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# REPORT ON THE

# AFRICA VENTURE CAPITAL PROJECT IN GHANA

PART I: RICHARD LOTH, HARVEY & COMPANY MEMORANDUM

PART II: JOHN LEECH, "A GHANA VENTURE CAPITAL INITIATIVE"

November 1990

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# REPORT ON THE

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PART I: RICHARD LOTH, HARVEY & COMPANY

MEMORANDUM, JANUARY 1991

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**MEMORANDUM**

TO: Warren Weinstein, AFR/MDI
Dean Bernius, AFR/MDI

THROUGH: Stephen Sposato, MDI

FROM: Richard Loth, AVCP

DATE: January 10, 1991

SUBJECT: Report by Rural Investment Overseas, Ltd. (John Leech) on the Ghana Venture Capital Initiative

While the Report John Leech prepared is an excellent one and does represent, to a large degree, a collaborative effort (Messrs. Loth and Leech), there are a number of areas where we have a different angle of vision. As John suggested in his Executive Summary, we, Harvey & Company, after having reviewed the Report are providing this explanatory memorandum from our perspective. We will discuss the various points in their order of appearance in the Report.

In the discussion of the "Financial Sector" in Chapter Two, pages 7-10, there is mention in Section 2.2 of two items which should be highlighted. One, the successful recent start-up of the Consolidated Discount House, Ltd., a money market intermediary, appears to be rather strong evidence of the opportunity for raising local capital. As the Report states, "...it is...a demonstration that investors...some private ones among them, are not slow to stake their funds on a proven opportunity."

The Fan Milk Ltd. public issue at year-end 1989, while unattractive from a fundamental value analysis and poorly handled by the underwriters, was fully subscribed by some 1,200 institutional and individual investors. While the Report is justifiably skeptical about the breadth and depth of local investment capital pools, both of these cases, contrary to the Report's implied conclusion (page 3), may be evidence that the

Ghanaian private investor is ready to risk his money in portfolio investment opportunities. Second, the Bank of Ghana (the central bank) is very interested in and supportive of any private approach to venture capital, even though there is no existing regulatory framework for this mechanism. It sees such a vehicle as highly desirable for soaking up short-term liquidity and transforming such funds into long-term investment capital.

In Section 3.6, "Profile of the Entrepreneur," the Report correctly identifies two categories of Ghanaian entrepreneurs (see pages 14-15). We would add a third category - "the survivor." This minor distinction is important when assessing business investment opportunities in Ghana, a feasibility consideration for AVCP support. As opposed to those starting over again and the "returnee" (returning Ghanaian expatriate businesspersons), the survivor has gained valuable experience, albeit painful, and has an existing business on which to expand diversify, and/or modernize. This type of enterprise often represents attractive later stage investment opportunities for the venture capitalist. Most of the companies I visited would fall into this category.

In Section 4.2, "Venture Capital in Africa," the Report emphasizes the equity side of venture capital. We would add that there are a number of equity-like debt mechanisms which can also be employed, e.g., adding "performance kickers" to long-term debt arrangements, which are structured to defer the payment of principal and interest. Also, if the present weakness of the commercial banking system in Ghana persists, any venture capital fund may have to address the needs of investee companies for working capital. Venture capitalists generally count on conventional financing being available for their portfolio companies.

As we have discussed with CDC in the context of Botswana, the issue of the corporate structure of the fund (see Section 5.4), limited liability company versus general/limited partnership, is discussed. The Report recommends the former, which may be the preferred structure in Ghana, but we would recommend that this technical aspect remain open to further discussion and review. There are certain aspects of the partnership form which are appealing, particularly those dealing with specialized market segments and the management function.

In discussing "Venture Capital Initiatives and Options" (Chapter Six), the Report advocates a joint venture-like approach: Commonwealth Development Corporation (CDC) - Continental Acceptance Limited (CDL). This approach has a great deal of merit, however, it appears to be too early in the game to reach such a definitive conclusion. CAL is an attractive potential sponsor, but we would not rule out other options. Just for the record, the Merchant Bank of Ghana (MBG) advised us that they planned to have a venture capital fund launched during the first half of 1991. It appears that their thinking is somewhat more advanced and concrete than indicated in the Report. If MBG's plans materialize, we would consider this a plus for additional venture capital development in Ghana, i.e., vis-a-vis CDC's plans for a fund. Multiple "players" in the venture capital business contribute to a more efficient processing of risk assessment and investment.

We would still like to reserve judgment regarding the availability of private sector funds for investment in a venture capital fund. The Report takes the position that this potential is "limited" (see Section 7.1). While it may be more expeditious, and prudent, to jump start a fund with external sources from CDC, we may be missing a real opportunity to mobilize local capital (a key test for the AVCP). Perhaps it is a question of phasing in local participation as and when it is feasible. We would simply recommend that this aspect of a venture capital fund in Ghana be closely monitored with an eye toward implementation sooner rather than later, if this is possible. AVCP financial assistance to help attract and underwrite the costs of a first-class management team/ institutional sponsor would surely impact on this situation.

In this regard, while not necessarily a point to be discussed in the Report, it seems worthwhile mentioning that we were very impressed with the business expertise of several of the Ghanaian professionals contacted who have returned to live and work in their country. They bring with them educational backgrounds and work experience which are most appropriate to the needs of venture capital management. If these individuals are representative of the potential talent pool for recruitment, competent management, a key venture capital component, appears accessible.

One last observation worth noting - it appears that the expected return-on-investment hurdle for the investing public, both institutional and individual, is not that high. Several informed sources indicated that a venture capital fund, properly sponsored and managed, would only need to beat the government treasury bill rate by a few basis points. The Report implies that a venture capital fund would need an exemption from the capital gain tax.

While elimination and/or a reduction of this tax burden is obviously highly desirable, its continuance at its present level is not a "deal breaker" regarding the establishment of a venture capital fund. It may be too sensitive an issue to link directly, at least from day one, to the development of the venture capital initiative.

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## EXECUTIVE SUMMARY

The US Agency for International Development (AID)'s Market Development and Investment department has recently launched the Africa Venture Capital Project (AVCP). AID believes that venture capital has an important place in supporting the private sector, in fostering its role in economic development, in encouraging African entrepreneurship, and in providing a focus for investment and capital formation.

Harvey & Company, Incorporated in Washington has been contracted to implement the AVCP. In relation particularly to countries selected for the Project in anglophone Africa, it was agreed to utilize the experience of certain British organizations active there, notably the Commonwealth Development Corporation (CDC) and Rural Investment Overseas Ltd (RIO).

A mission consisting of Richard Loth (Harvey & Co) and John Leech (RIO) visited Ghana from October 20-27, 1990. This report on their visit has been prepared by RIO for Harvey & Co. It incorporates their collective findings, suggests the ways in which the objectives of the AVCP may be realized in Ghana, and defines the inputs required to achieve that. Where Harvey & Co's conclusions differ in emphasis, they may wish to augment this report with an explanatory memorandum.

The economy of Ghana became rapidly depleted after independence. Political instability, drought and high oil prices during the 1970s and early 1980s led to a 30% decline in per capita incomes. The present Government, formed in 1981 by the Provisional National Defence Council under Fl Lt J.J. Rawlings, introduced an Economic Recovery Programme in 1983. Its main purpose - to restore fiscal and monetary discipline, shift prices in favour of production, and encourage private investment - appears on the way to being achieved. In consequence, Ghana enjoys liberal donor support.

The ERP and subsequent structural adjustment programs have resulted in a massive devaluation of the Cedi (from 2.75 to the US$ in 1983 to 340 to-day) and GDP growth of some 6% pa. Incentives to producers have begun to shift resources from the urban to the rural areas; they have also revived cocoa production and restored export earnings. Industry has been aided on the input side by trade liberalization, though a flood of cheap imports is forcing it to become more competitive.

Both the financial and the corporate sectors are in distress and in the process of drastic restructuring. The majority of bank loans are non-performing and have been placed in a special Trust to clear the banks' balance sheets. The Bank of Ghana is looking to opportunities for salvaging some of these assets and offering them to investors. There are also 32 state-owned enterprises to be privatized, of which 15 have meanwhile been liquidated and three are now on offer.

Although no longer short on liquidity, the banking system is still incapable of supplying the private sector with working capital and term loans. Inflation running at over 30% means that the Bank of Ghana is reluctant to relax capital adequacy ratios and allow the money supply to grow. The Bank has itself entered the market to mop up the system's excess liquidity with Government paper.

There is as yet no capital market, though the Ghana Stock Exchange is about to begin tentative operations. It will cater first for the capital needs of well-established companies, later for a second list of those with at least a three-year record. Trading in shares will be narrow, and the main volume will be in other securities. For the past ten years there has only been one public offering in Ghana. Poor handling of that makes the results somehwat incloriclusive, though the company now has some 1,200 shareholders.

Meanwhile capital is raised by private placement, principally through three merchant banks. There is a body of investors, led by the Social Security & National Investment Trust and consisting of other wholly or partly Government-owned organizations. The truly private investor is difficult to identify, except for some family concerns beginning to develop into small conglomerates as their activities expand.

There is evidence of growing entrepreneurship, assisted by Ghanaians lately returned from real or self-imposed exile. They bring skills and experience acquired overseas, coupled with independent resources. Those who stayed behind also see new opportunities, though they feel that Government is unhelpful. An indicator is the 50% increase in membership of the Association of Ghana Industries between 1986 and 1988. The number of project proposals discussed with the mission provides further evidence.

Venture capital can quite clearly make an important contribution in an environment where a lively private sector is starved for funds of all types, from foundation capital to term loans and even working capital. The Bank of Ghana would welcome it because investment is likely to be non-inflationary; but also because it is looking for a financing vehicle to put to work potentially viable non-performing assets acquired from the banks.

All three of the merchant banks are interested in venture capital. Ecobank has lined up possible shareholders but its plans have not yet crystallized. Merchant Bank (Ghana) is attracted by the concept but does not appear to have developed a clear strategy. Continental Acceptances Ltd (CAL), on the other hand, is proposing to go into partnership with CDC in setting up a Ghana Venture

Capital Company (GVCC). Its proposal is the most concrete and advanced; by associating CDC, one of CAL's shareholders, it also incorporates actual venture capital experience.

CAL and CDC would propose to set up GVCC owned initially as to 60% by CDC and 40% by Ghanaians, including CAL. Because of the lack of reliable evidence that the Ghanaian non-parastatal private investor is ready to risk his money in portfolio investment in untried ventures, CDC is willing to underwrite CAL's efforts to place up to 30% during the formation stage.

It is expected that GVCC would disburse its initial fund of US$ 2 million within two years. Three projects are already at various stages of preparation and appraisal by CDC, but await a vehicle capable of delivering the intensive management involvement and other inputs required for successful venture capital operations. It is estimated that additional local funds would be introduced by a second placement of US$ 3 million within two years. The company should then be ready for a substantial public offering, perhaps up to US$ 10 million, within a further three years.

Control of GVCC would be vested in its own Board, which would appoint the management. One expatriate would lead and train a team of Ghanaian professionals. Management would be assisted by an Advisory Board of five Ghanaians of high standing in the financial community, to whom investment proposals would be submitted. They would form a body of independent Directors when the capital is enlarged.

The report describes in detail the methods and criteria with which a GVCC should operate - whether set up by CAL and CDC or by any other promoters. From these and other best practice assumptions a set of illustrative financial projections has been prepared. They show that an acceptable rate of return can be achieved in time to present an attractive prospectus to Ghanaian investors for the second placement, provided that some initial costs can be borne by the AVCP.

These costs are set out in detail, together with proposals for a number of related activities to facilitate and enhance the effect of the GVCC's operations. It is considered that such comprehensive support from the AVCP, augmented by the active involvement of the Mission in Accra, should enable US AID to achieve in Ghana a rapid and successful demonstration of the principles on which the Project is based.

# CHAPTER ONE INTRODUCTION AND BACKGROUND

## 1.1 INTRODUCTION

The US Agency for International Development (AID) is resolved to strengthen private sector activity in developing countries as a means of harnessing greater energies and investment to speed economic development. Within the Africa Bureau, the Market Development and Investment department (MDI) has initiated the Africa Venture Capital Project as an instrument to assist productive investment in the private sector. The three-year project has the following objectives -

- to promote an understanding of venture capital investment on the part of entrepreneurs, institutions and the professions;
- to reduce obstacles to equity investment generally;
- to mobilize indigenous financial resources for private investment; and
- to identify opportunities for the creation of venture capital vehicles and to enhance their prospects of success with a range of financial support measures, but short of contributing to the venture capital fund itself.

AID has selected a number of countries in Africa, of which Ghana is one. A mission consisting of Richard Loth of Harvey & Company, Inc (the main contractors for the project) and John Leech of Rural Investment Overseas Ltd (RIO) in London visited Ghana from October 20-27, 1990. The AID Mission Director in Accra made available his Private Sector Adviser, Daniel Gyimah, who took part in most of the meetings and discussions. Their findings are given in this report.

## 1.2 THE ECONOMIC BACKGROUND

The Provisional National Defence Council (PNDC) and its Chairman, Flt Lt J.J. Rawlings, have constituted the Government of Ghana since December 31, 1981. Ghana's chequered political history since independence in 1957 had succeeded in depleting its economic resources. Drought and steep increases in oil prices in the 1970s and early 1980s led to a 30% decline in per capita incomes. Economic activity stagnated, import volumes fell by a third, real export earnings were halved, and inflation ran at some 120% pa.

Aided by suspension of the Constitution, the PNDC saw its first duty in a campaign against "corruption and profiteering". The result was demoralising for the private sector. Domestic savings and investment fell to negligible levels. Many able Ghanaians preferred exile to staying in a hostile and threatening environment.

In 1983 the PNDC began to come to grips with the worsening economic situation. It introduced an austerity budget, linked to a drastic economic recovery programme (ERP). The ERP sought to restore fiscal and monetary discipline, shift prices in favour of production, encourage private investment, and restore the economic and social infrastructure. The International Monetary Fund (IMF) then began to assist with loan and stand-by agreements. Continuing tight economic management, and progressive devaluation of the cedi, also gave increasing confidence to donors within the World Bank Consultative Group.

Since the introduction of the ERP, followed in 1987 by a structural adjustment program, GDP growth has averaged between 5% and 6% pa, some 2% above the growth rate of the population. A trade liberalization program was completed in 1988, when all imported goods became eligible for funds from the foreign exchange auctions. The auctions have led to a realistic exchange rate for the cedi, devaluing it from C 2.75 to the US$ in 1983 to C 340 now.

This massive devaluation has had dramatic consequences for both the financial and the private sector. Improved export earnings also helped to maintain high inflation, currently still around 30% pa. Interest rates have been progressively raised, petroleum prices made more realistic, and subsidies reduced. Adjustments in wages have sought to soften the impact on real incomes. Government revenues have benefited, and further augmented through improved tax collection.

