial institutions, to

arbitrary confiscations of financial assets. These would have been damaging enough in their own right, but their potency was considerably amplified by inflation.

The reform program has removed many of the more egregious interventions in the financial sector. But given the ongoing risk of macroeconomic instability and real exchange rate instability, the financial sector is not well placed to manage business risk. Further, the shadow of the past remains, for the public continues to remain leery of holding Cedi denominated financial assets. The financial sector is not yet playing its potential role in mobilizing savings, evaluating innovations, and channeling funds into activities with promise for success. Consequently, the ongoing process of transferring resources from low productivity activities to high productivity activities, which is fundamental to increasing productivity, is hampered.

Political Themes

Politics has always been a key determinant of Ghana's economic policy. The precise mechanism, however, requires careful elucidation. We begin by looking at the overstretched state, and then turn to look at the effect of regime type on the economic outcomes.

Overstretched State

A fundamental fallacy took hold during the colonial era: the absence of entrepreneurs engaged in the modern sector required the state to assume the role. Nkrumah expanded on this thrust, establishing numerous state owned enterprises. The augmented role of the state was also cloaked in nationalist rhetoric, first by Nkrumah, and later by others, such as Acheampong in his indigenization decrees. Yet the very limited capacity of the state to effectively manage both these enterprises and the more traditional activities of the state was never addressed.

Most of the SOEs created by Nkrumah were kept under the wing of the state by subsequent governments, following the political furore associated with the limited post-Nkrumah divestiture. The cost of the huge SOE sector can never be fully assessed, but the sheer inefficiency and waste associated with a vast network of establishments facing no serious budget constraint explain a considerable part of the low productivity of the Ghanaian economy. In an attempt to reverse the drain of the SOEs on the rest of the economy, an ambitious divestiture program was planned during the early years of the reform. But because of the limited capacity of the state, the process was slow to commence and, while accelerating in recent years, is still incomplete.

Nkrumah also began to use the power of the state to redistribute income from the political losers to the political winners -- i.e., his supporters. The winner-take-all system of government meant that the political losers were also the economic losers -- permanently, until power was wrested by force. Acheampong continued to use the state to create economic winners and losers. But the insecurity of that regime left it unable to limit access to the rents which its policies generated. The principal industries in the country became rent-seeking and smuggling. Had the effects of the redistributive policies been confined simply to the distortions of adverse incentives, the damage would have been far less. The cost was much greater because rent-seeking also wasted real resources.

Repeatedly new governments would blame the sorry state of the country on their predecessors' incompetent administration. Never was there any recognition that a large part of the blame lay in the combination of the limited capacity of the state and the growth retarding economic policies pursued. Having blamed their predecessors' problems on incompetent administration, successor governments failed repeatedly to limit the role of the state to those activities that could be efficiently administered. Successive governments also failed to achieve a national consensus on priorities within that administrative constraint, taking on commitments that could only be met if the administration of other activities lapsed.

It was only after harsh experimentation that Rawlings realized new economic policies were required. Yet he remained a reluctant convert, deeply suspicious of the entrepreneurs who had responded to the incentives created by his predecessors – a suspicion which was mutually felt – and loath to withdraw the state from many of the activities that had overstretched it. The reform program thus floundered as it moved beyond the administratively easier reforms (such as the exchange rate) into more complex initiatives (such as divestiture). This, in turn, led the various donor agencies supporting the reform program to demand in ever greater detail specific administrative actions, leaving the Ghana government less and less the owner of the reforms.¹

Regime Type and Economic Growth

Some regimes were more successful than others at achieving economic growth, and some of those differences in outcome were clearly attributable to different economic policies, and not to regime type. On first glance economic outcomes appear not to have been affected by regime type. For example, it was the military regime of Generals Acheampong and Akuffo that presided over the largest drop in real GDP per capita, while it was the military regime of Flt. Lt. Rawlings that initiated the economic reform program that stopped the economic atrophy and resumed economic growth. Nevertheless, this does not confirm the null hypothesis. On the contrary, an important question remains: Independent of the economic policies pursued, did the type of regime itself affect economic growth?

