

**Review Of Progress Toward Milestones Accomplishment  
and Achievement of TIRP Results**

**Year Three (July 2000 - June 2001)**

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**1.15 Evaluate progress toward milestones and results (Year 3)**

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## List of Acronyms

BOG	Bank of Ghana
CEPS	Customs, Excise, and Preventive Services
FAGE	Federation of Associations of Ghanaian Exporters
GEPC	Ghana Export Promotion Council
GIPC	Ghana Investment Promotion Centre
GLSS	Ghana Living Standards Survey
GSE	Ghana Stock Exchange
GOG	Government of Ghana
HIPC	Highly Indebted Poor Countries
HFC	Home Finance Corporation
ISSER	Institute of Statistical, Social and Economic Research
IMCC	Interministerial Competition Committee
IMF	International Monetary Fund
MOA	Ministry of Agriculture
MEPRC	Ministry of Economic Planning and Regional Cooperation
MOF	Ministry of Finance
MOTI	Ministry of Trade and Industry
NED	National Economic Dialogues
NEF	National Economic Forum
NPP	New Patriotic Party
NC	North Carolina
PEF	Private Enterprise Foundation
RTP	Research Triangle Park
SPEG	Seafreight Pineapple Exporters Group
SSNIT	Social Security and National Insurance Trust
TIRP	Trade and Investment Reform Program
TUC	Trades Union Congress
T-bills	Treasury Bills
VAT	Value Added Tax
WB	World Bank

## Executive Summary

This report is a comprehensive internal review of Sigma One Corporation's activities under the Trade and Investment Reform Program (TIRP) funded by the United States Agency for International Development Mission to Ghana (USAID/Ghana). It addresses the question, "Has Ghana moved closer to satisfying the USAID Intermediate Results Packages One?" through discussions with stakeholders and program managers and a review of published data. It demonstrates the linkages among the Request for Proposal for the Improved Policy Reform and Financial Intermediation component of TIRP, Sigma One's proposal (including Best and Final), the resulting contract's Section C (Statement of Work), the Milestones and Strategic Objective Number One.

Sigma One Corporation is on target toward satisfying the TIRP USAID Intermediate Results for Task One, except for the "Streamlined importation procedures" result. Partial improvements have occurred. Key challenges include getting the government to repay the Value Added Tax (VAT) and duty drawbacks in a timely manner, and continued problems with Customs and Excise Protection (CEPS) policy implementation.

None of the results have been fully satisfied in Task Two. The majority of the economic problems identified by Sigma One in 1998 still exist today. However, Sigma One has successfully completed the majority of its TIRP commitments, the corresponding policy reforms have officially been made, and results have been seen, though to a lesser degree than had been initially hoped for. This is mainly attributed to the recent change of government, and the necessary time lag needed for the new government's policies to take effect. This has impeded the introduction of new financial instruments, an aggressive and competitive financial sector, increased availability of net domestic credit, externally financed expansions, and linkages between the Ghanaian and global financial systems

Sigma One Corporation's areas of success in the Trade and Investment Reform Program include:

- Labor code draft process
- Implementation of a participatory policymaking process
- Broad budget presentation
- Reduction of exemptions and liberalization of tariffs
- Reducing intervention in the foreign exchange market
- Bonded warehousing
- Transparency of interest rate setting
- Domestic debt reduction
- Government spending reduction
- Cash budgeting
- Adherence to monetary targets

The following areas have been suggested for improvement:

- Follow through with a narrower project focus
- Increased attention for policy implementers
- Increased use of local talent
- Increased publicity for SOC activities and its research

## 1.0 Introduction

This report is a comprehensive internal review of Sigma One Corporation's activities under the Trade and Investment Reform Program (TIRP) funded by the United States Agency for International Development Mission to Ghana (USAID/Ghana). The company's activities in this program fall under the rubric of Improved Policy Reform and Financial Intermediation. This review was undertaken during the period of May 29 to August 10, 2001 at Sigma One Corporation headquarters in Research Triangle Park (RTP), North Carolina (NC) and in Accra, Ghana.

In 1992, Dr. David Franklin, President of Sigma One Corporation, described what Ghana would look like as a competitive state. He highlighted various economic problems that were impeding international competitiveness. Some of these problems were the outcomes of bad policies while other problems could be resolved by appropriate changes in policies. These are summarized in the chart titled "Improved Policy Reform and Financial Intermediation: Expected Improvements and Resulting Effects" (see **Table 1**). We use this chart as a framework to answer an important question: Has Ghana achieved the results set forth in USAID's Intermediate Results Packages One?<sup>1</sup>

Our overall strategy for answering this question is to demonstrate how the various stages involved in contracting and implementing the project are linked, beginning with the Request for Proposal (RFP) for the Improved Policy Reform and Financial Intermediation component of TIRP, followed by Sigma One's proposal, and culminating in the contract's Statement of Work (Section C). Integral to this Statement of Work are the Milestones to the USAID TIRP Intermediate Results Package Number One, which, if accomplished, should lead to increased private sector growth (USAID/Ghana's Strategic Objective Number One).

This report reviews the corporation's key TIRP activities over the life of the program by means of discussions with stakeholders and program managers, as well as a collection of published data. Discussions were held with Sigma One Corporation personnel in RTP and Ghana, USAID officials in Ghana, and both Ghanaian public and private sector representatives who have either participated in the implementation of the program or have witnessed its effects. Information was also obtained from reviews of Sigma One Corporation's program files in RTP and Ghana, as well as Ghanaian media reports, publications by third-party authorities, and selected government documents. They comprise the data used to assess the impacts of the program on Ghanaian economic policies and programs, as well as on the economy of the country at the macroeconomic and microeconomic levels.

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<sup>1</sup> This report also fulfills the Year Three Milestone 1.15, Evaluate Progress toward Milestones and Results.

**Table 1. Improved Policy Reform and Financial Intermediation: Expected Improvements and Resulting Effects**

Economic Problem	Policy Reform Measure To be Implemented	TIRP Action to Cause Improvement	Effects of Policy Improvements On:		
			<i>Farmers and Producers</i>	<i>Small and Micro-enterprises</i>	<i>Exporting Firms</i>
Dollar indexation of economy hurt exporting firms	Money supply targets are published and adhered to: "a monetary anchor"	BOG will implement effective secondary market for GOG debt	Farmgate prices will reflect world markets	Returns to market intermediation services for domestic goods will improve	Real exchange rate will be competitive
Government debt crowds out private sector borrowing	"Broad Budget" will be presented to Parliament with public borrowing limits	Assistance to GOG in budgeting and cash flow planning	Improved access to production credit	Improved access to longer term credit for investments in equipment and inventories	Ability to meet international commitments
High nominal interest rates de-capitalize firms	Introduce an inflation indexed bond in financial market	Assist with design of financial instruments	Enables longer investment cycle	Promotes formality and capitalization of firms	Modernization and expansion
Low quality of credit demand (high default risk)	Improved bank supervision and credit standards	Assist with design of credit reports services	Forward contracting	Reduces favoritism and cronyism in credit decisions	Expanded trade credits
Low domestic savings rate	Credible monetary targets and fiscal adherence to broad budget will create confidence in Ghana's financial system	Assistance to BOG on monetary targets and to Ministry of Finance on budget & expenditure control	Reverses outflow of savings from rural areas	Expands credit and improves available financial instruments for expansion into new products and services	Improved creditability in world markets For Ghanaian export firms
Excessive reliance on international donors for international investment	Broad Budget incorporates fiscal cost of donor projects-- reduced crowding-out	Help attract international private capital for infrastructure	Improved farm-to-market links	Resource allocation driven by market forces	Attract international investors