Ghana's principal exports are cocoa, gold and electricity. Once the world's largest producer of cocoa, it sank to third place through neglect of the farmer's interest. Government has begun to remedy this by increasing prices and improving the farmer's receipts from the marketing board. Their rise from a mere 8% to 50% of sales value has been a marked stimulus to production. Despite falling world prices, cocoa thus once more accounts for two-thirds of Ghana's export earnings. The 1989 outturn was cocoa US$ 407.8 million, gold US$ 159.9 million, electricity US$ 82 million, and timber US$ 80 million. However, the forex bureaux came in as the third largest foreign exchange earner with US$ 89 million.

Ghana's total external debt is currently estimated at some US$ 3.2 billion. The absorption of increasing amounts of aid on IDA terms is likely substantially to increase this, though the debt profile will be progressively improved. Due to debt cancellation and efforts to clear payment arrears by the end of 1990, the debt service ratio (including IMF debt service) is expected to fall from 64.49% in 1989 to 41.2% at end-1990.

It is clear that Ghana's economy is still in a state of transition. Sound macro-economic policies are producing visible results, but several bottlenecks in policy implementation need to be addressed before the full benefits will be realised, particularly in the private sector. Privatisation of state-owned enterprises (SOEs), and completion of the banking sector reorganisation are two critical areas awaiting more resolute action.

The divestiture program, published in 1988, consisted of 32 SOEs. Since then, 15 have been liquidated. Work is in hand on 10, of which 3 have finally been offered in November 1990.

Public investment has grown from negligible levels to 8.3% of GDP in 1989, indicating rehabilitation of the country's economic and social infrastructure. Yet an estimated half of the population still lives in absolute poverty. Improvements in producer incentives have begun to shift resources from urban to rural areas; health and education services have been improved. Public and private investment, and more realistic pricing of capital and foreign exchange, are visibly increasing employment, wages and productivity.

## CHAPTER TWO THE FINANCIAL SECTOR

### 2.1 BANKING

The three primary banks active in Ghana are Ghana Commercial Bank, Standard Chartered Bank Ghana Ltd and Barclays Bank of Ghana Ltd. There is a variety of secondary banks, consisting of the Social Security Bank, Bank of Housing and Construction, Agricultural Development Bank, National Savings and Credit Bank, National Investment Bank, and Bank of Credit and Commerce. These are augmented by three houses operating essentially as merchant banks, Merchant Bank (Ghana) Ltd, Continental Acceptances Ltd, and Ecobank Ghana Ltd. In addition, there are the Ghana Cooperative Bank and more than 100 rural banks.

The banking sector is in considerable distress. The causes are compounded of high foreign exchange exposure due to devaluation, huge non-performing loan portfolios coupled with inadequate provisions, and general weaknesses in management and control. Lending capacity has been affected by the impact on capital adequacy ratios, since inflation and non-repayment automatically increase exposure. Although interest rate controls and sectoral credit ceilings have been abolished, the result is a combination of high liquidity with an inability of the financial system to channel it into production.

Recognizing the crucial importance of restoring the banking sector to health, the donor community has recently agreed to fund the Non-Performing Assets Recovery Trust (NPART) as a vehicle for cleaning up the banks' balance sheets by purchasing their bad debts. However, care is being taken to prevent this from increasing the money supply; payment is in 5-year bonds which can be encashed only in equal parts over the last three years.

### 2.2 THE MONEY MARKET

The Consolidated Discount House Ltd was set up in 1988 to serve as inter-bank intermediary for short-term assets. This enables banks to improve the management of their liquidity position. The Discount House is permitted to deal in Treasury bills, short-dated Government Securities, bankers' acceptances, cocoa bills, negotiable short-term certificates of deposit, and commercial paper.

The success of this venture has now encouraged several investors to plan the setting up of a Second Discount House. The extent to which it will increase overall liquidity is unclear. It is nevertheless a demonstration that investors, and some private ones among them, are not slow to stake their funds on a proven opportunity.

The Bank of Ghana has recently begun to manage monetary aggregates through new financial instruments and open-market operations. In the first quarter of 1990 it sold financial instruments worth C 8 billion to absorb liquidity from bank and non-bank sectors.

## 2.3 THE CAPITAL MARKET

Based on a report commissioned by IFC in September 1989, the Ghana Stock Exchange is about to begin operations. These will be regulated by The Stock Exchange Act 1971, as well as its own newly devised listing and membership rules. Some 34 companies have so far paid C 5 million each towards the operating costs. The market makers will be the three merchant banks.

There will be two lists. Requirements for the first list are a capitalization of C 100 million and submission of 5 years' audited accounts. The second list is for companies with a capitalization of C 50 million able to file at least 3 years' audited accounts. There is as yet no indication of whether the dealers will seek to create an informal market for promising new and unlisted companies.

The IFC-sponsored report estimated that in its first year the Ghana Stock Exchange would have an available supply of shares with a market value of C 6.4 billion, and a demand of C 7.8 billion. The estimate for secondary trading is C 64 million, or 1% of total market capitalization. Trading in securities, bonds and Treasury stock would add some C 500 billion to the first year's trading. The Stock Exchange Director believes that there is evidence that all these estimates will be exceeded.

Whilst the opening date is still uncertain, the Director indicated that trading would start on an informal basis on November 12, 1990 so that experience can dictate the date of an official opening early in 1991.

## 2.4 THE NON-BANKING SECTOR

Non-banking institutions concerned with investment consist of eleven insurance companies and the Social Security & National Insurance Trust (SSNIT). The latter receives social security contributions and is charged with investing them so as to maximise the retirement fund. SSNIT receives some C 1.2 billion a month in contributions (5% from each employee, plus 12.5% from the employer). Investment income brings total new investable resources to C 1.5 billion a month.

The current SSNIT portfolio is said to stand at C 50 billion, a figure hard to substantiate as SSNIT are only just beginning to produce their first accounts since 1982. Holdings are said to consist of C 24 billion in Treasury bills, C 16 billion deposited with Bank of Ghana, and C 10 billion in various instruments including C 1.2 billion in selected equities.

## 2.5 DEVELOPMENT CAPITAL

All the government-owned development finance institutions are facing similar difficulties to those of the banks. Their sizeable foreign exchange liabilities have swollen massively with devaluation, their portfolios are for the most part non-performing, and their net worth has been completely eroded. About 75% of the National Investment Bank's portfolio is already with NPART. No significant resources will be available from these institutions until they, too, are restructured.

Donors have, however, tried to pump other resources into the system. Of special relevance is the Fund for Small and Medium Enterprise Development (FUSMED), a US$ 28 million apex facility established by the World Bank to assist SMEs. Participating financial institutions are able to draw on it for investment credits (including equity and quasi-equity), equipment leasing, and guarantees. Eligible beneficiaries are private enterprises in productive sectors and allied service activities (but not pure agriculture) whose total assets (excluding land) do not exceed C 500 million. Funds can be used for new ventures or rehabilitation or expansion of existing ones. Loans and sub-loans are in Cedis, the Government being responsible for the exchange risk of the overall credit. Sub-loans must not exceed C 500,000 each.

Experience with this facility has been poor, largely because the beneficiary is required to contribute at least 25% of the new project cost in equity or from internally generated funds. The handling institution is also required to contribute some 10-15%; they have been loath to do so because of the effect on their capital adequacy ratios. In the first nine months of the scheme only 17 applications were received, and only a handful actually processed.

## 2.6 THE REGULATORY FRAMEWORK

The activities of banks are governed by the Banking Law 1989 which repealed and substituted all previous banking legislation. Some of its provisions now also apply to those development finance institutions which have engaged in commercial banking operations to compensate for lack of investment business. The absence of a requirement on the latter to constitute a reserve fund from retained profits must be responsible in part for their present plight. There are also weaknesses in the supervision arrangements of the Bank of Ghana (BoG).

There is legislation also to regulate the activities of insurance companies. Nothing, however, exists in respect of non-banking financial institutions, which are expected to become a growing sector. The BoG is currently giving thought to the drafting of appropriate financial services legislation. This has considerable relevance to the scope of this report and is discussed further in Section 5.6 below.

## 2.7 FINANCIAL SECTOR PERFORMANCE

The weakness of the financial sector has hindered the response of manufacturers and investors to improved incentives and the mobilization of savings. Improvement in the willingness of the public to hold financial assets has been slow. The velocity of circulation decreased from a high of 7.8 in 1984 to 5.6 in 1987. Contributory factors are clearly inflation, negative interest rates, and the inability of banks to offer themselves as a convincing store of value.

The World Bank has laid down firm guidelines for improving the performance of the financial sector in connection with its Financial Sector Adjustment Credit. A unit within the BoG is assiduously monitoring progress. For the time being, however, the weakness of the financial system limits effective support of the productive sector and constrains financial savings.

# CHAPTER THREE THE PRIVATE SECTOR

## 3.1 THE ENVIRONMENT

The early years of the present Administration were accompanied by severe disincentives for the private sector. Demonetization of C 50 notes without compensation, the freezing of bank accounts in excess of C 50,000, recall of bank loans for trade finance, compulsory use of checks for all payments over C 1,000, all undermined confidence in the banking system. Investigations for tax evasion, corruption or fraud served to throw further suspicion on the accumulation of wealth. The resulting exodus of the more enterprising Ghanaians severely curtailed private sector activity.

The publication of the Investment Code in 1985 confirmed the Government's intention to redress the past decline in the economy by encouraging investment in production. The Code offered incentives and guarantees tailored according to the priority attached to each sector. Agriculture enjoys the highest priority, followed by manufacturing industry, construction and tourism. Strangely, tax benefits are meagre and reserved for tree crops and livestock, and projects located in priority areas.

The Code also lays down the enterprises wholly reserved for Ghanaians; and minimum capital requirements for foreign participation in those where this is permissible (US$ 60,000 for a joint venture, or US$ 100,000 for wholly foreign ownership). Dividends, realizations, loan servicing and fees for technology transfer can be freely remitted, as can expatriate earnings. There are guarantees against expropriation or forced divestment; and provisions for the settlement of investment disputes.

At the same time the Code established the Ghana Investment Centre to promote the purposes of the Code and grant approvals under it. The intention was for it to act as a priority route for permissions required from other ministries. In reality, neither the legislation nor the Centre appears to have been of much value. Investment, both domestic and foreign, is lagging; and many of those who do invest go ahead on their own without subjecting themselves to the cumbersome procedures of the Centre. In the absence of attractive tax concessions, and with the existence of a liberal foreign exchange regime, the incentives have little real value.

The World Bank has repeatedly argued for improvements in both. Laws and regulations need still to be realigned to overcome a web of regulations administered by different agencies. The relevance of some tax and tariff incentives has also been questioned, and the Code is even suspected of having restricted rather than encouraged foreign investment.

## 3.2 PERFORMANCE

There is no doubt that a combination of negative factors has severely restricted private sector performance. The poor economic climate, restrictions under the ERP, the non-performance of public and parastatal enterprises, massive devaluation, lack of working capital and institutional investment funds have meant a long struggle for survival. The trade liberalization program, whilst assuring enterprises of imported materials, has also brought a flood of cheap imports competing against local products for long protected.

A measure of the development of the private sector can be obtained from the membership of the Association of Ghana Industries. In 1986 the number of members stood at 1,017; by 1988 it had risen to over 1,500. Despite all the obstacles, manufacturing is expected to retain its relative buoyancy, and to turn increasingly to exports as a new source of growth.

The main impulse for increased investment will be investor confidence. Statistics from the Ghana Investment Centre show that the number of approvals under the Investment Code in the five years to end-1989 was 541, with a total value of US$ 1,318 million. Of these, 396 were for new investment projects. However, the 1989 figure of 117 was no more than the annual average.

Discussions with entrepreneurs, singly and in groups, elicited three broad strands in investor attitudes. First is the considerable resilience which has helped them through the rough times, now coupled with an understandable caution. The second is an abiding disappointment with Government attitudes to the private sector; its lack of understanding of the entrepreneurial process is blamed for many of their difficulties. In contrast, the third was a readiness to seize new business opportunities, particularly those offered by market changes, new technologies, and co-operation with foreign partners.

There are therefore good indications that the private sector has not lost its will to go forward, and indeed to invest in its own growth. The constraints upon it remain formidable, not least the problems of servicing past debts and locating fresh capital. These matters are discussed below.

## 3.3 PRIVATE SECTOR REPRESENTATION

The main bodies representing the private sector are the Ghana Chamber of Commerce, the Ghana Employers's Association and the Association of Ghana Industries. While they have certain opportunities to meet with high-level government officials, the dialogue between them has barely begun. Officials have not yet seen the need to assess the business environment and problems affecting the private sector. Neither is there much evidence that the associations have confidence in their ability to act as a bridge and to inform, advise and educate both government and their own members on new developments and policies.

### 3.4 PROJECT GENERATION

A further indication of the dynamism of the private sector, even if much of it currently remains frustrated, is the number of project proposals which were discussed with the AVCP mission by the promoters themselves as well as by financial intermediaries trying to assist them. The range covered export-oriented agriculture, seafood, forestry, milling, animal feed, furniture manufacture, food processing, metal fabricating, aluminium extrusions, carpets, low-cost housing, improvements to a medical clinic, and a number of service industries.

About half of these proposals concerned expansion of existing enterprises. In part they dealt with improvement and modernisation of going concerns, usually by bringing in new plant and processes. However, there were also instances of successful small conglomerates expanding into allied areas of activity by creating new subsidiaries. The remaining proposals were for greenfield ventures, generally well thought-out and promoted by responsible entrepreneurs whose abilities had been tested elsewhere.

Of significance is the role of returnees from overseas. The Ghanaian diaspora gave many able Ghanaians the opportunity to qualify in Europe and the USA, as well as to gain subsequent professional work experience. They have generally built up assets overseas which allow them the capital and security to return and take a stake in their own country. They constitute a most valuable resource, as well as testimony that experienced people perceive the possibilities of growth in the economy. To a large extent, their experience compensates for the lack of foreign investors.

### 3.5 PRIVATE SECTOR FINANCING CAPACITY

The lack of public issues of securities makes it difficult to assess the extent of the private sector's capacity and readiness to make portfolio investments. The only public issue to come on the market was the privatization of Fan Milk Ltd at the end of 1989. Inexpert handling by the (perforce) inexperienced underwriters meant that not all the C 50 million was subscribed in a first round. A second offering at C 10 per share is said to have finally attracted some 1,200 institutional and private investors. Until other privatization issues come to market, it will be difficult to obtain more conclusive data.

The most common method used for capitalizing companies is private placement. Although two of the three merchant banks are relatively new, there is good evidence that this process functions. Its main use so far has been for debt instruments, usually at a 1 - 2 point spread over the Treasury bill rate. Some equity deals have, however, also been placed by word of mouth.

This rudimentary capital market depends to an overwhelming extent on a narrow band of corporate investors. In many cases these are not private, but parastatals or companies in which government or parastatals are the predominant shareholders. Among them are SSNIT and other parts of the social security system, Ashanti Goldfields Ltd, National Petroleum Corporation and similar state-owned enterprises. As an example, all of the 42% Ghanaian stake in one of the more recent placements, Ecobank Ghana, is owned by such entities.