Before examining the possible effects of regime type, it is useful to characterize the different regime types. The most useful taxonomy for our purposes is to distinguish regimes on the basis

¹ See, for example, the detailed list of actions required by the IMF, attached to Ghana's letter of intent dated November 3, 1999.

of the interest of the ruler(s). On this basis there is a central distinction between democratic and autocratic rule. In the former, decisions are taken by the ruler(s) on the basis of the perceived interests of the dominant group in the electorate. In the latter, decisions are taken by the autocrat on the basis of his/her own interests. There is a third possibility – anarchy, where there is no overriding rule, with each individual acting in his/her own interests. This taxonomy involves considerable oversimplification, and glosses over some significant subtleties that distinguish the different regimes, and different time periods within regimes. Nevertheless, it is a useful starting point.

Mancur Olson (2000) identified two general conditions that are required for a market economy to be successful: (1) well defined and secure property rights; and (2) absence of predation. Olson also showed that both an autocrat and a democracy have an interest in making the society productive, and thus to provide well define property rights and to limit the extent of predation by the regime. However, because the members of the ruling group in a democracy are also recipients of their share of society's income, the optimal rate of predation by the ruling group in a democracy will be less than in an autocracy. In the third possible type – anarchy – each individual has only an infinitesimal interest in the overall welfare of society, so has an interest in taking as much as possible for himself without any consideration for the effect on the total income. Anarchy provides neither well defined property rights nor absence of predation, and hence generally does not lead to economic growth.

Characterizing Ghana's Regimes

With this taxonomy in mind, it is useful to review the different regimes in terms of governance (democracy, autocracy, or anarchy); and the impact of each regime on the two keys to successful market economies (respect for property rights and the absence of predation).

Nkrumah took power at independence as the leader of a democratically elected government. Much of his policy thrust was redistributive, albeit in the name of producing rapid economic growth.¹ The relative returns to traditional economic activities such as cocoa, were reduced, in favor of modern sector activities such as SOEs, thereby creating a new vested interest. Nkrumah

¹ Killick (1978), for example, characterizes the policies pursued by Nkrumah as “development economics in action,” suggesting that Nkrumah was simply trying to implement the orthodoxy of the time.

skillfully used his leadership position to gradually transform his government into an autocracy which would not tolerate any dissent. In the process, the redistributive economic policies became increasingly predatory, and a new vested interest was created. Although the Nkrumah regime never formally confiscated property, it did initiate the use of several confiscatory devices – the inflation tax on cash balances, the use of the producer price of cocoa to levy a tax far in excess of the optimal export tax, and the use of import licencing and exchange control to deny access to importers deemed “non-essential”.

The NLC that overthrew Nkrumah in early 1966 was also autocratic. But it used its power principally to restore the pre-Nkrumah status quo, both in terms of economic policy and governance. The democratically elected Busia government that took over from the NLC continued the broad economic thrust initiated by the NLC. Debate over economic policy was vigorous, but few entrepreneurs anticipated the downward political spiral that was to follow. The economic reward for Ghanaian society was a short period of rapid economic growth.

The Busia government sought to reverse the redistribution set in motion by Nkrumah. It was not simply a matter of reversing his policy thrust, however. A large part of the modern sector owed its existence to the distortions that Nkrumah had initiated. Those policies had thus created vested interests in the distributive arrangements he had put in place. The broad thrust of the NLC and Busia governments to restore the balance, faced the opposition of those interests. The devaluation of late 1971 which, perhaps unwittingly, tipped relative returns dramatically against the military, triggered the return of a military government.