Economic Problem	Policy Reform Measure To be Implemented	TIRP Action to Cause Improvement	Effects of Policy Improvements On:		
			<i>Farmers and Producers</i>	<i>Small and Micro-enterprises</i>	<i>Exporting Firms</i>
Stock market dominated by large government presence	Accelerate divestiture and reduce SSNIT purchases of stocks in SOE's	Assistance to GSE to increase number of private stock issues	Increased numbers of potential buyers	Firms use financial market for expansion of scale rather than only own cashflow	Access to equity capital for modernization
Job creation in the formal sector burdened by emoluments and fringe benefits	Incorporate emoluments into wages directly and reduce hidden burden of fringe benefits	Ghanaian consultants calculate wage equivalence of benefits as costs	Slows rural exodus and improves off-farm incomes	Firms can expand and contract as needed in response to market forces stimulates formality	Able to adjust to seasonal needs for workers
Tenure rules and end-of-service benefits cause labor to be a fixed factor	Reform labor code to allow part-time and intermittent jobs in formal sector and incorporate EOS into pension system	Support tri-partite policy review of labor codes and practices (GOG, TUC, employers)	Expanded use of non-family workers and improved off-farm incomes	No arbitrary limits on firm size, better able to provide linkages of producers to world markets, pay-offs to on-the-job training	Increased vertical intergration
Labor market practices cause skill and job mismatching	Private sector wages scales tied to skills not tenure	Tri-partite consensus on productivity	Access to skills	Better able to invest in workers (OJT)	Improved product quality
Government is the wage setter and wage bill is large	Abolish link of public wages to expected inflation	Tri-partite dialogue on de-indexing	Rural activities more attractive	Workers paid in relation to productivity	Higher margins
Labor market is impediment to increased international competitiveness	1) Incorporate most benefits into wage, 2) de-link wages from inflation and dollar, 3) flexible firing and hiring	Analysis and dialogue on real wages, labor market and competitiveness	Higher and stable real prices for agricultural products	Increased job creation with incentives to develop skilled work force	Increased international competitiveness
Dispersion in tariff structure distorts incentives for exports and reduces revenues	Uniform and lower tariffs for neutral trade incentives and reduced "smuggling"	Comparative analysis from other countries showing gains	Improved net farm incomes	Value-added activities more attractive than mere intermediation	Expand export volumes



Economic Problem	Policy Reform Measure To be Implemented	TIRP Action to Cause Improvement	Effects of Policy Improvements On:		
			<i>Farmers and Producers</i>	<i>Small and Micro-enterprises</i>	<i>Exporting Firms</i>
Administration of trade regime induces rent seeking	Eliminate tariff exonerations and export bans and quotas	"Gurus" urge GOG ro not pick winners	Market access improves	Reduced "smuggling" and "hawking"	Profit seeking
Explicit interventions such as bans and quotas on exports have perverse effects	Eliminate all trade bans and quotas not based on safety or environmental regulations	Case studies show bad affects on firms, jobs and nature	Improved environmental husbandry	Legitimate value-added activities not circumvention of restrictions	Increased exports
Government entities attempt to pick winners and distort economic incentives	High-level pronouncement that GOG role is to create stable environment for all	Studies to show picking winners also means picking losers	More potential buyers and reduced losses	Better chance to succeed when not competing with favored firms	Improved market responsiveness
Agriculture punished by the trade regime	Uniform and lower tariffs on imports, eliminate quotas and bans, liberalize imports of agricultural inputs	Dialogue on negative indirect effects of import barriers and direct effect of bans	Better prices and higher incomes	Increased opportunities to expand in farm to market value-added chain	Increased capability for "push-pull"
Customs and inspections procedures are cumbersome	Continue SGS and Inchape services--use random checking rather than 100%	Technical assistance to CEPS to use modern procedures	Lower cost of inputs	Improved access to technology and modern Inputs	Higher profits
Government has granted large wage increases and aggravated public sector balance problems	GOG wage setting de-linked from expected inflation, GOG role reduced	Studies to show wage indexing erodes real wages rapidly via debt and inflation	Planning is less risky	Fewer incentives for speculative activities and more for production	Stable exchange rates and improved profits
Domestic debt service one-third of recurrent budget	Coherent fiscal and monetary program will reduce interest rate burden	High-level policy consensus to agree on "national interest"	Better access to credit	Less reliance on internal cash flows and greater reliance on financial markets	Attractive to international investors

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Divestiture receipts used to fund current expenditures	Use divestiture proceeds to reduce public debt	Policy dialogue to promote transparency in public finances	Better infrastructure	Opportunities to provide services on competitive basis	Lower costs
Banking system is "forced" to lend to public sector by requiring excessive reserves	Eliminate use of required reserves as monetary policy instrument	Assist BOG in review of monetary policy instruments	Increased use of the financial sector	Increased use of formal financial services	Access to trade credit
Inflation taxes micro-enterprises severely	Credible budgets and money targets reduce inflation	Studies show social costs of inflation	Removes uncertainties	Reduce higher burden of inflation on SME's	Better "push-pull"
Inflation dollarizes the economy and hampers the effectiveness of policies	Reduced inflation without using nominal rate as anchor: policy focus on competitiveness	Analyses show indexing aggravates volatility of real prices and wages	Better prices for products	Reduces speculative activities and stimulates value-added production	Cost containment
Nominal exchange rate used as a nominal anchor results in high variable real returns to production	Eliminate BOG intervention in forex market as a tool to repress inflation and sterilize capital inflows externally	Seminars on real exchange rate, rational expectations and fundamentals	Higher and more stable prices for products (real exchange rate)	Opportunities to specialize and become more formal; incentives for "value-adding, activities"	Predictable export returns and reduced risks
Public Sector deficits expenditures cause loss of competitiveness by their effect on non-tradables	GOG and BOG work to avoid use of extraordinary means of financing GOG expenditures outside budget	Policy dialogue:GOG expenditures on non-tradables causes real appreciation of exrate	Reduces indirect taxation	Greater opportunity for expansion	More competitive
Reserves are misused to depress Cedi price of foreign exchange	BOG announces a foreign reserves policy consistent with competitiveness	Policy dialogue: a strong Cedi is bad for agriculture & industry	Better prices for products	Avoids incentives for speculation on currency	Reliable profits

<b>Economic Problem</b>	<b>Policy Reform Measure To be Implemented</b>	<b>TIRP Action to Cause Improvement</b>	<b>Effects of Policy Improvements On:</b>		
			<i>Farmers and Producers</i>	<i>Small and Micro-enterprises</i>	<i>Exporting Firms</i>
Economy is susceptible to speculative assaults on currency	BOG announces that it will not use reserves to support Cedi	Studies show that support of Cedi rewards speculators	Stable prices	Resources allocate to value-added activities	Predictable margins
Excessive reliance on trade taxes depresses outward oriented activities	VAT is successfully re-introduced and integrated with other taxes	Training on VAT administration and collection	Indirect benefits	Improves incentives for formality	Improved duty and tax relief for exports
Excessive role of government in enterprise level resource allocation	Eliminate implicit subsidies to energy and utilities and other public services	High-level policy dialogue on effective role of GOG	Technology and inputs driven by expected returns	Formality is encouraged and firms pay taxes and observe rules in hassle free ambiance	Firms invest in new products and markets
Inadequate fora for economy-wide and sectoral policy dialogue	High-level continued commitment to national consultations process	Assistance to think-tanks and advocacy associations/groups	Interests fully represented in policy dialogue	Informality addressed at real causes: economic disarray and high costs of formality	Firms become good corporate citizens
Lack government command and control system to convert policy pronouncements into administrative practice	High-level performance review of GOG practices to encourage public servants to serve private sector as clients (promote accountability)	Technical assistance to IMCC and for high-level policy fora to commit GOG to new style of business	Better services from GOG, e.g. extension, research, weather forecast	GEPC, GIPC, etc. provide valuable services which individual firms cannot obtain individually	Streamlined exporting procedures
Too many permits and licenses required for routine business activities	Top-down review of regulatory process to reduce number of permits/licenses	National Economic Forum theme for Year Two of TIRP	Improved access to technology and markets	Reduced costs of doing business which impinge harder on micro and small	More dynamic search for new markets
Government Business Assistance Fund is used to "bail-out" inefficient firms	"BAF" eliminated to signal to firms that it is no longer business as usual	Private sector associations promote new business ethics	More equitable incentive environment	Placed on better footing and eliminates cronyism	More entrepreneurial