The new Stock Exchange will in time provide more conclusive evidence on the extent to which a body of truly private shareholders already exists. In any event, part of its functions will be to encourage private persons and companies to invest. Wealthy individuals continue to be reluctant to reveal their identities, as the tax authorities are still prone to question the source of their funds. In any event, the Exchange will cater only for established companies coming to market. For those without a sufficient track record, private placement will remain the only solution. The creation of a truly private market will then depend crucially upon the willingness of the non-parastatal investor to risk portfolio investment in new ventures.

## 3.6 PROFILE OF THE ENTREPRENEUR

The typical Ghanaian entrepreneur falls into one of two categories. The first type is of riper years and experience. He will inevitably have seen his business go bankrupt or disappear in the years of turbulence. Either way, he will have had to start again from virtually nothing. Without significant resources, he will have started a new business or line in a cautious way, probably adapting both product and technology to changing conditions as he went along. Often he himself invented the technology and developed the equipment.

The second type is the returnee. He, too, is generally mature and may even have had a previous career in Ghana. In any event, he will have exercised or acquired his skills whilst overseas. His resources are superior, and hence the enterprises he undertakes are better endowed financially and technically. He is more likely to engage in service industries such as computers or derivatives of agency business. He will also have a better linkage to foreign partners.

At the base of both types of business are likely to be trading activities which provide the resources for keeping the enterprise afloat through hard times. They also compensate for the lack of bank finance for working capital needs. Such enforced independence will lead to the growth of small cluster groups or nascent conglomerates. Family or group interests will generally provide the means of growth, rather than external partners and investors.

The place of venture capital in such a typical enterprise has yet to be tested empirically. On the face of it, there is no doubt that many of these groups will soon reach the point where external resources will be vital for further growth. The extent to which they will be minded to share equity and management control with outsiders needs also to be established by experience. However, the cluster structure is more conducive to this, since the sharing will be confined to only a part of the whole. Although intensely self-reliant, the entrepreneur is also likely to have developed mature views on the need to introduce new blood into his undertakings.

## CHAPTER FOUR A ROLE FOR VENTURE CAPITAL

### 4.1 THE NATURE OF VENTURE CAPITAL

Venture capital financing is essentially equity or quasi-equity investment made for a predetermined period of time in small to medium scale businesses with high growth potential. However, venture capitalists will also participate in a wide range of business development financing, from providing seed capital to enable an entrepreneur to develop a new business to financing leveraged buy-outs.

Venture capital can be applied to any commercial activity or industry, but venture capitalists aim to spread their risks across several sectors as well as various stages of business development. Characteristically, venture capital financing -

- involves equity or equity-related participation in the form of direct purchase of shares, or through warrants, options or convertible securities;

- adds value to investments by developing an active involvement in the strategic and operational management of investee companies, often through Board representation, the provision of advice and assistance, and access to new technologies and markets;

- requires a relatively long period before achieving a significant yield on the investment.

The real returns on venture capital investment come through substantial capital appreciation. Prospects for divestment are therefore carefully evaluated before investments are made. Investments can normally be liquidated by public offerings, private placements, sale to another company or the other shareholders, or a buy-back agreement with the promoter or major shareholder. In developing countries extra care is needed, since the more direct of these solutions are unlikely to be available.

Venture capitalists can expect to participate in any of the following forms of financing business development -

a) Early stage financing

- Seed finance, consisting of relatively small amounts of capital provided to an entrepreneur to prove a concept. This often involves product development but not marketing.

- Start-up financing, for use in product development and initial marketing. Companies may be being established or have been in business a short time, without having sold their product commercially. Such firms have generally assembled their management team, prepared business plans, made market studies and prepared themselves for operations.

- First-stage financing, provided to companies which have expended their initial capital, perhaps in developing a prototype, and require funds to initiate commercial production and sales.

b) Expansion financing

- Second stage financing, providing working capital for the initial expansion of a company producing and marketing products but which has yet to make profits.

- Third stage financing, provided for the major growth and expansion of a company with an increasing sales volume which has reached break-even or profitability. Funds are used for plant expansion, marketing, working capital or product improvement.

- Fourth stage financing, generally the last round of private financing prior to a public offering or to qualifying for institutional term financing. This may also involve some turnaround aspects.

- Bridge financing, for a company expecting to go public within 6 - 12 months, often structured to be repaid from the proceeds of the issue. It may also involve restructuring of major shareholder positions through secondary transactions, for instance where early investors wish to reduce their holdings, or a departed manager had to be bought out.

c) Acquisition or management buyout financing

- Acquisition financing, provided to one firm to finance its purchase of another.

- Management/leveraged buyout financing, provided to an operating management to acquire a product line or business from either a public or a private company. This usually involves revitalizing the operation, with the entrepreneurial management acquiring a significant equity interest.

Venture capital requires the following conditions -

- sectors within an economy which have significant potential for growth;

- entrepreneurs with sound ideas and products with significant growth potential in identifiable markets, who are willing to accept venture capital and the management involvement it entails;

- corporate vehicles appropriate for absorbing venture capital;

- a tax environment which encourages the venture capital formula;

- a range of exit mechanisms to facilitate divestment;

- a legal system which recognizes intellectual property and patent rights.

## 4.2 VENTURE CAPITAL IN AFRICA

The concept of venture capital has become accepted in many developing countries as a mechanism for funding modernization and new technology. Not unnaturally, its swiftest development has been in South-East Asia where entrepreneurial dynamism, experienced fund managers and willing foreign capital have found in it a suitable marriage. In the more difficult circumstances of Africa venture capital, with its emphasis on equity financing, is offering an alternative to the foreign currency-backed lending of development banks which has been the classic and increasingly hazardous means of enterprise funding.

In the African context, therefore, venture capital is likely to mean principally the availability of equity funds, subscribed and remunerated in local currency. The risk element, a feature of all venture capital, will lie in the finer arts of equity as distinct from fixed income financing, and in the added difficulty of realizing capital gains in the absence of reliable exit mechanisms.

An additional risk element is the likely concentration on smaller scale projects. Whilst in the industrial countries small companies, usually with a hi-tech product, are the potential high fliers, in Africa they encounter special problems. Yet they are essential for the creation of an industrial fabric.

Special features of venture capital vehicles in Africa are likely to be -

- a modest capital base, in line with their initially experimental nature;

- high initial overhead costs, because of the need for management specialised in venture capital and its techniques, which may not be available locally;

- the need actively to stimulate a dealflow through a project development effort;

- a balancing of revenue sources with the lead times required for investments to yield dividends and eventual capital gains, and the need to widen sources of revenue beyond financial charges;

- the ability to provide management support for investee companies so as to minimize risks and accelerate returns;

- the need to stimulate the development of capital markets, formal and informal, as mechanisms for divestment;

- enlisting official support for the creation of capital markets, encouragement of the private sector, and the supply of training and other services for SMEs.

All these adaptations represent additional costs with which a venture capital vehicle in Africa will be burdened. Those which are most likely to require special funding are -

- starter funds for covering defined expenditures before an adequate revenue stream develops;

- appointment of experienced venture capital management;

- supervision and advice from a professional venture capital organisation;

- assistance from consultants specialized in identification and development of investment projects in Africa, so as to stimulate a rapid dealflow;

- assistance to investee companies with project formulation, costs of management support, introduction and supervision of financial systems, etc;

- development of capital market mechanisms;

- a possible incubator fund to cater for promising small-scale enterprises with potential to become candidates for second stage financing.

US AID's interest in supporting venture capital initiatives in Africa with funding for precisely such components is therefore likely to make a vital difference. In particular it is important for such funds to be off-balance sheet. This should enable the vehicle to demonstrate its viability within a measurable time, and thus to attract local investors for its further capital needs.

The following recommendations for a Ghana Venture Capital Company, and the financial projections for it, have been framed on this basis.

## 4.3 A NEW FORM OF FINANCING

It is important to distinguish between venture capital financing and traditional development banking. The differences concern not only the fact that venture capital is predominantly in the form of equity or quasi-equity.

More significantly, they lie in the selection of projects not for their "development value" but for their growth potential. Venture capital is the next step in the development of the African entrepreneur, rather than the economy as such. By associating him with all the modern techniques brought to bear on the management of his undertaking, new dimensions of growth and profit potential are being opened to him. In addition, he will become involved in perceptions and evaluation of risk alongside the venture capitalist.

Not everyone is likely to opt for the close association which venture capital requires. Some entrepreneurs will be reluctant to share the profits of a family concern; rather more may cavil at sharing the management of their business. A sizeable educational task therefore faces the venture capitalist. But his main function will be to assist the modernization of the productive sector and of the attitudes of those who operate within it.

## CHAPTER FIVE A GHANA VENTURE CAPITAL COMPANY (GVCC)

### 5.1 NEED AND ROLE

The need for a GVCC in the specific conditions obtaining in Ghana will be clear from the foregoing chapters. It is demonstrated essentially by the following factors -

(1) Economic recovery cannot succeed unless growth is accelerated through greatly increased private sector activity.

(2) The constraints on the financial system make it vital to inject additional financing capacity into the private sector.

(3) Equity and quasi-equity financing are the most desirable form in which to deliver new resources: it will not aggravate the problems of the banking sector; its effect would be immediate and well aimed, being linked to its own decision-making and project development capacity.

(4) Business in Ghana stands badly in need of the improved management techniques which venture capital can deliver.

(5) It is a critical moment in the resurgence of the private sector when it is important that renewed entrepreneurial initiatives should not be frustrated.

(6) There is an initial range of projects requiring finance of the kind a GVCC would exist to deliver.

(7) There is already some private interest in the creation of a GVCC, and evidence of official support for it. The Bank of Ghana has made it clear that a GVCC must be, and be seen to be, a wholly private sector vehicle.

The role of a GVCC would be to adapt the general techniques of venture capital financing to conditions prevailing in Ghana. Its position within the financial system would be between the banks and the development finance institutions, but distinct and separate from both. It would seek to compensate for their weaknesses and address the gaps left by them. It would cooperate closely with the more effective local merchant banks, as well as with foreign investment institutions supporting project development.

### 5.2 OBJECTIVES AND FUNCTIONS

Overall policy objectives would be to stimulate economic activity in the private sector by exercising the following functions -

- actively promoting opportunities for investment, particularly in small and medium-sized enterprises;
- mobilizing resources by providing a focus for local savings and investment;
- improving the efficiency of investment, and of the operations of enterprises;
- assisting entrepreneurs in developing their projects and in acquiring the skills to operate them successfully;
- concentrating on downstream industrial sectors particularly suited to the economy;
- assisting modernisation and rehabilitation, the introduction of technology to achieve export quality standards, and the observing of environmental standards.

In due course there may also be a role for a GVCC in assisting specific opportunities becoming available under the privatization programme. Similarly, it may render some assistance to NPART in divesting itself of any assets found to be active and saleable. Neither of these functions can come into play until Government overcomes the obstacles to proceeding with privatization, and reconstruction of the banking and corporate sectors is further advanced.

## 5.3 THE BUSINESS OF A GVCC

The business of a GVCC would be to provide venture capital, specializing in the productive sector of the Ghanaian economy.

GVCC would make a series of equity or equity-type investments, predominantly in production companies with above-average growth potential. It would aim to sell those investments at a profit after a number of years.

In order to achieve high growth targets, GVCC's professional management would actively supervise its investments through an involvement in the strategic planning and direction of each investee company. This would generally be achieved by representation on the company's Board but may also involve the provision of specialist advisory services.

To carry out these functions will require experienced financial management, linked to an intimate knowledge of the local market and the community. Specialist technical advice on specific sectors needs also to be available.

VC vehicles frequently also incorporate an incubator fund from which limited high-risk investments may be made in more speculative but promising small enterprises. In Ghana, the National Board for Small-Scale Industries has suggested that such an incubator fund might in due course be attached to a GVCC to support certain of its projects. The venture capital formula of intensive management support is clearly even more crucial to such enterprises, but both the fund and the additional management inputs would need to be separately financed.

## 5.4 CORPORATE STRUCTURE

Venture capital vehicles tend to take two principal forms. The first, prevalent in the USA and to some extent in Europe and Asia, is the unincorporated closed Fund. Capital contributions to the Fund are solicited by venture capital managers offering their services in putting the money to work. In relation to the Fund, the managers become general partners, with plenipotentiary powers, and the investors limited partners. At the end of the period for which the Fund was established, the assets are divided amongst all the partners, the managers benefiting from a generally substantial free share known as carried interest.

The second form is that of an "ever-green fund", usually incorporated as a limited liability company. The contributors are the shareholders, there is no liquidation date and the operations are continuous as within a normal finance company. The Board is the supreme organ, though it may delegate investment decisions to an investment committee. Management may be recruited individually or be confided to a specialised and experienced management organization.

The form chosen frequently depends upon local legislation and fiscal regimes. An unincorporated Fund may, for instance, be exempt from taxation itself; investors in it may additionally benefit from certain privileges on the income derived from it. The greatest yield normally takes the form of capital gains. A Fund implies the option of untaxed distribution of either the realized capital gain or the underlying shares themselves, whichever is more beneficial to the investor.

In the case of a GVCC it is considered that the most uncomplicated and familiar form will also be the most suitable. Venture capital techniques will in themselves be an innovation, without breaking further new ground with sophisticated structures. The latter would inevitably require special approvals under the Companies Code, and these could only lead to delay. There is nevertheless a need for certain tax privileges, even for a company, but these are on familiar grounds which also fit into a review of financial services legislation currently being conducted by the Ministry of Finance and the Bank of Ghana.

It is therefore proposed that a GVCC should be incorporated as a limited liability company under the Ghana Companies Code 1963 - Act 119.

## 5.5 THE TAX ENVIRONMENT

### 5.5.1 Income Tax

Ghana's tax structure is still rudimentary, relying basically on income tax for both personal and company taxation. Rates of company tax vary from 45% to 55%, depending upon the nature of the activity. Companies operating in banking, insurance, commerce and printing pay the highest rate; those in manufacturing pay the lowest. A minimum tax of 5% of total receipts is levied after the first 5 years of assessment (10 years for farming and mining).

The income of farming enterprises is exempted for periods varying from 3 to 10 years, depending upon the crop. Income from dealing in cocoa, coffee and sheanut is exempted indefinitely.

Other exemptions include interest on savings accounts; on bonds held by non-residents issued by Government or certain official bodies; and the first 5 years' income of real estate developers. Export rebates are granted in line with percentages of turnover earned abroad.

Ghana Investment Centre can award certain privileges under the Investment Code, but these are often not sufficiently attractive to warrant the delays involved (see Section 3.1).

Depreciation is added back to profits, but capital allowances are available in lieu thereof. The level is 75% of capital expenditure in the year of investment, and 50% of residual value in subsequent years. There is an investment allowance of 5%.

Losses cannot be carried forward, but unused capital allowances can. Provisions for bad debts are not allowable deductions.