Initially the military government led by Acheampong focused on continuing the policy see-saw, simply reversing the policies of Busia. The most dramatic was the appreciation of the currency, but a variety of other autarkic policies – including “operation feed yourself,” and the indigenization decrees – were instituted as well. In addition, the regime became increasingly autocratic. The military officers, acting like autocrats the world over, took an ever larger share of the economic spoils for themselves. Had the evolution of the regime stopped at that point, the damage would have been similar to the damage sustained during Nkrumah’s autocratic period.

General Acheampong’s government gradually descended into economic anarchy. As Leith and Lofchie (1993) argue, this was due to a combination of: (1) failure to control access to the rents generated by the control regime; (2) a shrinking of the size of the rent pool due to the increasingly

autarchic policies; and (3) a political discount rate that rose rapidly as the regime remained longer and longer in power. While the military attempted to restore its luster by first renaming the regime, and later by replacing Acheampong with General Akuffo, the descent towards anarchy began to take its toll on the economy. Rights to reap the rewards from past investments in things like cocoa trees, or even the right to retain the real value of cash balances, were withdrawn by the cocoa pricing and aggregate demand policies respectively. The rents created by the excess demand were distributed by caprice, and could just as capriciously be taken away. Both the nature of the political regime and the economic policies thus contributed to the economic atrophy of the mid 1970s.

The events of 1979, including the asset confiscations under Akuffo, and the chaotic rooting out of corruption by Rawlings, simply added to the insecurity of property. The combination of the ineptitude of the democratically elected government of Limann and the anarchy of 1979, meant that economic agents remained traumatized, so that none of the potential returns from a democratic form of government materialized during 1980 and 1981. Instead, economic agents engaged in a frantic scramble for whatever rents might be available.

The anarchy continued with the return of Rawlings on December 31, 1981, intent on destroying the corruption of the old regime. So too, the economic atrophy continued.

The chaos of 1982 gradually faded as the economic reform program took hold in 1983. The intention of Rawlings and his economic team to restore the economy to health became clear to all. In the years that followed, with Rawlings more securely in power, the regime progressed in economic terms from anarchy to autocracy. As the specter of anarchy faded, government provided more security of individual property rights, and began to provide some public goods. This transformation of regime type contributed significantly to the unbroken stream of increases in real GDP per capita starting in 1985.

The resumption of electoral competition in 1992, and the openly contested elections of 1996, re-established Ghana as a fundamentally democratic society. However, for many entrepreneurs, memories of the confiscations of the past remained vivid as long as Rawlings stayed associated with the government. Further, in the run-up to each of the elections, the PNDC/NDC governments chose to engage in deficit finance, indirectly engaging in the predation of inflation that Nkrumah had initiated in the early 1960s, and others had repeated subsequently. Thus, the

economic gain to Ghana of moving from anarchy to autocracy to democracy was less than it might have been.

Interaction

Each of the economic and political themes just outlined would have been sufficient to slow long-term economic growth on its own. When all were working in concert, as they were for a decade prior to launching the reform program, the effect of each was substantially amplified. In aggregate the effect was overwhelming, generating economic atrophy, not growth.

Efforts to reverse the thrust of each have been underway for some fifteen years, but the process is still incomplete. The reform program has succeeded in delivering real growth of GDP per capita, but that summary indicator has only reached about the same level that prevailed at independence, and total factor productivity is still less than in the early 1960s. Macroeconomic balance has not been maintained consistently. Currency overvaluation was reversed, but in recent years instability of the real exchange rate has emerged. Financial repression, which before the reforms was serious, has been eased, but not lifted. Memories of inflation and asset confiscation linger. Traditional exports of minerals and cocoa, which shrank to a fraction of their potential, have recovered from the depths, but have not fulfilled their potential as engines of growth. The limited capacity of the state, in the absence of a national consensus on priorities, remains a constraint on growth. And, finally, the potential fruits of a democratic form of government are yet to be fully realized.