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			<i>Farmers and Producers</i>	<i>Small and Micro-enterprises</i>	<i>Exporting Firms</i>
Government officials treat businesses as adversaries	Commitment to hassle-free business climate	High-level forum on "hassle factor"	Improved public services	Able to expand and have access to market information	Streamlined processes
Business organizations lack policy advocacy capacity	Members increase participation and support	Technical assistance: informed advocacy	Voices heard via associations	Previously disenfranchised groups obtain place at table	Responsible advocacy
Incentives encourage in formalization and prevent optimal firm size	Policies for labor market flexibility and reduced paper-work burdens on firms	Analysis/dialogue that informality is result of bad policy	Improved environment for investments	Horizontal and vertical expansion stimulated by removal of hassles and costs	Access to international investment
Land tenure rules prevent long-term investments	Promulgate land usufruct rules to encourage investment while respecting traditional practices	Include paramount chiefs in dialogue to make land usufruct rights reliable	Better husbandry and technology for trees and perennial crops	SME's encouraged to provide services to agricultural enterprises, e.g. forward contracting on crop marketing	International joint ventures encouraged by assured output

## **2.0 Findings**

The problems preventing Ghana from being internationally competitive are still present. However, progress has been made toward their alleviation. For each policy reform measure recommended by Sigma One Corporation (and listed in Table 1), this section will note whether the recommendation was implemented, and, if implemented, will highlight the key TIRP activities that made the change a success. If the recommendation was not implemented, it will discuss why the TIRP action did not have the anticipated effect. We grouped the problems into four main areas: domestic debt management, inflation, labor, and an improved business climate.

### **2.1 Domestic Debt Management**

Because of the gravity of Ghana's debt situation, the World Bank (WB) has agreed to let Ghana apply some of its Highly Indebted Poor Country (HIPC) relief funds toward reducing its domestic debt, rather than applying the funds directly poverty reduction as is generally the case. In addition, due to Ghana's huge debt repayment schedule, the Paris Club of international creditors decided to let Ghana forego its US, UK, and French debt servicing for this year as long as they put the savings toward reducing the domestic debt. These decisions have brought this issue to the forefront of economic discussions.

The reduction of Ghana's domestic and foreign debt has long been a key issue for Sigma One Corporation. At the North Carolina Conference on Ghanaian Policy-Dialogue in 1997, several of the key issues placed on the table by Sigma One dealt with various aspects of this issue, including the best use of government divestiture proceeds and the avoidance of budgetary shortfalls.

Sigma One Corporation recommended using any budgetary surplus, and particularly divestiture proceeds, to reduce the public debt (Sigma One Corporation, 1997 and 1998). One public sector official stated that Sigma One Corporation's work in this area, especially during the recent National Economic Dialogues (NED), has been a strong influence on policy makers. He stated that the use of divestiture money to pay down domestic debt is an old policy that has not been in force for some time. Now, however, the new government headed by the New Patriotic Party (NPP) has stated that all future divestiture revenue (estimated to be about \$50 million) will go to pay down domestic debt. The challenge, however, will be getting those who buy the companies to pay the money. The official estimates that while around 200 companies have been divested, very few buyers have actually paid the government the money they owe. To increase the amount of revenue available from divestitures, Sigma One also recommends the acceleration of divestitures by the Government of Ghana (GOG).

Sigma One Corporation further recommended avoiding future budgetary shortfalls in order to prevent the debt burden from increasing. In this regard, Sigma One addresses four key issues: (1) use of the broad budget in the budgeting process; (2) meeting money supply targets; (3) implementing a realistic budgeting process; and (4) improved revenue collection.

### 2.1.1 Use of the Broad Budget

A key Sigma One recommendation (1997a) that was adopted was to present the “broad” (versus “narrow”) budget to Parliament. One public sector official stated that this issue is one of Sigma One’s successes. Before the NC conference, the Ghanaian participants did not understand how high inflation fueled by money creation (to finance the broad public sector deficit) could prevail when the government was meeting its “narrow” budget deficit target each year. Consequently, there was a widespread sense that inflation was caused primarily by food shortages in the country, even though these have not been severe for many years (Goodwin, 2001). Drs. David Franklin and Curtis Youngblood presented a year-by-year analysis of the reasons for the deficit and high inflation, and each year it pointed to a lack of awareness by policymakers of the broad budget figures. As a result, since 1998, the broad budget has been presented to Parliament (Ministry of Finance, February 1998 and subsequent years).

### 2.1.2 Meeting Money Supply Targets

The second key issue is to meet the money supply targets published in each year’s budget. With the broad budget more accurately reflecting the amount of shortfall each year, Sigma One’s follow-up recommendation, as articulated in the 1997 National Economic Forum (NEF) is to adhere to the public sector borrowing limits listed in the broad budget. According to public and private sector representatives, through the NC Conference and related seminars, Sigma One was helpful in stimulating and informing this debate, and played an important role in facilitating the discussions. A public sector official noted that with the IMF also emphasizing the importance of meeting the monetary targets, a critical mass seems to have been reached that will tip the scales for the government to implement this policy in full force. Currently, the Bank of Ghana (BOG) has a program in place for money supply targeting and the government is restricted to 10% of last year’s revenues. However, the goal of the 2001 budget is to be on a cash basis only, with no domestic borrowing by the end of the year.

A supporting recommendation set forth by Sigma One Corporation (1997a and 1997b) is an independent Bank of Ghana whose bottom line is profit versus politics. Without more independence than it currently enjoys, BOG can set targets, but still be unable to refuse to finance a budget shortfall. In this case, the BOG would tend to miss its money supply targets, a concern voiced by one government official.

### 2.1.3 Realistic Budgeting

The third key issue is to implement a realistic budgeting process and to impose strict controls over spending, essentially by limiting spending to what is taken in. This philosophy is embodied in two recommendations laid out in the NC Conference and the 1997 NEF (Sigma One Corporation, 1997a and 1997b): (1) present credible budgets; and (2) avoid the use of extraordinary means to finance expenditures outside of this budget.

With respect to the first recommendation, one public sector official cited a historical analysis of government expenditures by Sigma One Corporation, as well as ongoing discussions with Sigma

One regarding revenue forecasting as activities whose findings had filtered into the work of the Ministry of Finance (MOF). Additionally, Sigma One has presented a budgeting model to GOG that projects revenues and expenditures based on past figures.

According to a public sector official, GOG is now using a rolling three-year broad-based budget and all involved parties (MOF and Chief Director) are signing off on the input and output figures and indicators of budget adherence. Officials noted the close communication between BOG, MOF, and the financial controller regarding what is coming in and what is going out, aided also by the help of the Economic Policy Coordination Committee. These officials say the first quarterly budget looks good and on target, although the time required to process receipts and payments must be shortened so “one hand can know what the other is doing”.

Once a credible budget is in place, the use of extraordinary means to finance expenditures outside of the budget must be avoided (the second recommendation). This involves putting measures in place to prevent overspending. A Sigma One analysis of the budgeting system for Road Construction presented in a Compendium of Deliverables (19??) highlighted the issues of consistent under-budgeting and overspending. For example, a road contractor often will perform work outside of the work specified in its contract with the government and then present a bill for this work. The Sigma One analysis recommended that the financial controllers take a hard line in these cases: refuse to pay the contractor for the work and take disciplinary action against the government official who authorized it.