### 5.5.2 Capital Gains Tax

Capital gains tax is payable on gains from the disposal of business assets, including goodwill, land, buildings, stocks and shares. Capital losses cannot be set off. Rates are regressive, varying from 50% for disposals in the first year of acquisition to 2.5% from the 20th year onwards. Disposal in the fourth year, likely to see the majority of a GVCC's divestment, still attracts 42.5%.

Gains on the sale of certain assets, such as dwellings, are exempt provided the proceeds are reinvested in a similar asset within one year. There is some doubt whether this could apply to stocks and shares.

### 5.5.3 Dividends

Dividends attract a flat rate of 30%. This is now a final tax, which means they are tax-paid in the hands of the receiver. Prior approval seems still to be required from the Prices and Incomes Board for any dividends declared in excess of 2.5% above the level of previous years.

### 5.5.4 Selective Alien Employment Tax

C 500,000 pa is payable in respect of each non-Ghanaian employed by a company within its immigrant quota. This does not apply to the Managing Director or CEO of a company, nor to persons employed in farming, logging, sawmilling, fishing, mining or oil prospecting; employees of Government or a statutory corporation; or employees in manufacturing industry in its first 5 years of operation.

Approvals for the employment of expatriates are relatively freely given. Problems may arise with the immigration authorities when permits have to be renewed.

## 5.6 METHODS OF GENERATING INCOME

Sources of income of a GVCC would be of four distinct types -

(a) Investment income

Principally by way of dividends, bonus issues, warrants and stock options on funds invested in equities or other forms of participations.

(b) Capital gains

Profits realized on sale or transfer of holdings to other parties once the investment has acquired sufficient value.

(c) Fixed interest

Returns from purchase of securities, loans to projects, deposits or short-term investment of surplus funds.

(d) Fees

A GVCC would raise normal fees from projects towards the costs of appraisal, negotiations and commitment of its funds, and on any additional services such as assistance with preparation of a feasibility study or business plan.

Fees would also be earned on the provision of professional services such as accounting, legal and management inputs, as well as consultancy services for assistance with export marketing, locating additional capital etc, whether provided by the GVCC's own staff or bought in.

Other fees would arise on later-stage financing through underwriting, syndication and allied financial services. The GVCC would be entitled to raising fees for investment funds procured from outsiders at any stage.

The GVCC's philosophy must be to assist its investee companies not with subsidized funds and services, but through the introduction and provision of the best and most sophisticated financial and management techniques. Though charged out at realistic rates, investee companies have to become accustomed to absorbing such costs as essential business tools and aids to their growth and profitability.

## 5.7 REQUIRED OPERATING CONDITIONS FOR A GVCC

Since the greater part of its revenues must be expected to come from the disposal of investments, the buying and selling of securities, and reinvestment of the proceeds, must be acknowledged to be the essential nature of its business. The GVCC should therefore be explicitly exempted from Capital Gains Tax on the basis that it is a dealing company. The analogy is with existing exemptions of gains on chargeable assets where the proceeds are reinvested within one year. However, the restriction that the new asset must be held for at least 5 years would also be inappropriate.

Aside from capital gains, a major part of the revenues of a GVCC will be in the form of taxed dividends. Again, because of the nature of its business, not only GVCC but also its investors should receive credit for the tax originally paid by the investee companies. For similar reasons, GVCC should not be required to submit the level of its dividend distributions to the Prices and Incomes Board for approval.

In view of the important role which a GVCC would play in stimulating economic activity, and therefore the tax base generally, it seems inappropriate that it should suffer the highest rate of income tax, in fact 10% higher than the rate for the enterprises it will assist. There is a case for a substantial reduction in this rate, especially if dividends were in practice to be treated differently from what is proposed above.

These requests should form the basis of a memorandum to the Bank of Ghana and Ministry of Finance, so that they can be taken into account in framing the new Financial Services Law.

## CHAPTER SIX VENTURE CAPITAL INITIATIVES AND OPTIONS

### 6.1 ECOBANK

Ecobank Transnational Incorporated (ETI) prides itself on being Africa's first off-shore international financial institution. It stems from an initiative by the Federation of West African Chambers of Commerce and was given official support when the Ecowas Fund agreed to take a 10% equity stake. ETI was incorporated in Togo in 1985 with an authorised capital of US$ 100 million of which US$ 31 million has been issued to shareholders in 16 countries.

Ecobank-Togo opened in 1988, Ecobank-Nigeria and Ecobank-Côte d'Ivoire in 1989, and Ecobank-Benin and Ecobank Ghana Ltd early in 1990. 1988-89 Accounts show that the Group made a promising start, even though it incurred early trading losses of nearly US$ 700,000 and exchange losses on its Naira investment of US$ 1 million. ETI now plans to open an international office in London.

The Group is go-ahead, well-managed and has innovative plans. Among these are a regional VC Fund. ETI hopes that the African Development Bank's desire to support private sector activity may make it a contributor to such a Fund. The indications are that, in view of their West African parentage and geographic presence, ETI would see themselves being approached to manage the Fund rather than to constitute it. Discussions on these possibilities are being pursued directly between US AID and ETI.

In a separate initiative, Ecobank Ghana Ltd (EBG) are exploring the possibility of creating a VC vehicle linked to their operations. Two of its Ghanaian shareholders, Ashanti Goldfields Corporation and Ghana National Petroleum Corporation, are said to be interested in supporting it. They are two of the wholly or majority government-owned entities which make up the bulk of the 42% Ghanaian holding in EBG alongside ETI's 58%.

EBG is intended to provide a full range of merchant banking services, directly and through subsidiaries such as EGB Stock Brokers Ltd and EGB Investment Managers Ltd. A captive source of VC for its clients would clearly be a useful addition. As in the case of ETI, however, whilst the concept is attractive, sufficient thought has not yet been given to the complexities of providing independent management and incorporating a vehicle with very different objectives into a banking group.

### 6.2 MERCHANT BANK (GHANA) LTD

Merchant Bank (Ghana) Ltd (MBG) was incorporated in 1971 as National Finance Merchant Bank Ltd, originally to act as the merchant banking arm of the National Investment Bank (NIB). NIB still owns 25% of its capital, alongside Government of Ghana (30%), State Insurance Corporation (15%) and Grindlays Bank plc, London (30%). Directly and indirectly through wholly-owned entities, Government therefore owns 70% of MBG.

MBG has developed a fairly full range of merchant banking activities. It also operates through a number of more specialized subsidiaries, such as National Stockbrokers Ltd, Investment Holdings Ltd, Credit Finance Ltd, Merban Forex Bureau Ltd; and it owns one-third of Home Finance Company Ltd which it also manages.

There is no doubt that MBG is an experienced group. To the extent currently possible in Ghana, it operates in the field of private placement which will be of some consequence to a VC operation. MBG no doubt sees a VC initiative as a natural extension of this activity. However, there was no evidence that any firm plans had yet been laid, or the concept elaborated in any way.

### 6.3 BANK OF GHANA

The Bank of Ghana is currently considering the report of a consultant appointed by the World Bank to examine proposals for restructuring the corporate sector. This is clearly necessary in the wake of the current reorganisation of the banking sector and the vesting in NPART of the banks' non-performing assets.

The consultants appear to have recommended the creation of a salvaging mechanism for these non-performing assets. This would take the form of a merchant banking operation capable of evaluating the assets, analyzing their intrinsic usefulness, forming them into potentially viable operational units, devising financial structures, and finally offering them to investors. In a bold extension, it is proposed that such a body should have its own financing capacity, so as to encourage outside investors with the provision of "venture capital" inputs.

In view of the rather massive challenge, the proposal is for a VC fund with a Cedi 5 billion equity, geared to Cedi 15 billion debt, to be subscribed by international financing organisations such as IFC and the bilateral institutions.

A Bank of Ghana committee, chaired by Deputy Governor Mrs Theresa Owusu, is examining the proposal. Wnen visited by the mission, she appeared to concur that it was important to separate the financing capacity from the promotional and merchant banking one. She also believed strongly that any VC initiative should not be funded directly or indirectly by Government, as this would send all the wrong signals to the private sector. She was therefore well pleased with the initiative US AID was taking, though she wanted to be reassured that any resulting VCC would cater for smaller enterprises and be prepared to look at viable projects based on restructured NPART assets.

## 6.4 COMMONWEALTH DEVELOPMENT CORPORATION/CONTINENTAL ACCEPTANCES

Commonwealth Development Corporation (CDC) is a British public corporation for investment in developing countries. Although it has been operating since 1948, its businesslike approach did not commend itself to Ghana's earlier governments. It now has a growing number of investments in Ghana, which are administered from its regional office in Abidjan. Its association with US AID goes back to the late 1960s when it administered an AID line of credit for projects in West Africa.

On the basis of its increasing involvement with smaller projects in Ghana, CDC has developed plans for a VCC. The rationale is not only the ability to make small investments without involving expensive central procedures, but also to provide the supervision, after-care and management support which such projects need. These plans are already at an advanced stage.

CDC recently helped to establish Continental Acceptances Ltd (CAL), a new merchant bank which is intended to provide specialized financial services in Ghana. These will include wholesale banking, as well as mobilizing financial resources in the money and capital markets and channelling them particularly into the production and export sector.

CAL's initial capital of US$ 3.5 million is held as to 40% by Vanguard Assurance Co Ltd (a Ghanaian private sector company), 25% by International Finance Corporation (IFC), 15% by CDC, and 10% each by Pryor, McClendon, Counts & Co, Inc (PMC) of New York and Zimbabwe Banking Corporation Ltd. Both the Chairman, Mr Edward Gyampoh, and the Managing Director and CEO, Mr Afare Donkor, have many years' experience in leading positions in the Ghanaian financial sector. They are assisted by PMC under a three-year Technical Partner Agreement.

CDC intends its involvement with CAL to be extended through the formation of a VCC. Although CDC would initially provide the majority of the capital alongside a CAL minority interest, it is intended to give CAL the opportunity to find other Ghanaian private investors at the formation stage. Indicative proportions might be CDC 60%, Ghanaians 40%, of which CAL would retain at least 10%. Underwriting arrangements for the test marketing of up to 30% have yet to be worked out, but CDC seems willing to underwrite this component itself if necessary.

The intention is to use the VCC to attract greater numbers of private investors when the fund needs stocking up. CDC estimates that the initial US$ 2 million fund is likely to be fully invested within two years. It is considered that a placement at that stage could be successfully achieved on the record which the VCC will by then have established. This will dilute CDC's holding, and that process will be further advanced when a market can be established in the shares. It is then estimated that, perhaps within five years, the time may be ripe for a full public offering.

## 6.5 THE OPTIONS

There is potential merit in all the initiatives discussed above. Ecobank, MBG and CAL are all solid institutions, led by experienced directors and staff well versed in banking and fund management operations. They are in close touch with the financial community and would therefore be able to identify investment opportunities as well as investors.

The difficulty is that venture capital operations require very different techniques from merchant banking. They demand the opposite approach from that of commercial bankers with which these bodies are staffed. It is perhaps not difficult to recruit staff experienced in VC techniques; the major hurdle lies in a recognition of the need for such staff and to give them the independence of decision-making which they would need.

A further problem arises over the nature of the subscribers. Neither Ecobank Ghana and its potential investors nor MBG would satisfy Mrs Owusu's criterion that a VCC should be not only firmly in the private sector, but also financed from non-government sources.

The first point would apply also to the CAL initiative, but the link with CDC adds the missing venture capital dimension. The private sector nature of the investors is perhaps of greater consequence for US AID, since the mainspring of the AVCP is to engage the energies of the private sector.

Neither the Ecobank nor the MBG proposal is sufficiently defined to make judgments other than on their sponsorship. Whilst it is not the function of this report to pre-empt a US AID decision on which proposal to support, its final sections take into account much of the detail which CDC and CAL have already elaborated for their own planning. This seems helpful because it is, for the time being, the only model available. It may also be justifiable on the grounds that US AID will wish to identify with the best practice available, so that any alternative proposal would need to incorporate most of the more positive features.

## CHAPTER SEVEN A POSSIBLE MODEL

### 7.1 BASIC CHARACTERISTICS

On the basis of the potential investment business already identified (see section 8.1 below) it is estimated that a resonable initial size of fund would be US$ 2 million. Although many of the proposals are illustrative, they represent the kind of project available and give an indication of the likely volume.

As has been indicated, the availability of genuinely private sector funds for investment in a GVCC is likely to be limited. Although efforts would be made to bring in Ghanaian private investors during the formation period, the majority of the capital would be subscribed from external sources.

The US$ 2 million initial fund is expected to be fully invested by the end of Year 2. Based upon a period of successful operation, a prospectus would be prepared within 18 months, and efforts to locate qualified investors begun in readiness for a stocking up of the capital.

In choosing the structure of a limited liability company, the nature of the fund will be "ever-green" and without a terminal date. Investors will, however, be expected to offer part of their holdings to the public, or for placement with new Ghanaian investors, as shares become sought after and acquire a market value, allowing them to realize an appropriate return on their investment.

### 7.2 SUBSCRIPTION OF SHARE CAPITAL

The initial investors will fully pay up their shares upon allotment. Any funds not required for immediate investment shall be invested short term by GVCC, in a manner which combines the greatest return with the least fall in value.

In order to facilitate attracting the private investor, shares should have a par value of not more than C 500 each. The minimum subscription should be equivalent to US$ 1,000, but only for so long as GVCC remains a closed company.

### 7.3 CONTROL AND MANAGEMENT

Control of GVCC will be vested in its Board. It is proposed that, in the initial phase, this should consist of six Directors. Any shareholder or group of shareholders holding between them 15% or more of the issued capital would then have the right to appoint a Director, but this might be reduced to 10% if, at the beginning, the number of Ghanaian shareholders is limited.

The management would be appointed by the Board to carry out the policy laid down by it. It may do so either by individual appointments or by entering a management contract with an experienced organisation.

It is expected that the management complement would consist initially of one expatriate manager experienced in VC operations and two qualified Ghanaian professional staff, rising to four by Year 3. They would be serviced by three secretarial/clerical staff, a bookkeeper and a driver. The management budget will include a training component, both for staff costs and a provision for training courses. It will also allow for the hire of external consultants as required for technical services and the preparation of feasibility studies.

## 7.4 ADVISORY BOARD

It is also proposed that there should be an Advisory Board to assist management in carrying out its responsibilities. This should be composed of five ranking Ghanaians of high standing in the financial community. They would be appointed by the shareholders.

Members of the Advisory Board would then be automatically available to serve as independent Directors when share ownership is widened, particularly through a public offering.

## 7.5 INVESTMENT DECISIONS

Venture capital management requires flexibility and the ability to make decisions independently and quickly. Whilst the ultimate authority for investment decisions would rest with the GVCC Board, it would in practice delegate this to the Manager. He would be required to submit investment proposals to the Advisory Board for its views before the company enters a commitment. The Board would intervene only if the Manager and the Advisory Board were unable to agree.