Many Ghanaians, and the international agencies supporting the reform program, recognize that these elements explain much of the atrophy and later recovery. What remains to achieve is consistent application of these lessons over the long term.

Future Prospects

Given what has been learned from the past, what are the prospects for future growth? One way to assess the potential for future growth in Ghana is to simulate scenarios, given a certain set of assumptions. Scenario simulations are obviously crude, and should not be interpreted literally. However, they are useful to provide a rough idea of the impact of certain assumptions. Hence, we construct two different scenarios, using the same simple analytical framework as for the growth accounting exercise earlier. We also compare the two scenarios with the Ghanaian authorities' own long term forecast or development plan.

In the first scenario, which we call the baseline scenario, we simply extrapolate the growth rates of the capital stock and total factor productivity, using the average growth rates for the period 1992-96, corresponding to the period after the first post-ERP elections. The second scenario is as optimistic as we judged possible without crossing the line of the unrealistic, and should be considered as a best case scenario. For this we use the total factor productivity growth rate of the 1984-89 period together with the highest investment rate attained during the ERP (20 per cent of GDP). Projections of labor force growth are taken from UN World Population Prospects.¹

These scenarios may be compared to the major long term development goal presented by President Rawlings to the Parliament of Ghana in 1995, called Vision 2020. This document proposed that Ghana should become a “vibrant-middle income nation within the next twenty five years.”² Economic growth was targeted to attain 8 per cent per annum on average, through a strategy of human capital development, improved macro-economic policies, diversification of the economy, the creation of a business friendly environment, trade openness, the promotion of an efficient financial system, among others.

The underlying GDP growth rates of the base line and best case scenarios are compared with Vision 2020 in Table 5 along with the resultant GDP per capita. Figure 39 shows the results from

¹ The baseline TFP growth rate is assumed to be 1.6% per annum, and the best case rate is 2.1% per annum. The labor force growth rate begins as 3.35% per annum in 1996, and in stages declines to 2.70% in the later years.

² Vision 2020, p. 5.

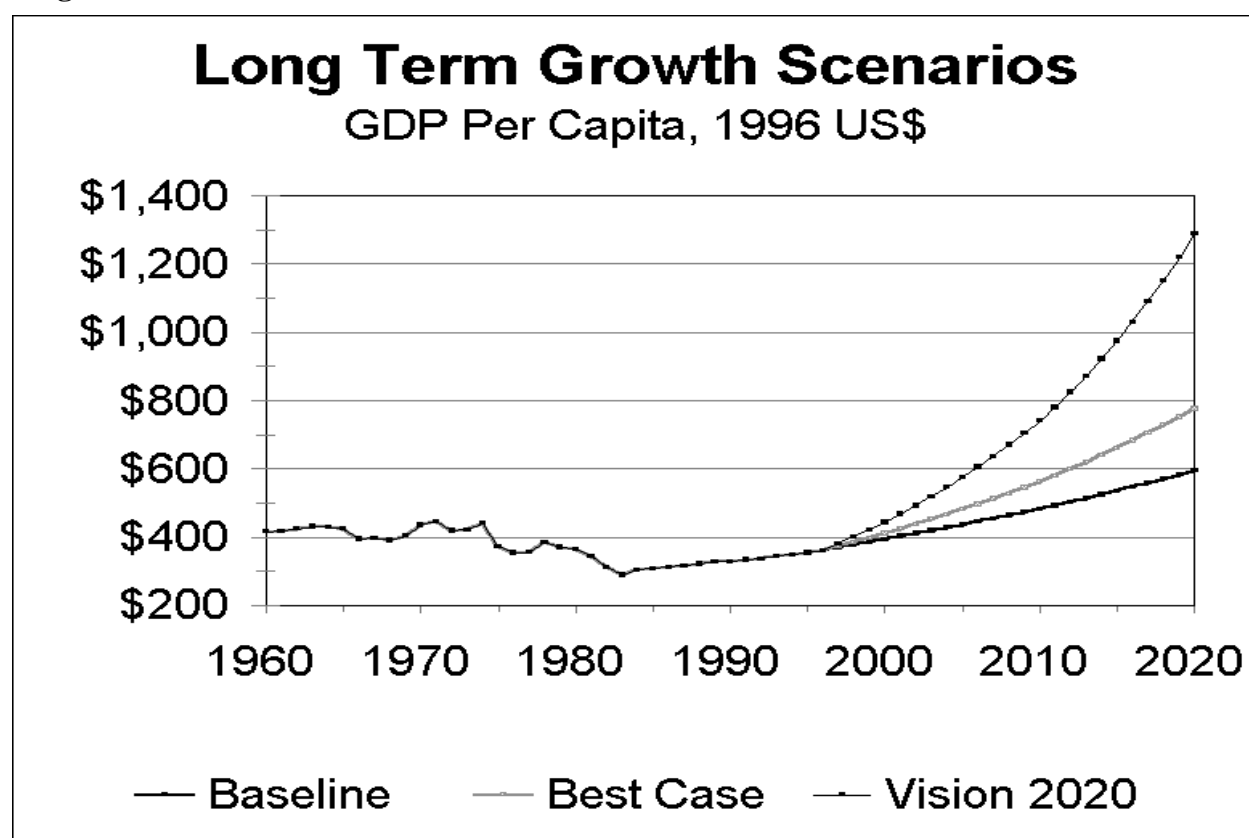
the two scenarios compared with the Vision 2020 goal in the context of real GDP per capita since 1960.