To date, no significant measures to control spending have been implemented. Nevertheless, there currently are yearly public expenditure reviews where key areas are selected and analyzed. Policy hearings precede budget hearings and financial requests, and each Ministry/Department/Agency (MDA) is required to justify their requests. The recurrent budget, in the past separated from the capital expenditures budget, has been streamlined for easier viewing. However, adherence to the budget is only checked after the fiscal year has ended, and there is currently no measure in place to require officials to have additional money approved before it is spent. One reason offered for this is cultural—there is an aversion to embarrassing people, holding people accountable, and “taking food from people’s mouths”. Thus, no one is held accountable for sticking to a budget, and there are no consequences for missing an MDA’s budget targets.

#### 2.1.4 Improved Revenue Collection

Improved revenue collection is necessary to avoid incurring additional debt. Sigma One consultants have examined Ghana’s tax collection methods from assessment to seizure to identify areas for improvement. They have worked to set nominal tax collection targets to help the government better estimate future revenues. In the past, governmental departments were always able to meet their tax collection targets because each year’s increase was only 1.25% higher than the year before. The Sigma One analysis added realism to the targets by basing them on a regression model that used past revenues to estimate future ones. The consultants said that there have been improvements in this area, but the government still needs to increase corporate taxes, personal taxes, etc. in order to collect more money. As an additional success in this area, the

VAT was successfully re-introduced at the 10% level, and increased with little problem to 12.5%.

## **2.2 Inflation**

The reduction of inflation through the implementation of appropriate monetary and fiscal policies is another critical problem area. The recent economic stability has been credited in the Ghanaian media to an adherence to stricter fiscal and monetary policies. A public sector official noted that one of the reasons the broad budget was not met last year was because of increased government spending around the time of the elections. Aspects of monetary policy that Sigma One recommends that the Bank of Ghana address include money supply targets, exchange rate and interest rate setting, and bank supervision.

### **2.2.1 Money Supply Targets**

Money supply targets are built up from targets on high-powered money, one component of which is bank reserves. Banks are required to hold primary reserves (vault cash and deposits at the BOG) and secondary reserves (Treasury bills), both for monetary control purposes and to help insure the soundness of the banking system. Sigma One maintains that the secondary reserve requirement of 35% is "excessive", and in effect forces the banking system to lend to the government. Sigma One (1997a and 1997b) laid out its recommendation for BOG to eliminate the use of required reserves as a monetary policy instrument.

Sigma One has assisted the BOG in a review of monetary policy instruments (Gockel, 2000; Youngblood, 2000). One public sector official said that it is the Bank's aim to gradually eliminate secondary reserves requirements. This policy has not yet been implemented because there is concern that the banking system is not yet mature enough to be without such a "safety net". Moreover, secondary reserves are only required to be held in liquid assets such as cash, CD, bonds, T-bills, commercial papers, etc. While 35% is the requirement, the banks actually hold closer to 40% in secondary reserves, because T-bills have been their safest and most lucrative investment. Unfortunately, the T-bills have been most attractive for all the wrong reasons. Profiting from high inflation and high real interest rates that are a result of bad government policy fosters a very short-term view on the part of economic agents (including banks). Banks should diversify to grow, and profit from investments whose returns are high for the right reasons.

### **2.2.2 Exchange Rates and Interest Rates**

Another aspect of monetary policy concerns the setting of the exchange rate and the nominal interest rate. Sigma One (1997a) recommended that BOG cease using its foreign exchange reserves to support the cedi as one step in improving Ghana's international competitiveness. This recommendation was strongly re-emphasized in a 1998 paper in which the BOG was warned that continued pursuit of this policy of exchange rate intervention was setting the stage for a speculative attack on the currency. Subsequent to the speculative attack that took place in late 1999 and early 2000, one public sector official believes that this battle has been won with



BOG, albeit belatedly. Both public and private sector representatives flagged this as one of Sigma One's signature issues. Sigma One's success in this area is attributable in part to numerous discussions that Sigma One representatives had with the Ministry of Trade and Industry (MOTI). A private sector representative said that a convincing argument was demonstrating that exporters had been hurt by past exchange rate practices.

During the throes of the last elections, the previous government continued to squander foreign exchange reserves to support the cedi. The new government, however, has declared its intention to allow the exchange rate to float, although this has not been stated publicly. One outside observer gives Ghana credit for a tight monetary policy. A related policy change is that as a result of new program, BOG will now hold reserves equal to the value of at least six months of imports (up from three months), indicating a desire to build up foreign reserves. A public sector official cited the strong foreign exchange bureau market as evidence that exchange rate setting is more transparent. His benchmark is the percentage difference between the exchange rate in the bureaus and that set in the interbank market. Greater than a 10% difference indicates a potential problem, and the current difference is less than this.

Sigma One Corporation also recommended (1997a and 1997b) increased transparency in interest rate setting. According to a public sector official, Sigma One raised awareness on this issue, and he believes the battle has been won. Sigma One Corporation employees held monetary control workshops with BOG representatives regarding this issue, and Sigma One's recommendation was on the table at the recent NED (NED Action Plan, 2001).

A public sector official believes interest rate setting is now transparent. The current operative rate is the Treasury bill rate, which is determined in a weekly auction. However, one BOG official thinks this is not the best way to signal monetary policy since it really measures the strength of demand for government debt. Instead, he would like to return to using the interbank loan rate (the rate at which BOG lends to other banks) as the base rate. The challenge for the government is that they would have to give up the power to approve the increases of base rates, which is problematic for them. The official expects this sentiment to change, though, before the year is out.

Others do not agree that the BOG's policies for setting interest rates are transparent. Some think that the notes of interest-rate setting meetings should be made available to the public like in the United States. Furthermore, the BOG Governor should make a presentation to Parliament on a quarterly basis regarding the financial sector performance (NED Action Plan, 2001). In this view, the BOG's rationale for setting interest rates is not clear, is not talked about, and is not explained well to the public. One BOG official counters that this, in part, is due to BOG's desire to "have a clean house before inviting guests in", as well as the reluctance to single-out individuals and make them accountable for their actions. In Ghana, as in other post-Socialist countries, officials are still reluctant to make information available to the public.

### 2.2.3 Bank Supervision

One of the results of poor bank supervision is low quality of credit demand. A donor official noted that this low quality was caused by a high incidence of non-performing loans, a condition exacerbated by high interest rates. A vicious cycle then forms because the unprosecuted non-performing loans beget higher interest and depreciation rates. A public sector official commented that the formal financial system review done by Sigma One in 2000 flagged the issue of low quality of credit demand well. Sigma One's Best and Final TIRP proposal (1998b) recommends improved bank supervision, including auditing loans, holding banks accountable for bad loans, and the development of a credit reporting service.

Sigma One has had difficulty garnering interest and getting cooperation from the BOG on this issue. As a result, the majority of Sigma One's activities in this area have not been completed. A financial sector representative thinks that the initial approach of TIRP did not allow the key stakeholders to buy into the program as well as it could have. USAID consulted primarily with the MOF, which reached an agreement with USAID, but did not follow through with other governmental organizations that would be involved in or affected by the program. In addition, the appropriate effort was not made by USAID to get input from other key players (including BOG and other financial intermediaries, the Securities and Exchange Commission, National Insurance Commission, Ghana Stock Exchange [GSE], Association of Bankers, etc.) about what they really needed or wanted from TIRP. USAID counters that achieving cooperation is difficult for several reasons: the time lag between TIRP conceptualization and implementation; the sensitivity of some of the issues that make change difficult; and bad organizational communication about what was to happen in the program.

Notwithstanding the setbacks faced in this area, some progress has been made in Ghana. To better identify their non-performing loans, banks now provide more detail about the composition of their assets and liabilities. The BOG also closed two state banks that were unsound.

### 2.2.4 Reducing Subsidies

A tighter monetary policy needs to be supported by a more disciplined fiscal policy in order to ensure macroeconomic stability. Expenditure reductions signal a more disciplined fiscal policy. This issue was addressed above with respect to reducing the burden of the debt. Additional specific measures to reduce government spending were laid out at the NC Conference and included in Sigma One's TIRP proposal (1998a). These included the elimination of the Business Assistance Fund (BAF) and abolishing implicit subsidies to utilities and other public services.