The manager's investment proposal will contain technical and financial information on the proposed investment, including -

- historic statistics and projected balance sheets, profit and loss accounts and cash flow statements;

- marketing concept, strategy and tactics, existing corporate structure and organization, and any proposed reorganization;

- critical aspects of the financial plan, including sources of finance and the impact of taxation;

- risk analysis of the products, markets, technology and operations generally;

- management expertise, licensing, and technology arrangements;

- investment incentives applied for;

- potential and intended exit mechanisms and a time-frame for disposal of the investment;

- a timetable for the investment of funds, and details of existing and potential investors;

- an assessment of the effect of the proposed investment on GVCC's exposure and portfolio.

## 7.6 INVESTMENT POLICY

GVCC will provide medium and longer term capital through equity type investments in Ghanaian companies which have the following characteristics -

- substantial growth potential

- potential to achieve and sustain a dominant market share, especially in a high growth market segment, in Ghana or in export markets

- potential for improving or introducing proven technology

- management with an established track record

- an effective and independent Board of Directors

- low entry investment valuation

- potential for achieving early disposal value.

In order to ensure a sound operating strategy, a detailed Policy Statement on the selection and divestment principles to be used should be adopted by the GVCC Board, and the management would be expected to follow these guidelines. Some of these are summarized below.

## 7.7 INVESTMENT OF FUND

It is expected that GVCC will invest its initial fund in approximately eight projects. Size of investment, including both equity and some lending, will not in the early years be less than US$ 100,000 or normally exceed US$ 750,000. It is expected that the initial fund will be fully invested by the end of Year 2.

## 7.8 TYPES OF HOLDINGS

GVCC will, in principle, concentrate on equity or equity type investments consisting of ordinary or preferred equity. Other forms of equity-linked investments may also be considered from time to time, to provide flexibility and to promote improved financial structuring of investee companies, so long as these are consistent with prudent operating procedures and Ghanaian law.

## 7.9 TYPES OF INVESTEE COMPANIES

GVCC will seek to invest principally alongside entrepreneurs who have proved their ability. In the early stages it will give preference to existing companies, or new ventures within experienced groups. Seed financing, investment in start-up companies, management buyouts and turnaround opportunities are not excluded but should be subject to intense scrutiny. The quality of the investee company's management should be one of the principal investment criteria.

## 7.10 INVESTMENT LIMITS

In order to spread their risks, VCCs normally adhere to the following investment limits -

- not more than 25% of the committed capital should be invested in a particular sector;

- not more than 10% of the committed capital should be invested in a single company;

- investment in a company should not exceed 49% of that company's total equity (unless exceptional circumstances cause it to be increased beyond that).

It would not be realistic to apply the first two of these until GVCC's capital has been significantly increased beyond the initial US$ 2 million.

## 7.11 FINANCIAL RETURNS

GVCC's portfolio policy should be to achieve an overall financial return on its funds which is significantly in excess of the return on low risk bank deposits. GVCC should aim to invest in companies which have the potential to achieve compound capital growth rates of 30% and above in real terms. This is equivalent to increasing the value of the investment by approximately 5 times in 6 years.

### 7.12 PARALLEL INVESTMENT

GVCC should actively seek co-financing for its investee companies, particularly from other equity investors. Attractive co-investment proposals should be brought to the notice of GVCC's shareholders who may wish to invest on an individual basis. GVCC might in time take the lead in causing other VCCs to be established for such purposes.

Parties making parallel investments would be expected to dispose of their holdings no earlier than GVCC, and substantially on the same financial terms.

### 7.13 PORTFOLIO ADMINISTRATION

Within the constraints of GVCC's budget, maximum attention should be given to the protection and development of GVCC's assets. It should play a significant role in building up the value of portfolio companies, participating in their strategic planning, operational control, key personnel recruitment and financial management.

GVCC should seek to recover from projects the full cost of assistance provided to them, in particular any legal, technical or financial services rendered or procured on their behalf.

The level of resources devoted to ailing ventures should be closely monitored, and the Board be promptly informed of all such cases and consulted on the advisability of writing down any such investments.

To facilitate strict management control, GVCC should require the submission of quarterly reports on operating results, financial position and marketing prospects, as well as of audited annual accounts from all investee companies.

GVCC should have the right to Board representation in all investee companies, this right to be exercised at the discretion of GVCC.

For each investee company, GVCC will designate a staff member to act as Investment Manager, who shall make periodic visits and report on the physical and financial progress and prospects of the company's operations.

GVCC should reserve the right to require each investee company to appoint auditors acceptable to GVCC.

GVCC should reserve the right to carry out investigations into any aspect of an investee company's activities and affairs at any time, and to require the company at its own expense to appoint members of GVCC or outside specialists to assist the investee company.

When GVCC becomes a public company, it should consider circulating a quarterly bulletin to its shareholders reporting on the growth of investee companies and the valuation of the portfolio. This will require the establishment of an independent Valuation Committee.

## 7.14 SALE OF INVESTMENTS

GVCC's income will arise mainly from the realization of capital gains on disposal of shares in investee companies. Most typically, shares will be sold at a stage when prospects of future profitability have been clearly established and are visible to potential purchasers. This will call for the exercise of judgment to ensure that profits are realized at the optimum time.

In cases where an investment does not meet its original growth expectations, and where prospects of achieving those objectives are not good, careful consideration should be given to the timely liquidation of GVCC's investment.

It is recognized that a small proportion of GVCC's investee companies may fail, but the majority should yield good returns and a minority should yield very high returns.

When disposal of an investment is under consideration, the full range of market mechanisms for valuing and promoting such transactions should be explored. In appropriate cases, GVCC may enter into subscription agreements that would give purchase options to promoters, founder shareholders or management. In such cases, a basis for share valuation should preferably be included in the subscription agreement.

GVCC, in conjunction with US AID and the authorities concerned, should assist the development of secondary and informal securities markets. This will serve to develop wider share ownership and facilitate trading and disposals for the benefit of GVCC and other investors.

Where GVCC's shares in investee companies are intended for sale to the general public, GVCC's own shareholders should be allowed an opportunity to negotiate an allocation of such shares prior to the public offering.

# CHAPTER EIGHT GVCC FINANCIAL MODEL

## 8.1 BUSINESS IDENTIFIED

The US AID Mission brought the mission in contact with about a dozen private entrepreneurs. The majority were preparing to expand or diversify their undertakings; others intend to install new machinery to become more competitive. Activities covered export-oriented agriculture and processing, forestry and furniture manufacture, milling, metal fabricating, carpets, a medical clinic and a variety of services.

Their total capital requirement was generally in the US$ 200,000 - 500,000 range, but in two cases up to US$ 1 million. Most were anxious to find co-investors, particularly in view of the dearth of working capital. Expected returns were said to be 30 - 40%, with pay-back periods likely to be up to 5 years.

Inter-Afrique Holdings Ltd (IAHL), a rapidly growing Ghanaian business group with which RIO is associated on project work, also explained their plans for further expansion and subsidiaries. In addition to commodity trading and the Compaq computer agency, they are in joint venture with the UK Motherwell Bridge engineering group and with the Swiss-based Panalpina Worldwide.

IAHL will be an investor in the Second Discount House. It also has plans for computer expansion, and a cassava plantation to produce starch and glucose. A recently formed partnership between IAHL and United Guarantee plc in London has bought a 1,000-acre farm which RIO is helping to develop into a major producer of pineapple. These initiatives are also likely to provide interesting investment opportunities.

RIO is also engaged on a number of forestry and woodworking projects, including furniture for export. Having been commissioned by APDF to prepare the feasibility studies, RIO is now assisting the physical development of the projects. They, too, will shortly be requiring capital inputs.

Merchant Bank (Ghana) is advising promoters of two projects, in tuna packing and the expansion of a fruit juicing business.

CDC is at an advanced stage with the appraisal of three projects in the fields of fish and seafood exports, aluminium extrusions, and the construction of low-cost housing with newly developed technology. It has also begun examining three others, in poultry feed, cotton production and processing, and furniture export. Its intention to set up a VCC is based on the attractiveness of these projects; but costs of appraisal and negotiation from London and Abidjan are out of all proportion to the size of the individual investment.

A new financing vehicle will always find an accumulation of project proposals, either because everyone else has rejected them or, as is the case in Ghana, the existing financial system is inadequate. However, their existence confirms that there is a good level of private sector project development activity. This underlines the need for GVCC, as well as the likelihood of its having an adequate dealflow in the early stages. If the CDC/CAL option were chosen, there would by then be three fully appraised and negotiated investments ready to hand.

## 8.2 ILLUSTRATIVE FINANCIAL FLOWS

From all these proposals it has been possible to construct a set of illustrative investment profiles. These are shown at Annex A, Table I. Together with the projected rate of investment in Table II, and estimated operating costs in Table III, they form the basis for the financial projections shown in Tables IV - VII.

It is important to understand that these calculations do not represent forecasts. The mission has not been able to analyze the potential projects in depth to satisfy itself that they can reach the high capital growth required. Also the rate at which future investments will be identified and made can only be stated as a target.

Based on these assumptions, Table IV illustrates potential profits, taking into account a likely rate of accrual of capital gains from the sale of investments. It has been assumed that the operating conditions set out in Section 5.7 will be granted and that no capital gains tax will be payable on these.

The projections assume that US AID will make the inputs at its disposal under the Africa Venture Capital Project in order to support in particular the management capsule over the first three years. These inputs are set out in detail in Chapter 9 below.

Profits accruing from Year 3 are assumed to be retained until Year 5, by which time the investment portfolio will have reached US$ 7 million. A first dividend around that point will be an encouragement for investors to participate in a substantial new capital issue.

It should be noted that, without the AID contributions, the investment portfolio at the end of Year 5 would stand at no more than US$ 3.6 million and both revenues and profitability would be correspondingly reduced.

On the basis of these and the more detailed assumptions in Section 8.3 below, total capital employed and cumulative distributions to shareholders are US$ 44.4 million by the end of Year 10. For the original investors and those in Year 2 this represents an internal rate of return (IRR) of 23%. For the new subscribers in Year 5, the IRR in Year 10 is 20%.

## 8.3 DETAILED ASSUMPTIONS

### 8.3.1 ACCOUNTING POLICIES

Accounting convention Figures in constant 1990 US$.

Turnover Turnover comprises investment income, being dividends and capital gains received, less capital losses, and interest from short and longer term investment.

Fixed assets Costs of establishing GVCC are estimated at US$ 166,000; they are capitalized and depreciated over 5 years.

Investment in investee companies Investments are valued at cost. No capital gains or losses are taken into the balance sheet until they are realized. Term loans made to investee companies are not shown separately from equity investments, given that the periods for loan repayment and equity disposals are roughly similar.

### 8.3.2 UNDERLYING ASSUMPTIONS

Illustrative Financing Plan

A single call on share capital for US$ 2 million is assumed on formation. A further issue of US$ 3 million would be expected at the end of Year 2. Investment approvals over Years 1 - 3 would be at the rate of US$ 1.5 million pa, and at US$ 2 million pa thereafter until reinvestments allow the rate to be progressively improved. Disbursements have been taken at US$ 1 million pa over years 1 and 2, US$ 1.5 million pa in Years 3 and 4, rising to US$ 2 million pa thereafter. That means a further issue to raise as much as US$ 10 million in Year 5.

The new shares offered at the end of Year 2 will be marketed at a premium of 33%, and those at the end of Year 5 at a premium of 60%.

The balance of funds awaiting investment will be available for short-term investment as bank deposits or other forms of risk-free commercial instruments, and as working capital.

Illustrative assumptions for investee company performance

Section B of Table I shows the six types of projects in which GVCC's resources will be invested. These are considered typical of those generally available to and made by VC companies. Capital value is in constant terms.

Type I investments are in companies which for one reason or another fail to implement their business plan, become insolvent and cease trading or require substantial restructuring or refinancing within three years. These circumstances are commonplace for VC companies and it is assumed that initially 10% of GVCC's investments will be of this type. This is reduced to 5% from Year 3 onwards as GVCC gains in experience.

Type II investments are assumed to be in companies with modest annual growth of 12%, yielding dividends from the third year of operation. They should be divested in Year 5. These profiles are typical of companies which, at the time of investment, have excellent growth prospects but fail to meet them for technical or managerial reasons.

Types III, IV and V are investments with compound annual growth of 20%, 30% and 40% respectively over a period of 5 to 6 years. Type IV also achieves a good dividend stream. Initially 20% of GVCC's funds will be invested in Types II, III, IV and V. From Year 3 investment in Types III, IV and V increases by 2.5% as the number of Type I investments is reduced.

Type VI investments are highly successful companies showing average growth of 50% pa and a high dividend stream. It is assumed that 10% of GVCC's funds are placed in this type of investment, rising to 12.5% in Year 3.

Management and other fees earned from investee companies are assumed to accrue at 5% of total investment in each of Years 1 - 5, and at 3% thereafter.

On the basis of these assumptions, the overall FIIR realized from the investments over a 10-year period is 36%.

It is assumed that all income received on divestment is reinvested, aside from dividend distributions equivalent to 50% of available profits from Year 6 onwards.

All investments are assumed to be made on the first day of the year, and all divestments on the last day of the year.

Table II shows the illustrative investment income based on the above assumptions. Section I of Table II shows the portfolio value as it appears in the balance sheet, ie at cost taking into account divestments made. Section J is used to calculate the remaining realizeable assets at the end of the period.

Capital investment, replacement and depreciation

No capital investment is assumed, other than capitalized start-up costs of US$ 166,000 written off over 5 years.

Operating expenditure

Details of operating expenditure are shown in Table III. As discussed in Chapter 9 below, they are assumed to be offset over the first three years by annual grants from US AID.

Provision for debtors is 6 months for interest from short-term investments and dividends, and 12 months for capital gains from sale of investments.

## 8.4 SENSITIVITY ANALYSIS

Major variables are the performance of investee companies and the assumption that the right operating conditions will be available, notably exemption from capital gains tax.

The base case model used here shows a total FIIR from investee companies of 36%, assuming no capital gains tax is payable.

If tax were payable on capital gains from investee companies at the rate of 42.5% applicable to assets held for 4 years, the FIIR to the original investors would be 18%, to the Year 2 investors 16%, and to the Year 5 investors 11%. The incidence of income tax on fee income would not affect the return significantly.

If there were a 10% reduction in performance, the return offered to investors would still be considered attractive.

As discussed in Section 8.2 above, the most critical variable for GVCC's prospects lies in the US AID support. This is likely to make the crucial difference to GVCC's ability to offer Ghanaian private investors an early and acceptable level of risk remuneration.