Table 5:

Long term growth rates (%)

	<u>GDP growth rate</u>	<u>GDP/capita growth</u>	<u>GDP/capita in 2020 (1996 \$)</u>
Base line	4.4	2.1	595
Best case	5.5	3.3	777
Vision 2020	8.0	5.7	1,290

Figure 39



Source: Authors' calculations

The base line scenario gives a fair, yet not impressive, long term per capita growth rate of 2.1 percent per year. The level of GDP per capita attains \$595 in constant 1996 dollar terms in the year 2020, which corresponds to a cumulative growth of about 65 per cent in the 1996-2020

period. This performance is improved considerably in the best case scenario, where growth is more than one percentage point higher.

As is clear from Table 5 the Vision 2020 goal appears hopelessly unrealistic from the perspective of the year 2000. In the best case scenario, per capita income is estimated just under \$780 in 2020. This is more than double the level in 1996, but still significantly below the middle income status aspired to in Vision 2020. The GDP growth rate in the best case scenario is 2.5 percentage points short of the goal.

There is no doubt that our scenarios have a wide margin of error, and the objective of formulating these scenarios is not to provide a precise forecast of the state of the Ghanaian economy two decades ahead. Nevertheless, the results are telling. The Ghana government has adopted a long term view of development, with a time horizon that stretches more than two decades into the future. Such long term projections could provide important information for agents contemplating investment decisions in the face of future risk – but only if the projection is credible. Unrealistic targets only reinforce suspicion about the economic policy package.

Despite these reservations, it is clear from the foregoing that Ghana has good potential for future growth. But it will remain a low income country for the foreseeable future.

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Table A 9:
Mineral Production Indexes
(Figure 30)

Year	Total	Gold
1955	81.7	80.5
1956	91.0	74.7
1957	104.0	92.6
1958	100.0	100.0
1959	101.4	107.0
1960	103.0	103.0
1961	93.8	97.7
1962	93.0	104.1
1963	91.8	108.0
1964	91.9	101.4
1965	90.5	88.5
1966	91.5	80.2
1967		
1968		
1969		
1970		
1971	100.0	100.0
1972	104.5	103.8
1973	98.3	104.5
1974	85.3	88.1
1975	79.3	75.1
1976	76.8	76.3
1977	69.3	75.1
1978	60.0	62.8
1979	51.9	55.7
1980	51.2	55.1
1981	47.3	53.2
1982	41.5	51.6
1983	34.8	43.2
1984	40.1	44.9
1985	45.3	46.8
1986	41.8	44.9
1987	44.8	51.4
1988	48.0	58.5
1989	55.9	66.6
1990	68.5	77.8
1991	102.4	122.1
1992	121.6	141.1
1993	137.1	193.9
1994	148.5	217.7
1995	171.8	257.9
1996	172.4	242.4
1997	187.8	269.0