The BAF was intended to be a revolving low-interest fund for "distressed but viable" companies negatively effected by the Structural Adjustment Program (SAP). There is little disagreement that the fund failed because the companies who received loans did not repay them. There is less agreement on the details of the failure. Sigma One's position is that the fund perpetuated private sector inefficiency, embodying the sentiment that "government money is everyone's money, and you can always get more". Proponents of the BAF would agree with Sigma One that many of the decisions about which companies were viable were not good. But they would say that the bigger

reasons that the BAF failed were one, that the funds provided insufficient, and two, that the decentralization of the program in its later years was fraught with cronyism that led to severe delinquencies. Unfortunately, the new government has resurrected the BAF under another name (the Ghana Investment Fund), with a different structure but with the same objective.

Abolishing implicit subsidies to energy, utilities and other public services has been a sensitive political issue. Leaders know it must be done, but few have the courage to do it. Sigma One emphasized the importance of such reforms during the recent NED. The new government has been forthright in taking steps toward these changes. There have been petrol increases of 64%. In addition, 100% increases (less than the 300% desired by GOG) have been made in the area of electricity pricing.

#### 2.2.5. Reform of the Tariff System

The second component of a more disciplined fiscal policy is an improved trade tax structure. Sigma One Corporation (1997a and 1997b) made four recommendations in this area. The first was to reduce the average level of tariffs, and reduce the disparity between the highest and lowest tariff rates. According to government officials, the change in tariff rates from 25% to 20% and the increase from 0% to 5% flowed directly from Sigma One recommendations. These officials cited numerous discussions with Sigma One Corporation staff as well as Sigma One's analyses as useful sources of information with which to advise policymakers. The rate changes have increased government revenue. Previously goods to which the 25% rate applied actually paid 7% due to smuggling, misrepresentations, and exemptions; with the reduction in rates, smuggling and other forms of evading the tariff have decreased, so that government is effectively getting more revenue.

The second recommendation was to reduce the number of tariff exemptions. Government officials credit Sigma One with the success in this area, particularly restricting the scope of exemptions granted to NGO's. The third recommendation was to streamline the bonded warehousing system. A government official notes that even before Sigma One's involvement, there was a problem with leakage of warehoused goods intended for export into the domestic market. He credits Sigma One for effectively articulating the issue, and providing a forum for discussion, which was a tremendous help in the streamlining process. He said specifically that the movement toward random checking at customs, as well as implementation of computerized tracking systems for inputs flowed directly from Sigma One recommendations

The fourth recommendation was to provide timely duty drawbacks and VAT refunds to exporters. This has been a very challenging area. While the refunds are in effect, exporters are not seeing the return of their money in a timely fashion. Instead of the three-month period proposed, many receive their refunds after two years with no interest accrued. The problem is that duty and VAT collections are completely spent, rather than setting aside a portion to reimburse exporters. One suggestion is that once the government determines a particular import to be for export only (packaging was mentioned often as an example) it should be exempt from duty or VAT charges. The government should then be responsible for monitoring the situation to

make sure the goods are really used for export. A request for technical assistance has already been made by Sigma One to have someone look into this problem.

#### 2.2.6. Effects at the Firm Level of Improved Financial and Trade Policies

The policy reforms discussed above were expected to have certain effects on firms (summarized in **Table 2**). The overarching firm-level effect that was desired was a stable and competitive macroeconomic situation. To date this has not been consistently seen. The results of the fiscal and monetary policies of the new government are beginning to show in a stable cedi, but not enough time has passed for the stricter policies to really take effect.

For this reason, the real exchange rate (RER) has not been maintained at a competitive level and access to long-term credit has not improved. Thus, very little increase in use of the formal financial sector has been seen. Dollar indexing is also still occurring. Labadi Beach Hotel quotes its rates in dollars, and a business person complains that it is hard to budget because input prices are quoted in dollars. Additionally, the data show little increase in value-added production activities. Numerous people are seen in the streets hawking. While most interviewees report that export procedures have been successfully streamlined, imports still need some work. Also, despite the perception of most interviewees, large increases of foreign investment projects have not been documented in the data.

Equally surprising for interviewees is the fact that evidence does point to higher prices and lower costs for agricultural products, and thus increased on-farm profitability. Farm-gate prices, however, do not seem to be converging with world prices, possibly due to the current macroeconomic instability.

Data were harder to obtain for some effects. Interviewees postulated that the lack of modernization and expansion projects could be blamed on macroeconomic instability, and specifically the lack of long-term credit. Also, the perception is that GOG's services have not improved. Producers cannot get the technical help they need and quality research is difficult to come by. On the other hand, improved linkages have definitely developed in and among exporters (most significantly pineapple producers), enabling some "push-pull" to occur.

### 2.3 Labor

A third critical issue affecting macroeconomic conditions in Ghana is labor. One official believes that without a strong labor law or mediating body, no other policy addressed in this report will be effective. The kick-off event for discussing these issues was in 1999 at the Hotel Cisneros Conference. Here, Sigma One laid out the extent of the labor-related recommendations.

All of the following recommendations are either addressed or allowed by the draft of the new labor code. The funding, guidance, and discussion facilitated by Sigma One, as well as the organization of a labor mission to Scandinavia, Japan and the US were all a "tremendous success" in moving the new labor code to law according to this official. The code is currently under the protocol of consideration by the new government, but is expected to be passed relatively soon.

**Table 2. Firm-level Effects of Financial Market and Trade Policy Reforms**

Issue	Measure (Data Source)	Data Results	Agrees With General Sense Of Interviewees?	Comments: Why Has Effect Not Been Seen?
Increased stability in the economy	Trends in inflation rate, exchange rate, and interest rates (2000 EIU Country Profile)	Unstable inflation and exchange rates continue with spreads as wide as approximately 63 and 35 percentage points, respectively from 1990-1999 while interest rates (of central bank, T-bills, and commercial bank deposits) have been dropping for all since 1997	Yes, despite recent NPP gains, there is still a widespread sense of instability and fear of further currency depreciation	Stricter policies of new government haven't had time to take effect.
Competitive RER	Trend direction of the RER (IMF's CY 2000 International Financial Statistics)	Decreased competitiveness indicated by an appreciating RER since 1995 (from 87 units of foreign currency per unit of domestic currency in 1995 to 126 in 1999)	Yes	Stricter policies of new government haven't had time to take effect
Improved access to credit	Credit allocation to the private sector (ISSER 2000)	Falling allocation percentage ever since it peaked in 1996 at 68.8%. CY 2000 showed 34.7%	Yes, in that the consensus was that access to long-term credit was at best unchanged. While Central Government credit has fallen, the excess has been picked up by small increases by the public enterprises.	Stricter policies of new government haven't had time to take effect.
Increased formality	M2/GNP and Currency/M1 (IFS and BOG Bulletins)	Formality level fluctuating indicated by financial depth percentages between 17 and 19% since 1992, and up again at 19% in 1997; Slight increase in formality levels as indicated by increased level of monetization from 52.3 to 55.7% from 1998-1999 (with fluctuation over the last 10 years).	Yes, as perception was that the macroeconomic environment has been so unfavorable, very few people are utilizing the formal financial sector	Stricter policies of new government haven't had time to take effect.