# CHAPTER NINE SCOPE FOR INPUTS FROM US AID'S AVCP

## 9.1 GVCC'S ESTABLISHMENT COSTS

| Incorporation expenses | US$ |
|---|---|
| Legal fees | 40,000 |
| Prospectus, printing | 4,000 |
| Statutory fees, licences | 4,300 |
| Capital duty | 2,000 |
| Placement fees | 18,000 |
| Contingencies | 6,700 |
| | 75,000 |

| Capital items | |
|---|---|
| Air conditioning | 7,500 |
| Telephone, fax, telex | 7,000 |
| Furniture, copier, computers | 28,500 |
| Vehicles | 40,000 |
| Contingencies | 8,000 |
| | 91,000 |

| | |
|---|---|
| Total establishment costs | 166,000 |
| Amortization over 5 years, say | 33,000 pa. |

## 9.2 GVCC'S OPERATING COSTS

Staff (all-in costs) US$ '000

| | Year 1 | Year 2 | Year 3 |
|---|---|---|---|
| Manager | 145 | 145 | 145 |
| Ghanaian professionals | 80 | 120 | 160 |
| Secretarial/clerical | 20 | 40 | 60 |
| Bookkeeper | 20 | 20 | 30 |
| Driver | 15 | 15 | 30 |
| | 280 | 340 | 425 |
| Training costs | 33 | 33 | 33 |
| Misc. Consultancies (incl. US VC Adviser) | 100 | 150 | 200 |
| | 413 | 523 | 658 |

Office US$

| | Year 1 | Year 2 | Year 3 |
|---|---|---|---|
| Office rental | 5,500 | 5,500 | 10,000 |
| Electricity, water | 5,300 | 6,500 | 8,000 |
| Telephone | 17,500 | 20,000 | 30,000 |
| Professional fees | 10,000 | 15,000 | 20,000 |
| Subscriptions | 2,000 | 4,000 | 4,000 |
| Audit, accountancy | 10,000 | 10,000 | 15,000 |
| Vehicle running | 3,500 | 4,000 | 8,000 |
| Insurances | 8,000 | 8,000 | 12,000 |
| | 61,800 | 73,000 | 107,000 |
| Amortization of establishment costs | 33,000 | 33,000 | 33,000 |
| Total operating costs | 507,800 | 629,000 | 798,000 |

From the financial projections it is clear that absorption of these amounts by GVCC would involve a period of initial losses. These in turn would reduce the funds available for investment and lead to unnecessary finance charges. Total portfolio at the end of Year 5 would be US$ 3.6 million instead of US$ 7 million, with a consequent reduction in revenues and profitability.

All these factors would militate against GVCC's plans for raising local capital, even at the formation stage.

It is therefore considered that a US AID contribution of these amounts over a three-year period would enable GVCC -

a) to be set up with a staff complement necessary for a rapid build-up of its operations;

b) quickly to reach the several points where more substantial local investment can be brought in;

c) to demonstrate the profitability of its operations so as to attract a measure of local investment already from the outset;

d) in this way to achieve an increasingly important leverage of Ghanaian funds;

e) to make a more effective contribution to the development of its investee companies by having adequate staff for management assistance.

These possibilities coincide closely with the principal objectives of the Africa Venture Capital Project. A partnership of the kind outlined above between US AID and other organizations prepared to use their own resources to promote venture capital would enable US AID itself to leverage very substantial direct and indirect contributions of capital.

## 9.3 RELATED ACTIVITIES

If the AVCP budget allows, there are further tasks to be undertaken. The need for these has already been explained in Section 4.2 above. The first is to ensure that the capital market in Ghana, particularly the secondary and informal, develops in such a way as to facilitate the operations of GVCC.

A second would be to assist the examination of non-performing assets as a potential basis for new project development.

A third would in due course be to assist the establishment of additional VC funds, on the principle that such funds help to support each other, rather than being competitive.

A fourth could be to foster the development of local consultants and professional advisers, to cater for the growing needs of the private sector for such services. GVCC, together with some of the other actions suggested here, would pose an increasing need for these, and a growing ability by entrepreneurs to pay for them on a commercial basis.

Lastly, the concept of an incubator fund to assist small enterprises having the potential to come to GVCC for second-stage financing deserves to be explored.

These additional activities are peripheral to GVCC but clearly relate closely to its operations. It is for consideration whether they should be sited within GVCC or mounted separately.

Such activities would require further financial support in the short term. They would, however, constitute highly appropriate expenditures under - or in association with - AVCP. Comprehensive support in all these ways should enable US AID to achieve in Ghana a convincing and successful demonstration of the principles on which the AVCP is based.

## CHAPTER TEN ACKNOWLEDGEMENTS

The mission was greatly facilitated by the US AID Mission Director, Joseph Goodwin, and his staff, in particular Edward Birgells and Daniel Gyimah. Their recognition of the crucial role of the private sector in the Ghanaian economy, and their contacts within it as well as among officials at all levels, enabled us to conduct the assignment swiftly, effectively and agreeably. We also much appreciated the interest and support of the Ambassador, Hon Raymond Ewing.

We were received with openness and goodwill by a great variety of leaders in Government and the private sector. From Governor Agama through to the members of the industry associations, the visit caused genuine and lively interest.

The co-operation of the financial sector, in particular the CEOs of CAL, Ecobank and Merchant Bank (Ghana) and the West Africa Representative of CDC, gave us considerable assistance in assessing the practical opportunities for a GVCC.

A personal appreciation is due to Richard Loth for making the assignment both smooth and agreeable, and with his energies ensuring that it should bear early and concrete results.

TABLE I: GVCC - ILLUSTRATIVE ASSUMPTIONS FOR VENTURE CAPITAL INVESTMENTS

| :nt 1990 US$000's) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| **VESTMENT OF INITIAL CAPITAL** | | | | | | | | | | |
| pe I Investments | 105 | 105 | 75 | 75 | 97.5 | 97.5 | 98 | 98 | 105 | 0 |
| pe II Investments | 210 | 210 | 309 | 309 | 401.7 | 401.7 | 402 | 402 | 433 | 0 |
| pe III Investments | 210 | 210 | 309 | 309 | 401.7 | 401.7 | 402 | 402 | 433 | 0 |
| pe IV Investments | 210 | 210 | 309 | 309 | 401.7 | 401.7 | 402 | 402 | 433 | 0 |
| pe V Investments | 210 | 210 | 311 | 311 | 403.65 | 403.65 | 404 | 404 | 435 | 0 |
| pe VI Investments | 105 | 105 | 188 | 188 | 243.75 | 243.75 | 244 | 244 | 263 | 0 |
| tal Investment of Initial Capital | 1,050 | 1,050 | 1,500 | 1,500 | 1950 | 1950 | 1,950 | 1,950 | 2,100 | 0 |
| mulative Investment | 1,050 | 2,100 | 3,600 | 5,100 | 7050 | 9000 | 10,950 | 12,900 | 15,000 | 15,000 |

| VESTMENT PROFILES | 1st Year | 2nd Year | 3rd Year | 4th Year | 5th Year | 6th Year | 7th Year | 8th Year | 9th Year | 10th Year |
|---|---|---|---|---|---|---|---|---|---|---|
| **PE I INVESTMENTS** | | | | | | | | | | |
| vestment Period (Years) | 3 | | | | | | | | | |
| vidend (% per Year) | 0 | 0 | 0 | | | | | | | |
| pital Value (% of Initial Investment) | 50 | 25 | 0 | | | | | | | |
| **PE II INVESTMENTS** | | | | | | | | | | |
| vestment Period (Years) | 5 | | | | | | | | | |
| vidend (% per Year) | 0 | 0 | 5 | 5 | 5 | | | | | |
| :ital Value (% of Initial Investment) | 112 | 125 | 140 | 157 | 176 | | | | | |
| **E III INVESTMENTS** | | | | | | | | | | |
| estment Period (Years) | 5 | | | | | | | | | |
| :idend (% per Year) | 0 | 0 | 5 | 8 | 8 | | | | | |
| :tal Value (% of Initial Investment) | 120 | 144 | 173 | 207 | 249 | | | | | |
| **E IV INVESTMENTS** | | | | | | | | | | |
| estment Period (Years) | 6 | | | | | | | | | |
| :dend (% per Year) | 0 | 5 | 8 | 10 | 10 | 10 | | | | |
| :tal Value (% of Initial Investment) | 130 | 169 | 220 | 286 | 371 | 483 | | | | |
| **E V INVESTMENTS** | | | | | | | | | | |
| estment Period (Years) | 6 | | | | | | | | | |
| .dend (% per Year) | 0 | 0 | 0 | 5 | 8 | 8 | | | | |
| .tal Value (% of Initial Investment) | 140 | 196 | 274 | 384 | 538 | 753 | | | | |
| **E VI INVESTMENTS** | | | | | | | | | | |
| stment Period (Years) | 6 | | | | | | | | | |
| :dend (% per Year) | 0 | 5 | 10 | 15 | 15 | 15 | | | | |
| tal Value (% of Initial Investment) | 150 | 225 | 338 | 506 | 759 | 1139 | | | | |

| ESTMENT OF INCOME FROM FUND | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| estment in Type I (% of Income) | .0 | .0 | .0 | .0 | .0 | 2.5 | 2.5 | 2.5 | 2.5 | 3.5 |
| estment in Type II (% of Income) | .0 | .0 | .0 | .0 | .0 | 10.3 | 10.3 | 10.3 | 10.3 | 14.4 |
| estment in Type III (% of Income) | .0 | .0 | .0 | .0 | .0 | 10.3 | 10.3 | 10.3 | 10.3 | 14.4 |
| estment in Type IV (% of Income) | .0 | .0 | .0 | .0 | .0 | 10.3 | 10.3 | 10.3 | 10.3 | 14.4 |
| estment in Type V (% of Income) | .0 | .0 | .0 | .0 | .0 | 10.3 | 10.3 | 10.3 | 10.3 | 14.4 |
| estment in Type VI (% of Income) | .0 | .0 | .0 | .0 | .0 | 6.3 | 6.3 | 6.3 | 6.3 | 3.8 |
| Percentage of Income Reinvested | .0 | .0 | .0 | .0 | .0 | 50.0 | 50.0 | 50.0 | 50.0 | 70.0 |
| :e Used for Operational Funding, ion and Appropriated Profits | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 50.0 | 50.0 | 50.0 | 50.0 | 30.0 |
| **TERM INTEREST RATES ON INITIAL FUNDS UNINVESTED** | | | | | | | | | | |
| Term Interest Rate (%) | 10 | 10 | 10 | 10 | 10 | 10 | 10 | 10 | 10 | 10 |
| tage of Available Funds Invested | 80 | 0 | 50 | 0 | 80 | 70 | 50 | 50 | 0 | 0 |

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TABLE II : GVCC - ILLUSTRATIVE VENTURE CAPITAL INVESTMENT

| US$ ('000's) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| ESTMENTS | | | | | | | | | | |
| vestment | 105 | 105 | 75 | 75 | 98 | 98 | 98 | 98 | 105 | 0 |
| s from Fund Income | 0 | 0 | 0 | 0 | 0 | 29 | 126 | 138 | 196 | 294 |
| stments | 105 | 105 | 75 | 75 | 98 | 126 | 223 | 236 | 301 | 294 |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| come | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| ins | 0 | 0 | (105) | (105) | -75 | -75 | (98) | (126) | (223) | (236) |
| e | 0 | 0 | (105) | (105) | -75 | -75 | (98) | (126) | (223) | (236) |
| VESTMENTS | | | | | | | | | | |
| vestment | 210 | 210 | 309 | 309 | 402 | 402 | 402 | 402 | 433 | 0 |
| s from Fund Income | 0 | 0 | 0 | 0 | 0 | 118 | 519 | 570 | 807 | 1,213 |
| stments | 210 | 210 | 309 | 309 | 402 | 520 | 921 | 972 | 1,240 | 1,213 |
| | 0 | 0 | 0 | 0 | 370 | 370 | 545 | 545 | 708 | 916 |
| come | 0 | 0 | 11 | 21 | 36 | 41 | 51 | 62 | 92 | 121 |
| ins | 0 | 0 | 0 | 0 | 160 | 160 | 236 | 236 | 306 | 396 |
| e | 0 | 0 | 11 | 21 | 197 | 201 | 287 | 297 | 398 | 517 |
| VESTMENTS | | | | | | | | | | |
| vestment | 210 | 210 | 309 | 309 | 402 | 402 | 402 | 402 | 433 | 0 |
| s from Fund Income | 0 | 0 | 0 | 0 | 0 | 118 | 519 | 570 | 807 | 1,213 |
| tments | 210 | 210 | 309 | 309 | 402 | 520 | 921 | 972 | 1,240 | 1,213 |
| | 0 | 0 | 0 | 0 | 523 | 523 | 769 | 769 | 1,000 | 1,294 |
| come | 0 | 0 | 11 | 27 | 49 | 57 | 70 | 83 | 120 | 164 |
| ns | 0 | 0 | 0 | 0 | 313 | 313 | 460 | 460 | 598 | [illegible] |
| e | 0 | 0 | 11 | 27 | 362 | 370 | 529 | 543 | 718 | 938 |
| ESTMENTS | | | | | | | | | | |
| estment | 210 | 210 | 309 | 309 | 402 | 402 | 402 | 402 | 433 | 0 |
| from Fund Income | 0 | 0 | 0 | 0 | 0 | 118 | 519 | 570 | 807 | 1,213 |
| tments | 210 | 210 | 309 | 309 | 402 | 520 | 921 | 972 | 1,240 | 1,213 |
| | 0 | 0 | 0 | 0 | 0 | 1014 | 1,014 | 1,491 | 1,491 | 1,939 |
| come | 0 | 11 | 27 | 53 | 82 | 118 | 141 | 190 | 245 | 224 |
| ns | 0 | 0 | 0 | 0 | 0 | 804 | 804 | 1,182 | 1,182 | [illegible] |
| e | 0 | 11 | 27 | 53 | 82 | 921 | 945 | 1,372 | 1,428 | 1,361 |
| STMENTS | | | | | | | | | | |
| estment | 210 | 210 | 311 | 311 | 404 | 404 | 404 | 404 | 435 | 0 |
| from Fund Income | 0 | 0 | 0 | 0 | 0 | 118 | 519 | 570 | 807 | 1,213 |
| tments | 210 | 210 | 311 | 311 | 404 | 522 | 923 | 974 | 1,242 | 1,213 |
| | 0 | 0 | 0 | 0 | 0 | 1581 | 1,581 | 2,338 | 2,338 | 3,039 |
| come | 0 | 0 | 0 | 11 | 27 | 49 | 57 | 70 | 83 | 120 |
| ns | 0 | 0 | 0 | 0 | 0 | 1371 | 1,371 | 2,027 | 2,027 | 2,636 |
| e | 0 | 0 | 0 | 11 | 27 | 1420 | 1,428 | 2,097 | 2,111 | 2,756 |