Source: Ghana Quarterly Digest of Statistics.

Table A 10:
Growth Accounting
(Figure 38)

Cumulative per centage Changes			
Year	Output/worker	Output due Capital/worker	TFP
1960			
1961	1.5%	2.2%	-0.7%
1962	3.8%	3.9%	-0.2%
1963	6.3%	6.0%	0.4%
1964	6.8%	8.2%	-1.5%
1965	6.5%	10.1%	-3.6%
1966	0.3%	11.0%	-10.7%
1967	1.9%	11.0%	-9.2%
1968	1.1%	11.2%	-10.0%
1969	5.6%	11.5%	-5.8%
1970	13.8%	12.1%	1.6%
1971	16.7%	12.6%	4.1%
1972	11.3%	12.4%	-1.1%
1973	11.8%	12.1%	-0.3%
1974	16.5%	12.5%	4.0%
1975	-0.3%	12.5%	-12.8%
1976	-6.2%	12.5%	-18.6%
1977	-6.8%	12.6%	-19.4%
1978	0.2%	12.5%	-12.3%
1979	-3.8%	12.2%	-16.1%
1980	-5.7%	11.9%	-17.6%
1981	-11.8%	11.3%	-23.0%
1982	-21.6%	10.4%	-32.0%
1983	-29.2%	9.5%	-38.7%
1984	-23.9%	8.7%	-32.6%
1985	-22.0%	8.2%	-30.2%
1986	-20.1%	7.6%	-27.7%
1987	-18.7%	7.4%	-26.1%
1988	-16.4%	7.4%	-23.8%
1989	-14.7%	7.5%	-22.2%
1990	-14.8%	7.6%	-22.3%
1991	-12.4%	7.4%	-19.8%
1992	-11.6%	8.0%	-19.6%
1993	-9.7%	7.5%	-17.2%
1994	-8.8%	8.0%	-16.8%
1995	-7.2%	8.5%	-15.7%
1996	-5.0%	9.5%	-14.5%

Source: Authors' calculations.

Note: Percentages may not add exactly due to rounding.

Table A 11:
Long Term Growth Scenarios, 1997 - 2020
GDP per capita, 1996 US\$
(Figure 39)

Year	Actual
1960	416
1961	419
1962	425
1963	432
1964	430
1965	424
1966	395
1967	397
1968	390
1969	404
1970	436
1971	446
1972	420
1973	421
1974	441
1975	374
1976	354
1977	355
1978	384
1979	371
1980	365
1981	345
1982	313
1983	290
1984	304
1985	308
1986	313
1987	316
1988	323
1989	328
1990	328
1991	335
1992	337
1993	344
1994	348
1995	354
1996	362

Projections	Baseline	Best case	Vision 2020
1997	370	374	381
1998	378	386	401
1999	386	398	422
2000	394	411	445
2001	403	425	468
2002	411	438	493
2003	420	452	519
2004	428	467	547
2005	437	482	576
2006	446	497	606
2007	455	513	638
2008	464	529	671
2009	473	546	705
2010	482	563	742
2011	493	581	780
2012	503	600	825
2013	514	620	873
2014	525	641	923
2015	536	662	976
2016	547	683	1,032
2017	559	706	1,091
2018	571	729	1,154
2019	583	753	1,220
2020	595	777	1,290

Source: Authors' calculations.