Issue	Measure (Data Source)	Data Results	Agrees With General Sense Of Interviewees?	Comments: Why Has Effect Not Been Seen?
Increase in value-added production activities	Sectoral GDP Growth: Agriculture and Industry proxy Production and Wholesale/Retail Trade for Intermediation (ISSER, 2000)	Slight decrease in "production" (from 42.9% in 1996 to 41.6% in 2000) and slight increase in "intermediation" (6.1% in 1995 to 6.8% in 2000)	Yes, as an increasing number of street vendors are appearing in the streets, as well as an increased number of vendor stands	Value-added is catching on, but production units are challenged with difficult upgrades and constraints. Trading is still easier.
Attraction of international investors and joint ventures	Numbers of foreign investment projects initiated in Ghana (GIPC Bulletin)	Declining investment project numbers from the peak in 1997 of 234 projects to 180 in 2000.	No, most interviewees felt that foreign project interest had been increasing despite yet unstable macro climate	Macro climate has not stabilized, nor has new government proven itself long enough yet for new investors
Higher prices and lower costs for agricultural products	Increase in profit margins reflected by a reduction in poverty of farmers (both export and non-export) (2000-2002 Interim Poverty Reduction Strategy)	Drop in percentage of impoverished self-employed agricultural exporters (from 67% in 1991-92 to 39% in 1998-99) and crop producers (67% to 61%)	No, instability of the economy has kept costs high and, thus, competitiveness low	Stricter policies of new government haven't had time to take effect.
Improved credibility of meeting international commitments	Increase in foreign buyers via the value of Ghanaian exports (ISSER, 2000)	Increasing values since 1996 (from \$1,700 million to \$1,940 million in 1999)	Yes, from the business associations' perspectives, but not so much from the producers'	
Increased exports	Increase in non-traditional exports (NTEs) in volumes and value. (GEPC Reports for 1997-2000)	Increase in the number of NTE products from 270 in 1997 to 272 in 2000; NT exporters has remained around 3,200; Value in US dollars was as high as 404.4 million in 1999, but dropped to 400.6 in 2000)	Somewhat, however business and product associations (GEPC, FAGE, VPEG, etc.) perceive a more dramatic increase in NTEs	Possibly, the perceived increase in NTEs just occurred during TIP, and is now being developed. An explanation for the drop in value could simply be the terms of trade shock.

The recommendations include, first, tying private sector wages to skills and not just tenure. The initial step of this recommendation has been taken in the PriceWaterhouseCooper salary structure evaluations. Implementation of the structure has been hindered by weaknesses in the Central Management Board, the body that is supposed to know salary administration. According to one official the Board needs to be recomposed with the technical abilities of credible human resource people to administer the program. Implementation of a universal salary structure in Ghana would also fulfill the second recommendation—incorporating emoluments directly into wages.

The third recommendation is to make the End-of-Service (EOS) benefits subject to negotiation instead of a mandatory benefit. While this is part of the labor code, public and private sector officials agree that this must include an improved Social Security system via the improvement of the Social Security and National Insurance Trust (SSNIT).

Sigma One recommended in the TIRP “Best and Final” proposal that SSNIT reduce purchases of stocks in state-owned enterprises (SOEs), as part of a strategy to diversify and improve the profitability of SSNIT’s investment portfolio. This recommendation has been echoed by representatives in the private sector. A donor official noted that SSNIT’s portfolio is only showing a 2.3% overall return on investment. However, there are concerns as to how this diversification can occur. One financial sector representative noted that other than SSNIT there are not many potential investors in the market (other than possibly some individuals, or some foreign investors, though many have pulled out due to currency risk). A donor official asks “if SSNIT doesn’t invest in the GSE, what will they invest in? Real Estate? This market could crash at anytime due to the fact that so many new buildings are currently standing empty. Treasury bills? But there aren’t that many available since government has vowed not to borrow domestically”. Nevertheless, he did assert that the government’s commitment to the private sector and divestitures will deepen stock market holdings. Increased investment in real estate will also meet another need that reduced EOS benefits will leave, namely affordable housing options.

A financial sector representative observed that the GSE is the wrong target organization to promote private stock issues since the GSE has no power to attract companies to join it, only to facilitate their trading once they join. The more appropriate focus would be on the companies themselves who make the decision to go public or not. He said if the goal is to increase the number of companies in the stock exchange there are two approaches. One, increase incentives for the companies to go public by reducing the high administrative costs associated with it. Two, facilitate new investors’ GSE involvement, such as insurance companies, by reducing the amount of restrictions on the types of investments they can make.

A fourth recommendation is to allow part-time and intermittent jobs in the formal sector. Officials agreed that this recommendation was covered in the draft of the new labor code. One public sector official noted the increase in more flexible jobs such as information processing with health insurance companies like Aetna and Keystone Mercy (Friedman, 2001). The officials also noted that in addition to the labor code change, the development of labor market institutions such as training and information centers are also necessary for this flexibility to become a reality.

A fifth recommendation was to abolish the link between wages and inflation. While this is officially the case, one public sector official is not sure how realistic it will be until the inflation comes down. One Sigma One staff member noted that due to Sigma One's work the realization that the benefits of nominal wage increases are eroded by inflation is now common knowledge. Government employees are showing their support for the new government by agreeing to accept only a 20% increase in pay for next year instead of a normal inflationary rate of 32%. Yet if the government does not bring inflation down, they may request more than the projected inflation rate for the next year to make up for this year's losses.

### 2.3.1 Firm-level Effects of Changes in Labor Market Policies

The labor market policies addressed above had expected effects at the firm level (summarized in **Table 3**). The new draft of the labor code addresses all of the above policy recommendations. Yet the new government has not yet passed the bill, desiring to go through it for themselves first. Still, some of the expected effects have been seen. The Ghana Living Standards Survey (GLSS) Two and Four indicate a slowed rural exodus, well as improved non-farm enterprise incomes. Though employment status data is not readily available before the 2000 Ghana National Labour Market Survey (2001), it lists a variety of situations including part-time employment (1.5% of EAP) and casual employment (1.2%). This variety points toward some flexibility in the labor force. In addition, though difficult to quantify, the interviewees' sense was an increased incidence of pay based on productivity versus time on the job. A consultant to the private sector noted that the daily rate of pay was not promoting productivity, so many farmers have gone to piece rate work. Exporters propose that the quality of Ghana's products is improving. Fish and fish products, as well as fresh fruits and vegetables breaking into the UK market are among those. One exporter, however, commented that the lack of streamlining of quality assurance procedures, and uniformity in grading, classification, and marketing present the pineapple industry with quality issues. He suggested that a partnership between the public and private sectors could aid in this area.

The interviewees perceived an overall improvement in the amount of investment in the workforce. The goal of FAGE's Strategic Management training program is to have entrepreneurs see labor as an investment, not a cost. Medium- to large-scale firms see on-the-job training as a valuable investment. Small and micro enterprises still see it as a cost because of the tendency of the trained person to look for a better opportunity after they are trained. However, the majority of firm-level interviewees indicated they saw on-the-job training for their workers as an investment. Thus, interviewees also indicated increased access to skills via on-the-job training or business association offerings like that of FAGE.



**Table 3. Firm-level Effects of Changes in Labor Market Policies**

Issue	Measure (Data Source)	Data Results	Agrees With General Sense Of Interviewees?
Slowed rural exodus	Percentage of Rural* to Urban migration (GLSS 2&4)	Percentage decreased from 67% in 1988-89 to 10% in 1998-99, though a rough call due to difficulties comparing GLSS 2 and 4 because of reporting differences	N/A
Improved non-farm enterprise income	Value of income received for all non-farm enterprises (GLSS 3&4)	Increase from an average annual value per enterprise in 1991-92 of 511,500 cedis to average revenue per enterprise of 4,045,600 in 1989-99.	N/A

\*Defined as “Small towns, and small and large villages” for GLSS 2, and simply “Rural” for GLSS 4

## 2.4 Improved Business Climate

The fourth and final critical issue is an improved business climate. This was one of the key topics at the NC Conference.

Improved trade policies are an important component of an improved business climate. Examples of improvements include the elimination of export bans, and fewer administrative hassles in dealing with CEPS. As of January 1999, export bans for cotton lint, natural rubber, scrap metal and yams were lifted (Deliverables Milestone chart, 2001). Sigma One did not directly influence this policy change—it had been completed before TIRP got underway. Nevertheless, previous Sigma One analyses affirm the GOG’s decision to remove these bans.