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TABLE II : GVCC - ILLUSTRATIVE VENTURE CAPITAL INVESTMENT (contd)

| Constant 1990 US$ ('000's) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| **TYPE VI INVESTMENTS** | | | | | | | | | | |
| Initial Investment | 105 | 105 | 188 | 188 | 244 | 244 | 244 | 244 | 263 | 0 |
| Investments from Fund Income | 0 | 0 | 0 | 0 | 0 | 72 | 317 | 349 | 494 | 740 |
| Total Investments | 105 | 105 | 188 | 188 | 244 | 316 | 561 | 592 | 756 | 740 |
| Divestment | 0 | 0 | 0 | 0 | 0 | 1196 | 1,196 | 2,136 | 2,136 | 2,776 |
| Dividend Income | 0 | 5 | 16 | 36 | 60 | 91 | 112 | 152 | 198 | 280 |
| Capital Gains | 0 | 0 | 0 | 0 | 0 | 1091 | 1,091 | 1,948 | 1,948 | 2,533 |
| Total Income | 0 | 5 | 16 | 36 | 60 | 1182 | 1,203 | 2,101 | 2,146 | 2,813 |
| **TOTAL INVESTMENTS AND INCOME** | | | | | | | | | | |
| Total Investments | 1,050 | 1,050 | 1,500 | 1,500 | 1950 | 2524 | 4,470 | 4,718 | 6,017 | [illegible] |
| Total Divestments | 0 | 0 | 0 | 0 | 893 | 4683 | 5,104 | 7,279 | 7,673 | 9,964 |
| Total Dividends | 0 | 16 | 64 | 148 | 255 | 356 | 431 | 556 | 738 | 1,009 |
| Capital Losses | 0 | 0 | (105) | (105) | -75 | -75 | (98) | (126) | (223) | [illegible] |
| Total Capital Gains | 0 | 0 | 0 | 0 | 473 | 3738 | 3,961 | 5,854 | 6,062 | [illegible] |
| Total Investment Income | 0 | 16 | (41) | 43 | 652 | 4019 | 4,295 | 6,284 | 6,577 | 8,645 |
| Total Funds Available for Reinvestment | 0 | 16 | 64 | 148 | 1147 | 5039 | 5,535 | 7,835 | 8,411 | [illegible] |
| **PORTFOLIO AT COST DURING YEAR** | | | | | | | | | | |
| Type I Investments | 105 | 210 | 285 | 255 | 248 | 299 | 447 | 586 | 760 | [illegible] |
| Type II Investments | 210 | 420 | 729 | 1,038 | 1440 | 1750 | 2,460 | 3,123 | 4,054 | [illegible] |
| Type III Investments | 210 | 420 | 729 | 1,038 | 1440 | 1750 | 2,460 | 3,123 | 4,054 | [illegible] |
| Type IV Investments | 210 | 420 | 729 | 1,038 | 1440 | 1960 | 2,670 | 3,432 | 4,363 | [illegible] |
| Type V Investments | 210 | 420 | 731 | 1,041 | 1445 | 1966 | 2,679 | 3,443 | 4,374 | [illegible] |
| Type VI Investments | 105 | 210 | 398 | 585 | 829 | 1145 | 1,601 | 2,088 | 2,657 | [illegible] |
| Total Investments | 1,050 | 2,100 | 3,600 | 4,995 | 6840 | 8869 | 12,318 | 15,795 | 20,262 | [illegible] |
| **PORTFOLIO AT COST AT YEAR END** | | | | | | | | | | |
| Type I Investments | 105 | 210 | 180 | 150 | 173 | 224 | 350 | 459 | 537 | [illegible] |
| Type II Investments | 210 | 420 | 729 | 1,038 | 1230 | 1540 | 2,151 | 2,814 | 3,652 | 4,345 |
| Type III Investments | 210 | 420 | 729 | 1,038 | 1230 | 1540 | 2,151 | 2,814 | 3,652 | 4,345 |
| Type IV Investments | 210 | 420 | 729 | 1,038 | 1440 | 1750 | 2,460 | 3,123 | 4,054 | 4,365 |
| Type V Investments | 210 | 420 | 731 | 1,041 | 1445 | 1756 | 2,469 | 3,132 | 4,064 | [illegible] |
| Type VI Investments | 105 | 210 | 398 | 585 | 829 | 1040 | 1,496 | 1,901 | 2,470 | 2,966 |
| Total Investments | 1,050 | 2,100 | 3,495 | 4,890 | 6345 | 7849 | 11,078 | 14,244 | 18,428 | 21,989 |
| **PORTFOLIO AT REALISABLE VALUE AT YEAR END** | | | | | | | | | | |
| Type I Investments | 53 | 79 | 64 | 56 | 68 | 87 | 143 | 174 | 209 | 222 |
| Type II Investments | 235 | 499 | 905 | 1,359 | 1972 | 2377 | 3,278 | 4,150 | 5,427 | 6,544 |
| Type III Investments | 252 | 554 | 1,036 | 1,614 | 2419 | 2900 | 3,957 | 4,992 | 6,556 | 8,123 |
| Type IV Investments | 273 | 628 | 1,218 | 1,985 | 3103 | 4709 | 6,002 | 7,748 | 9,744 | 12,306 |
| Type V Investments | 294 | 706 | 1,423 | 2,426 | 3962 | 6277 | 7,866 | 10,162 | 12,692 | 16,194 |
| Type VI Investments | 158 | 394 | 872 | 1,589 | 2749 | 4598 | 5,945 | 8,012 | 9,948 | 12,828 |
| Total Investments | 1,264 | 2,859 | 5,517 | 9,030 | 14272 | 20948 | 27,191 | 35,238 | 44,576 | [illegible] |

## TABLE III : GWCC - ILLUSTRATIVE OPERATING EXPENDITURE

| | Unit Co ('000's US$) | Uni | Year 0 | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 |
|---|---|---|---|---|---|---|---|---|---|---|
| RATING EXPENDITURE QUANTITIES | | | | | | | | | | |
| ager | 145.0 | Year | .0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1. |
| naian professionals | 40.0 | Year | .0 | 2.0 | 3.0 | 4.0 | 4.0 | 4.0 | 4.0 | 4. |
| retarial/clerical | 20.0 | Year | .0 | 1.0 | 2.0 | 3.0 | 3.0 | 3.0 | 3.0 | 3. |
| keeper | 20.0 | Year | .0 | 1.0 | 1.0 | 1.5 | 1.5 | 1.5 | 1.5 | 1. |
| ver | 15.0 | Year | .0 | 1.0 | 1.0 | 2.0 | 2.0 | 2.0 | 2.0 | 2. |
| ining Costs | 33.0 | Year | .0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1. |
| : consultancies | 30.0 | man month | .0 | 3.5 | 5.0 | 6.0 | 6.0 | 6.0 | 6.0 | 6. |
| ice rental | 5.5 | Year | .0 | 1.0 | 1.0 | 2.0 | 2.0 | 2.0 | 2.0 | 2. |
| :, water | 5.0 | Year | .0 | 1.0 | 1.2 | 1.5 | 1.5 | 1.5 | 1.5 | 1. |
| ephone | 30.0 | Year | .0 | .5 | .7 | 1.0 | 1.0 | 1.0 | 1.0 | 1. |
| fessional Fees | 20.0 | Year | .0 | .5 | .7 | 1.0 | 1.0 | 1.0 | 1.0 | 1. |
| scriptions | 2.0 | Year | .0 | 1.0 | 2.0 | 2.0 | 2.0 | 2.0 | 2.0 | 2. |
| lt,accountancy | 15.0 | Year | .0 | .7 | .7 | 1.0 | 1.0 | 1.0 | 1.0 | 1. |
| icle running costs | 4.0 | Year | .0 | 1.0 | 1.0 | 2.0 | 2.0 | 2.0 | 2.0 | 2. |
| rances | 8.0 | Year | .0 | 1.0 | 1.0 | 1.5 | 1.5 | 1.5 | 1.5 | 1. |
| | .0 | Year | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |

| . 1990 US$ ('000's) | Year 0 | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 |
|---|---|---|---|---|---|---|---|---|
| ATING EXPENDITURE | | | | | | | | |
| ger | .0 | 145.0 | 145.0 | 145.0 | 145.0 | 145.0 | 145.0 | 145. |
| aian professionals | .0 | 80.0 | 120.0 | 160.0 | 160.0 | 160.0 | 160.0 | 160. |
| etarial/clerical | .0 | 20.0 | 40.0 | 60.0 | 60.0 | 60.0 | 60.0 | 60. |
| eeper | .0 | 20.0 | 20.0 | 30.0 | 30.0 | 30.0 | 30.0 | 30. |
| er | .0 | 15.0 | 15.0 | 30.0 | 30.0 | 30.0 | 30.0 | 30. |
| ning Costs | .0 | 33.0 | 33.0 | 33.0 | 33.0 | 33.0 | 33.0 | 33. |
| consultancies | .0 | 105.0 | 150.0 | 180.0 | 180.0 | 180.0 | 180.0 | 180. |
| ce rental | .0 | 5.5 | 5.5 | 11.0 | 11.0 | 11.0 | 11.0 | 11. |
| , water | .0 | 5.0 | 6.0 | 7.5 | 7.5 | 7.5 | 7.5 | 7. |
| phone | .0 | 15.0 | 21.0 | 30.0 | 30.0 | 30.0 | 30.0 | 30. |
| essional Fees | .0 | 10.0 | 14.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20. |
| criptions | .0 | 2.0 | 4.0 | 4.0 | 4.0 | 4.0 | 4.0 | 4. |
| t,accountancy | .0 | 10.5 | 10.5 | 15.0 | 15.0 | 15.0 | 15.0 | 15. |
| cle running costs | .0 | 4.0 | 4.0 | 8.0 | 8.0 | 8.0 | 8.0 | 8. |
| rances | .0 | 8.0 | 8.0 | 12.0 | 12.0 | 12.0 | 12.0 | 12. |
| | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |
| | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |
| | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |
| | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |
| | .0 | .0 | .0 | .0 | .0 | .0 | .0 | . |
| ingencies at 10 Percent | .0 | 59.6 | 59.6 | 74.6 | 74.6 | 74.6 | 74.6 | 74. |
| l Operating Expenditure | .0 | .0 | .0 | .0 | 820.1 | 820.1 | 820.1 | 820. |

TABLE IV : GWCC - ILLUSTRATIVE PROFIT AND LOSS ACCOUNT

| 990 US$ ('000's) | Year 0 | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| E | | | | | | | | | | | |
| from Investments and Fees | 0 | 129 | 121 | 209 | 292 | 1,630 | 4,705 | 4,867 | 6,863 | 7,185 | 9,378 |
| Capital Losses | | | | | | | | | | | |
| ING COSTS | | | | | | | | | | | |
| : Capital Overhead and Investment ment Costs | 0 | 0 | 0 | 0 | 820 | 820 | 820 | 820 | 820 | 820 | 820 |
| ING PROFIT | 0 | 129 | 121 | 209 | ( 528) | 810 | 3,885 | 4,047 | 6,043 | 6,365 | 8,558 |
| ATION | 0 | 29 | 29 | 29 | 29 | 29 | 4 | 4 | 4 | 4 | 4 |
| (LOSS) BEFORE FINANCE CHARGES | 0 | 100 | 92 | 181 | ( 556) | 782 | 3,881 | 4,042 | 6,038 | 6,360 | 8,553 |
| : CHARGES | | | | | | | | | | | |
| t and Charges on Term Loans | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| t on Overdraft | 0 | 0 | 14 | 0 | 35 | 0 | 0 | 0 | 0 | 0 | 0 |
| inance Charges | 0 | 0 | 14 | 0 | 35 | 0 | 0 | 0 | 0 | 0 | 0 |
| (LOSS) BEFORE TAX | 0 | 100 | 78 | 181 | ( 591) | 782 | 3,881 | 4,042 | 6,038 | 6,360 | 8,553 |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| (LOSS) AFTER TAX | 0 | 100 | 78 | 181 | ( 591) | 782 | 3,881 | 4,042 | 6,038 | 6,360 | 8,553 |
| ATION OF PROFITS | | | | | | | | | | | |
| ds | 0 | 0 | 0 | 0 | 0 | 0 | 1,940 | 2,021 | 3,019 | 3,180 | 4,277 |
| rred to Reserves | 0 | 100 | 78 | 181 | ( 591) | 782 | 1,940 | 2,021 | 3,019 | 3,180 | 4,277 |
| | 0 | 100 | 78 | 181 | ( 591) | 782 | 3,881 | 4,042 | 6,038 | 6,360 | 8,553 |
| distributions as % Profits | .00 | .00 | .00 | .00 | .00 | .00 | 50.00 | 50.00 | 50.00 | 50.00 | 50.00 |
| | | | 0 | 0 | 0 | 0 | 1,940 | 2,021 | 3,019 | 3,180 | 4,277 |

TABLE V : GVCC - ILLUSTRATIVE SOURCE AND APPLICATION OF FUNDS STATEMENT

| 1990 US$ ('000's) | Year 0 | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| s OF FUNDS | | | | | | | | | | | |
| se in Share Capital | 0 | 2,000 | 0 | 2,000 | 0 | 4,000 | 0 | 0 | 0 | 0 | 0 |
| se in Share Premiums | 0 | 0 | 0 | 1,000 | 0 | 6,000 | 0 | 0 | 0 | 0 | 0 |
| se in Term Loans | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| se in Overdraft | 0 | 0 | 184 | 0 | 460 | 0 | 0 | 0 | 0 | 0 | 0 |
| ion in Working Capital | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| iation | 0 | 29 | 29 | 29 | 29 | 29 | 4 | 4 | 4 | 4 | 4 |
| . (Loss) Before Tax | 0 | 100 | 78 | 181 | (591) | 782 | 3,881 | 4,042 | 6,038 | 6,360 | 8,553 |
| ations Before Capital Gains | 0 | 0 | 0 | 0 | 0 | 420 | 945 | 1,143 | 1,425 | 1,610 | 2,089 |
| l Losses | 0 | 0 | 0 | 105 | 105 | 75 | 75 | 98 | 126 | 223 | 236 |
| | 0 | 2,129 | 291 | 3,314 | 3 | 11,305 | 4,905 | 5,287 | 7,594 | 8,199 | 10,882 |
| ATION OF FUNDS | | | | | | | | | | | |
| and Intangible Assets | 0 | 164 | 0 | 0 | 0 | 0 | 46 | 0 | 0 | 0 | 0 |
| e Capital Investments | 0 | 1,050 | 1,050 | 1,500 | 1,500 | 1,950 | 2,524 | 4,470 | 4,718 | 6,017 | 5,886 |
| Term Investments | 0 | 760 | (760) | 700 | (700) | 6,360 | (2,160) | (2,175) | (975) | (1,050) | 0 |
| se in Working Capital | 0 | 132 | 24 | 108 | 24 | 867 | 3,139 | 177 | 1,932 | 281 | 1,979 |
| se in Term Loans | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| se in Overdraft | 0 | 0 | 0 | 184 | 0 | 460 | 0 | 0 | 0 | 0 | 0 |
| n (Previous Year) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| ds (Previous Year) | 0 | 0 | 0 | 0 | [illegible] | 0 | 0 | 1,940 | 2,021 | 3,019 | 3,18C |
| | 0 | 2,106 | 314 | 2,492 | 824 | 9,637 | 3,548 | 4,413 | 7,696 | 8,267 | 11,045 |
| RPLUS (DEFICIT) | | | | | | | | | | | |
| Cash | 0 | 0 | 23 | 0 | 822 | 0 | 1,668 | 3,025 | 3,900 | 3,798 | 3,729 |
| Surplus (Deficit) | 0 | 23 | (23) | 822 | (822) | 1,668 | 1,357 | 875 | (102) | (68) | (163) |
| Cash | 0 | 23 | 0 | 822 | 0 | 1,668 | 3,025 | 3,900 | 3,798 | 3,729 | 3,566 |