There has not been much improvement in reducing the administrative hassles of dealing with CEPS. Inspection of goods has been made more random with the help of the new X-ray machine. However, one official notes that the import regime has only been improved on paper. “Just try clearing goods at the port”, he quipped. Indeed, some goods such as South African wines and liquors are stuck at the port for days, even weeks, on end. One official says the reason for this is that the implementing officials have not bought into the new procedures. He postulates that low salaries and poor managerial communication channels are to blame. He recommends one-day stakeholder discussions to alleviate the problem. Nothing has been done on this, he believes, because the private sector has not put enough constant pressure on CEPS to do anything different, and the former CEPS director was very hostile to any such suggestions. The effect of the new government’s leadership in this area remains to be seen.

A second recommendation is to reduce the “hassle-factor” by reducing the number of permits and licenses to do business. There has been a top-down review of this regulatory process, and GOG has made some reductions. This topic was anticipated as a theme for the Year Two TIRP Forum,

but GOG has not been interested in convening these fora since the one in 1997. However, the most recent NED did address this issue (NED Action Plan, 2001). One official corroborates the reductions on the ground by saying that 3-5 years ago, to export fresh fruits and vegetables, for example, one used to have to register the company with GOG, GEPC, the product association, the IRS, SPS officiate, etc. At this time, nothing is required to export except that the company be legally registered with the Ministry of Justice.

The new government heralded its assumption of power by proclaiming the “Golden Age of Business”. Several interviewees pointed out that this will remain meaningless until the GOG follows up with concrete actions. One businessman does not currently see many incentives to invest. There is little financial security, and there is a constant threat of currency depreciation. He feels the Ghanaian banks should doing much more, such as offering interest free funds for expansion purposes to be repaid in 3 years.

A third recommendation is to improve the service and advocacy functions of business associations. According to representatives of groups such as FAGE, Seafreight Pineapple Exporters Group (SPEG), and Vegetable Producers and Exporter Group (VPEAG), many reported policy changes related to improved service and advocacy functions. One official noted that FAGE has begun offering more services and products. Examples of these are office equipment and internet use, internet hosting, a weekly commodity price report, and management training courses. SPEG acts as a coordinator of sea-freight pineapple space, as well as a pressure group on GOG and other service agencies for better facilities for the pineapple industry. Another official cites the drop in port handling charges and the creation of the Export Development Fund as two examples in which the government finally demonstrated it was listening to SPEG. He anticipates even more advocacy power once SPEG merges with HEG.

Yet some have made critical comments regarding the effect of these advocacy groups. There is a sense that the export groups are “talk shops” with not much action. One consultant to the private sector also noted that the traditional by-laws of groups like SPEG and HEG pointed to a “good ole boy” network that worked to keep people out instead of in (protecting the best product deals, etc.). Historically they have been good at doing things in their own interest. However, they are rewriting these by-laws, and making the right noises now toward moving ahead.

The fourth recommendation is to improve access to land in order to encourage expansion and investment. One official cited Sigma One’s work (Owusu Boadu, 2000) and discussions on this issue as an area of success. Challenges remain. Usufruct land is still difficult to secure because all individual owners must agree on the land use. Individuals can obtain long-term leases, only to discover that the “correct” person’s permission has not been obtained. In addition, traditional rules allow tribal leaders to hold land in trust for others, and secure title cannot be given. Fragmented lands pose an additional challenge. Often many different families inhabit lands, and the chief would have to remove people to get a lot of land together in one place.

#### 2.4.1 Firm-level Effects of an Improved Business Climate

The recommendations were expected to effect desired changes at the firm level (summarized in **Table 4**). The majority of interviewees thought that the business climate has improved in Ghana, though exact indicators are difficult to pinpoint. Evidence includes the government's declaration of the "Golden Age of Business", as well as an increase in the amount of participation perceived by the private sector. At the least, more firms are participating in their associations, and being heard via that venue. Projects like TIP and TIRP have influenced access to new markets and technologies. For example, with respect to better environmental husbandry, many Farma Pine workers have their own farms on which they apply the technologies seen on the job. While "who you know" is still important, excessive cronyism was not specifically mentioned as a continuing problem. Yet some producers still sense an underlying anti-business sentiment, for example, that seeking to maximize profits is a bad thing. This post-socialist attitude could be part of the explanation for why interviewees have not seen several other of the expected effects.

Regarding the provision of adequate public services to support business, the general sense is that they have not improved. Better infrastructure "roads, cold storage, and warehousing" has not been seen either. One official postulates this is due to a poor macroeconomic situation and a lack of investors to build the infrastructure.

**Table 4. Firm-level Effects of an Improved Business Climate**

Issue	Measure (Data Source)	Data Results	Agrees With General Sense Of Interviewees?
Smaller firms given a voice	Level of participation in business associations (Business organizations, e.g., FAGE, VPEG)	Increase in FAGE membership from 12 to 16 (1992-2001); Increase in VEPEAG membership from 7 (before 1997) to 150 (after)*.	Yes

\*Increase due in large part to reconstitution of group (became a producer and exporter association)

### 3.0 USAID Intermediate Results (IR) Progress

In this section we explore whether USAID is accomplishing what it hoped to accomplish when it designed the Trade and Investment Reform Program. Is there evidence of an improved policy reform process (Task 1)? Have improvements occurred in the financial intermediation services (Task 2)? The expected results whose presence will answer these questions are summarized in **Table 5**.

### 3.1 Task 1 Results: Improved Policy Participation

The Task One results of the IR package "Improved Policy Environment and Financial Intermediation" call for the promotion of participatory policy change. One USAID/Ghana representative said that in evaluating any policy program one must look at two separate areas: discrete impacts and process changes. Sigma One has made and carried out several recommendations regarding improved policymaking processes. These include developing a protocol for informing Parliament of working group recommendations, a plan for national consultations on a policy agenda, contact assistance for officials or private sector leaders, participatory policy working groups, and mail-based communication networks (Sigma One Corporation, 1998b).

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**Table 5. Expected Results from Tasks 1 and 2**

#### **Expected results from Task 1: Improved policy participation**

- (1) A viable policy reform agenda to increase international competitiveness
- (2) Ongoing participation of private sector in the policy dialogue and change process
- (3) Increased public knowledge of policy reforms
- (4) Implementation plans for agreed-upon policy reforms
- (5) Streamlined procedures for importation of agricultural and industrial inputs
- (6) Improved policies for exportation of specific products such as wood, cotton, yams, etc.
- (7) Elimination of export bans for products such as cotton lint, natural rubber, scrap metal, yams
- (8) Enforced compliance with BOG policy eliminating foreign exchange controls for exporters

#### **Expected results from Task 2: Improved financial market instruments**

- (1) An expansion of viable financial instruments used in Ghana
  - (2) A more aggressive and competitive financial services sector
  - (3) An increase in net domestic credit provided to the private sector
  - (4) A decrease in enterprises citing self-financing as a principle source of funds for expansion
  - (5) Increased linkages between the Ghanaian and global financial system
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The USAID/Ghana representative acknowledged that Sigma One's activities in this area have affected the way policy changes are made. Sigma One has been an objective third party that has identified and articulated a policy problem that has enabled policymakers to understand what they are dealing with. Sigma One's successful role in facilitating the negotiations for a new labor law was given as an example. One labor leader said that the summaries Sigma One prepared for the Labor Code discussions two years ago helped facilitate the negotiations. A USAID/Ghana representative commented that Sigma One has also been successful because it had the ear of high-level decision makers. One public sector official commented on the importance of Sigma One's strong relationships with various MOF officials.