TABLE VI : GWCC - ILLUSTRATIVE BALANCE SHEET

| 90 US$ ('000's) | Year 0 | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| SSETS | | | | | | | | | | | |
| sets at Cost | 0 | 164 | 164 | 164 | 164 | 164 | 210 | 210 | 210 | 210 | 210 |
| umulated Depreciation | 0 | 29 | 57 | 86 | 114 | 143 | 147 | 151 | 156 | 160 | 164 |
| d Assets | 0 | 136 | 107 | 79 | 50 | 22 | 63 | 59 | 55 | 50 | 46 |
| NTS | | | | | | | | | | | |
| Capital Investments at Cost | 0 | 1,050 | 2,100 | 3,495 | 4,890 | 6345 | 7849 | 11,078 | 14,244 | 18,428 | 21,989 |
| rm Investments at Cost | 0 | 760 | 0 | 700 | 0 | 6,360 | 4,200 | 2,025 | 1,050 | 0 | 0 |
| vestments | 0 | 1,810 | 2,100 | 4,195 | 4,890 | 12,705 | 12,049 | 13,103 | 15,294 | 18,428 | 21,989 |
| ASSETS | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 9 | 9 | 15 | 15 | 15 | 15 | 15 | 15 | 15 | 15 |
| Progress | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 51 | 34 | 112 | 136 | 1,003 | 4,193 | 4,370 | 6,303 | 6,583 | 8,562 |
| Hand and at Bank | 0 | 100 | 119 | 968 | 146 | 1,814 | 3,120 | 3,995 | 3,893 | 3,824 | 3,661 |
| rrent Assets | 0 | 161 | 163 | 1,094 | 297 | 2,832 | 7,328 | 8,380 | 10,210 | 10,422 | 12,238 |
| SETS | 0 | 2,106 | 2,370 | 5,368 | 5,237 | 15,559 | 19,440 | 21,542 | 25,559 | 28,900 | 34,273 |
| IABILITIES | | | | | | | | | | | |
| draft | 0 | 0 | 184 | 0 | 460 | 0 | 0 | 0 | 0 | 0 | 0 |
| for Taxation | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| for Dividends | 0 | 0 | 0 | 0 | 0 | 0 | 1,940 | 2,021 | 3,019 | 3,180 | 4,277 |
| (Less than 1 Year) | 0 | 6 | 7 | 9 | 9 | 9 | 9 | 9 | 9 | 9 | 9 |
| rent Liabilities | 0 | 6 | 191 | 9 | 469 | 9 | 1,950 | 2,030 | 3,028 | 3,189 | 4,286 |
| NT ASSETS | 0 | 2,100 | 2,178 | 5,359 | 4,768 | 15,550 | 17,490 | 19,511 | 22,531 | 25,711 | 29,988 |
| LIABILITIES | | | | | | | | | | | |
| Loans | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| (More than 1 Year) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| g Term Liabilities | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| S | 0 | 2,100 | 2,178 | 5,359 | 4,768 | 15,550 | 17,490 | 19,511 | 22,531 | 25,711 | 29,988 |
| ITAL AND RESERVES | | | | | | | | | | | |
| ital | 0 | 2,000 | 2,000 | 4,000 | 4,000 | 8,000 | 8,000 | 8,000 | 8,000 | 8,000 | 8,000 |
| remium | 0 | 0 | 0 | 1,000 | 1,000 | 7,000 | 7,000 | 7,000 | 7,000 | 7,000 | 7,000 |
| Loss Account | 0 | 100 | 178 | 359 | (232) | 550 | 2,490 | 4,511 | 7,531 | 10,711 | 14,988 |
| CAPITAL AND RESERVES | 0 | 2,100 | 2,178 | 5,359 | 4,768 | 15,550 | 17,490 | 19,511 | 22,531 | 25,711 | 29,988 |

TABLE VII: GVCC - RETURNS TO INVESTORS

| Constant 1990 US$ (000's) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| 0 | | | | | | | | | | |
| 0 | | | | | | | | | | |
| 1 | | | | | | | | | | |
| Dividend Flow | | | | | | 1940 | 2021 | 3019 | 3180 | 4277 |
| Residual Value | | | | | | | | | | 29988 |
| Total Resource Flow | 0 | 0 | 0 | 0 | 0 | 1940 | 2021 | 3019 | 3180 | 34265 |

Resource Flows for each class of shareholder US$(000's)

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| Shareholders A | -2000 | | | | | 485 | 505 | 755 | 795 | 8566 |
| ($2M share capital) IRR= | 23% | | | | | | | | | |
| Shareholders B | | | -3000 | | | 485 | 505 | 755 | 795 | 8566 |
| ($2M share capital) IRR= | 23% | | | | | | | | | |
| Shareholders C | | | | | -10000 | 970 | 1011 | 1510 | 1590 | 17133 |
| ($4M share capital) IRR= | 20% | | | | | | | | | |

ANNEX B

## TERMS OF REFERENCE - STATEMENT OF WORK

The consultant, John Leech, will work with AVCP Project Director Richard Loth to identify a venture capital vehicle in Ghana, as the first step in the creation of a three-party co-operative effort to set up a venture capital operation in Ghana. The consultant will assist in developing the analysis and design features for this venture capital fund under consideration.

The scope of work under this effort will include, but not be limited to the following:

A. Preparatory work (2 days)

B. Meetings in Zurich with EDESA (1 day)

C. Work in Ghana (5 days)

1. Identify potential local venture capital vehicles;

2. Do background research on and analysis of these vehicles with a view to the structuring and design of a Venture Capital Fund in Ghana;

3. Assess the potential for developing competent management for a venture capital fund;

4. Research capital investment opportunities and possibilities to determine the potential for success of a venture capital fund in Ghana;

5. Assess the potential for raising capital;

6. Identify potential investee companies and/or projects and comment on their likely viability;

7. Identify potential local private and institutional investors; and

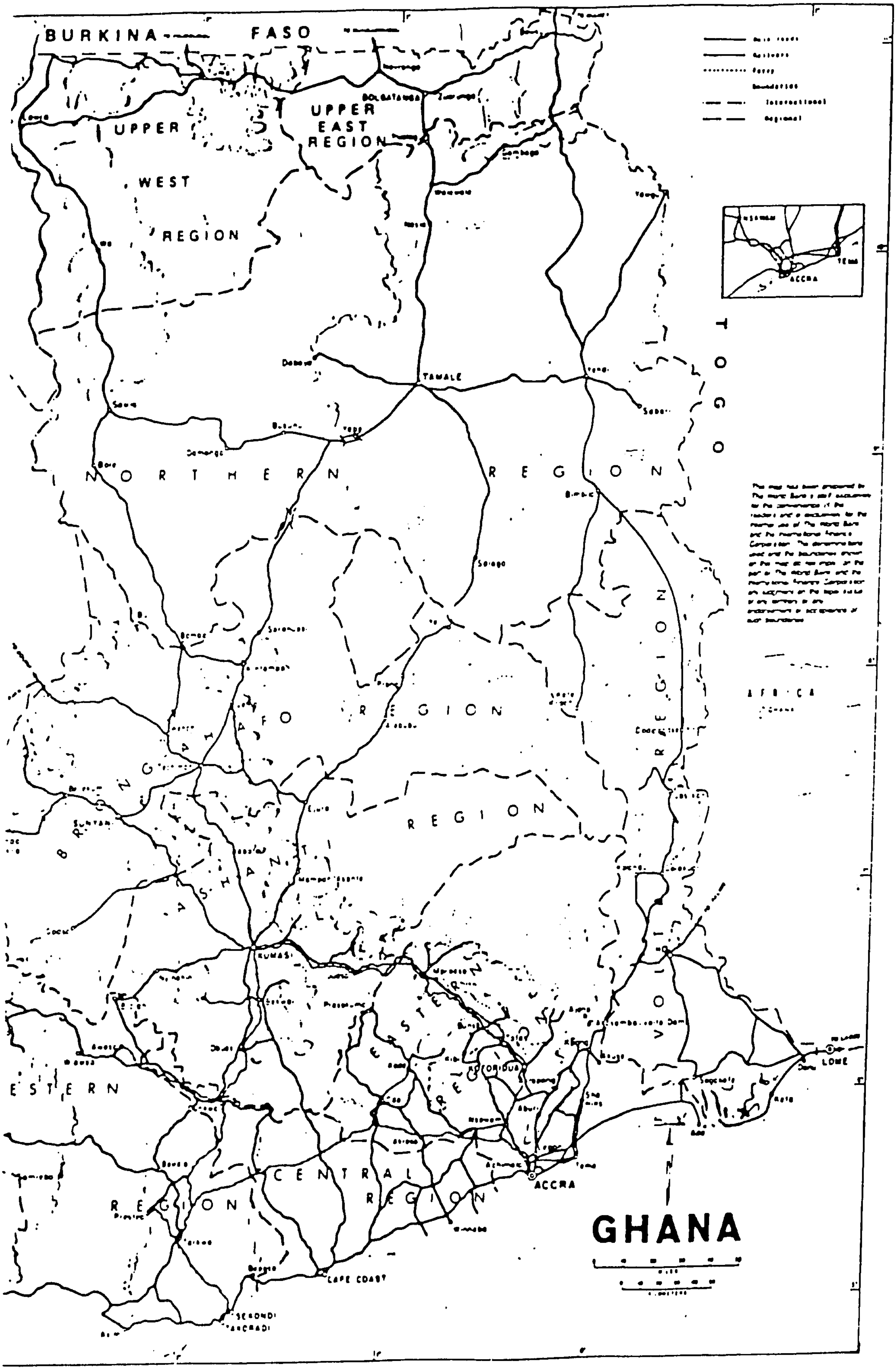
8. Research the overall investment and regulatory environment affecting business investment in Ghana.

9. Prepare estimated financial projections indicating the period needed for a Ghanaian venture capital fund to reach profitability, and the inputs which may be required under the AVCP to assist it in reaching the break-even point.

D. Work in Togo (2 days)

1. Assist AVCP Project Director in doing a preliminary analysis of the potential for a bank-related venture capital initiative with Ecobank, Lome, Togo.

The contractor will prepare a draft and final report on the results of his findings, and make recommendations detailing the structure and design features of this venture capital fund in Ghana. The report must be acceptable to HC and AFR/MDI. The consultant will provide a copy of this report to HC in both digital and hard form. He will also debrief AVCP Project Director on his findings and views on Ecobank in Togo (12 days).


BURKINA FASO
UPPER WEST REGION
UPPER EAST REGION
TOGO
TAMALE
NORTHERN REGION
VOLTA REGION
AFRICA
KUMASI
KOFORIDUA
ACCRA
LOME
CENTRAL REGION
CAPE COAST
SEKONDI
TAKORADI
GHANA

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ANNEX D

# KEY ECONOMIC INDICATORS

| | 1980 | 1987 | 1988 | 1989 |
|---|---|---|---|---|
| Population | | | 14 m | |
| Population growth rate 1980-88 | | | 3.5% | |
| Per capita GNP US$ | | | 400 | |
| Gross Domestic Product (constant 1987 prices, C bn) | 700 | 746 | 792 | 840 |
| (current US$ m) | 4445 | 5075 | 5228 | 5258 |
| GNP growth rate | | | 6.1% | 6.1% |
| Gross Domestic Saving | 4.9 | 7.9 | 6.4 | |
| Gross National Saving | 4.5 | 9.3 | 7.1 | |
| Consumer Price Index | 6.3 | 100.0 | 131.4 | |
| Balance of payments data US$ m, current prices - | | | | |
| Exports - Goods & Serv | 1210 | 899 | 957 | 912 |
| Imports - ditto | 1175 | 1189 | 1265 | 1348 |
| Resource Balance | 35 | -290 | -308 | -436 |
| Long-term capital inflow - | | | | |
| Direct investment | 16 | 5 | 5 | 8 |
| Net loans | 98 | 221 | 212 | |
| Changes in net Reserves | 96 | -66 | -148 | |
| Total debt incl.IMF/GDP | 29.57 | 61.73 | 59.27 | 64.49 |
| Official exchange rate (C to US$) | 2.75 | 153.73 | 202.35 | 270.0 |

ANNEX E

## LIST OF INTERVIEWS

| | |
|---|---|
| US EMBASSY | Hon Raymond Ewing, Ambassador |
| US AID MISSION | Joseph B. Goodwin, AID Representative<br>Edward Birgells<br>Robert Wuertz<br>Daniel Gyimah, Private Sector Adviser |
| **FINANCIAL INSTITUTIONS** | |
| Bank of Ghana | Governor Agama<br>First Dy Governor Mrs Theresa Owusu<br>Alex Ashiabor (seconded to UNCTAD)<br>Dr Eli Saleeby, World Bank Adviser |
| Ghana Investment Centre | Dr Kobena Gyapea Erbynn, Ch Executive |
| Ghana Stock Exchange | Yeboa Amoa, MD |
| Social Security & National Security Trust | Eric N.A. Adjei, GM Admin<br>Kodwo Ahlijah |
| National Investment Bank | Yaw Osafo-Maafo, MD |
| Barclays Bank Ghana Ltd | Geoff Lock, Controller Risk Management |
| Standard Chartered Bank Ghana | S.A. Fleming, MD |
| Ecobank Ghana Ltd | David C. Johnson, MD<br>Lauretta Lamptey, Capital Markets Group |
| Merchant Bank (Ghana) Ltd | Mrs Stephanie Baëta Ansah, Dy MD<br>Edusei Derkyi<br>Jude Arthur, Mgr Corporate Finance |
| Continental Acceptances Ltd | Derek Peacock, GM |
| Commonwealth Developmt Corpn | Jim Romanos, Rep West Africa<br>Mark Edwards |
| EDESA SA (Zurich) | Claude Bachmann<br>Heinz Reeb |
| **INDUSTRY AND COMMERCE** | |
| National Board for Small-Scale Industries | Dr E.K. Abaka, Ex Director |

| | |
|---|---|
| Ghana National Chamber of Commerce | Ms Grace Otoo Kwadey |
| Association of Ghana Industries | Eddie Imbeah-Amoakuh, Ex Secy |
| | A.B. Dadzie, Ghana Mats & Carpets<br>E.R. Hayford<br>William Inkumsah<br>J. Kobina Richardson<br>F.W. Tuyee |
| Others | Silvain Amegashi<br>Pat Mensah, Inter-Afrique Group |
| LEGAL ADVISER | E.P.L. Gyampoh |
| EUROPEAN COMMISSION | Friedrich Nagel, Acting Delegate |

LOME, TOGO

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| US AID Mission | Mark Wentling, AID Representative<br>Dennis E. Panther |
| Ecobank Transnational Inc | Ian Grundberg, Group Credit & Marktg<br>Fogan Sossah, Investmt & Developmt |
| Société Togolaise de Sidérurgie | Stanley G. Ansett, GM |
| Industrialization Fund for Developing Countries, Denmark (IFU) | Mogens Hasdorf, Rep West Africa |