A Sigma One staff member cited the recent NED as the epitome of participatory policy change. Ghanaian economists prepared and presented about 20 papers for the NED. All group members were policy stakeholders including the government, donors, civil society, and the private sector. The unique strength of these dialogues is that, unlike the 1997 NC Conference and NEF which were "threatening to GOG because they were private sector-led from the grass roots", the recent dialogues were called by the MOF in the budget statement, and thus organized and led by the government. The recommendations that came out of them are more likely to be successful because of the extensive participation of the public and private sectors.

Reform efforts will be coordinated by the National Stakeholders Oversight Committee comprising the Ministry of Economic Planning and Regional Cooperation (MEPRC), MOF, Ministry of Agriculture (MOA), MOTI, TUC, PEF, and others. This replaces the Interministerial Competition Committee (IMCC), which failed due to inefficient management and over-extended responsibilities, according to one donor official. Since December there is a new cast of characters with improved competence, commitment, focus, and dedication.

### 3.1.1 Viable Policy Reform Agenda to Increase International Competitiveness

Sigma One's "Monitoring Plan for Measuring Progress on Reform Agenda" (1998) laid out the indicators for this result. One indicator, approval of draft policy agenda, was completed in August 1998 (Milestone 1.6 in Deliverables Milestone chart, 2001). This agenda has been furthered during the NED, in which working groups consisting of all stakeholders agreed on the policy issues, recommended actions, and implementing agencies (NED Action Plans, 2001). A second indicator, implementation of policy changes, is mostly completed with approximately five key policies at varying stages of completion. The third, increased exports, has been observed. Finally, increased growth in real GDP has not been seen since 1998 as a 4.5% rate dropped to 4.2% in 1999, and finally 1% in 2000 (EIU Country Report, 2001). Despite this, all indicators point toward the existence of a viable policy reform agenda, as defined by Sigma One.

### 3.1.2 On-Going Participation of Private Sector in Policy Dialogue

Several interviewees commented on the improvements in this area. Private sector representatives noted that while the government still finds it difficult to encourage the private sector to think for themselves, at least now they are consulted. They cited the Labor bill and the Fair Trade bill as examples. They said that now 40-50% of their time is spent talking to government and participating in shareholder workshops. They pointed out that these consultations are not just to rubber stamp a government decision. As an example, when the government wanted a private sector endorsement for Destination Goods Inspection, the private sector felt it needed time to do its homework and return to the discussion table, and the government allowed this.

Another private sector representative cited the drop in port handling charges and the creation of the Export Development Fund as two examples in which the government finally demonstrated it was listening to the private sector after years of ignoring requests for action on these issues. Another private sector representative cited an example of GOG's effective involvement of private sector. When the government was in the process of creating a "Competition Law" some

elements in the private sector had objections to it. The government had a stakeholders discussion in which the private sector reviewed the proposed law with a fine-toothed comb and government representatives were on hand to answer questions. According to this individual, this would not have happened in the past.

### 3.1.3 Increased Public Knowledge Of Reforms

There are more opportunities for the public to be informed of policy changes, though more awareness is still necessary. Each daily newspaper reports on changes in policy. Members of the press (print and radio) are free to attend and report on parliament meetings. More people now call to express their opinion on the latest political happenings. One public sector official believes that the government, as well as organizations like Sigma One, should more widely publicize their activities and research findings. He thinks there is a lot of good research that very few people know about.

### 3.1.4 Established Reform Implementation Plans

The recent National Economic Dialogues have set in place implementation plans for agreed-upon policy reforms. In each of the areas addressed—"the private sector, agriculture, infrastructure, energy, the economic and financial sector, syndicate, employment, human resource development, and basic services"—working groups consisting of the relevant stakeholders agreed on the issue, recommended actions, and implementing agencies (NED Action Plans, 2001).

### 3.1.5 Streamlined Importation Procedures

The consensus among interviewees is that while export procedures have been successfully streamlined, that of imports still has challenges. Of particular challenge is the difficulty with which exporters receive VAT and duty drawback payments on their imported goods such as fruit packaging or industrial equipment. Where the delay for receiving VAT reimbursements should be about 3 months, it often takes up to two years to get the money back, if ever. This severely decapitalizes exporting firms. Several interviewees recommended that the more viable solution would be to designate the products for export use only, and make them exempt from VAT or duty in the first place. Another suggestion is to allow imported equipment used for value added processing in duty free. Finally, a few observers note that CEPS continues to fail to implement policy changes.

### 3.1.6 Improved Export Policies

According to GEPC representatives and private sector interviewees, exporting procedures have been successfully streamlined on the ground. GEPC representatives say this is obviously a big relief and a respite from the hassles previously encountered in exporting. They emphasize how much easier it is now for anyone to begin exporting because barriers to entry have been lowered. An example is the A4A form, which replaced the A2 form; the new form helps GEPC maintain a database of export values and volumes, but it does not require that exporters physically come to Accra to file it as the A2 form did.

### 3.1.7 Eliminate Export Bans

As of January 1999, bans on the export of cotton lint, natural rubber, scrap metal and yarns were lifted (Deliverables Milestone chart, 2001). Sigma One did not directly influence this policy change since it had been completed before TIRP got underway. Nevertheless, previous Sigma One analyses of these issues affirmed the GOG's decision to eliminate the bans.

### 3.1.8 Enforced Elimination of Foreign Exchange Controls on NTEs

In January of 1999, Sigma One completed an action plan to enforce compliance with the BOG policy that eliminated foreign exchange controls (Deliverables Milestone chart, 2001). These controls involve two main issues: one, control of how much currency can be held in dollars by exporters, and two, reduced hassle over export forms. GEPC reports that exporters can now keep 100% of their earnings in dollars. This is an improvement over the 30%, then 70%, of export earnings that the government allowed exporters to keep in dollars just four to five years before.

The majority of interviewees reported that the change from the A2 to the A4A form had greatly eased and simplified the export process. One private sector representative said the streamlining had been good overall, but commented that at times the A2 form was still being required, and that this was a problem.

## 3.2 Task 2: Improved Financial Intermediation

### 3.2.1 Expansion of Financial Instruments

In its TIRP proposal, Sigma One suggested several activities to increase the size and effectiveness of the financial system in Ghana. These included implementation of a secondary market for GOG debt, the design of a credit reporting service, and the introduction of an inflation index bond (Sigma One Corporation, 1998b). However, these initiatives have not been altogether successful, nor altogether appreciated by TIRP partners, some of whom commented that such specific suggestions of instruments on the part of Sigma One was a bit presumptuous without doing more "market research".

With respect to an inflation-indexed bond, these observers noted that the bond market is not very developed, and that there is already a dollar indexed bond issued by the Home Finance Corporation (HFC). There are too many unanswered questions about what the financial market needs to start by suggesting a particular instrument such as an inflation-indexed bond. *(Since the first draft of this report was submitted in September 2001, an inflation-indexed bond has been issued by the GOG.)*

Regarding a secondary market, an observer notes that legally this market exists. However, it will never be viable without a lower inflation rate, and training for administrators on how to use electronic methods of registering and exchanging the financial instruments. He recommends that some of these smaller implementation "pieces" (including the establishment of a credit reporting service) be picked up by organizations like Sigma One. In this way, they can focus their energy

on walking through a project with those who will be responsible for after the end of the project. To date, issues like these have usually been the focus of a study only; no follow-up or implementation has been attempted (in this observer's opinion) because of a lack of temporal and financial resources on the part of Sigma One.

### 3.2.2 More Aggressive and Competitive Financial Services Sector

Sigma One's "Monitoring Plan for Measuring Progress on Reform Agenda" (1998) laid out in the indicators for this result: an increase in private sector loans, a decline in interest rates, and an increase in private sector savings. Private sector loans, as a percentage of total domestic credit, have been falling from a peak of 69% in 1996 to 35% in 2000. Interest rates, exemplified by the T-bill rate, have declined 43% in 1997 to 32% in 1999 (EIU Country Profile, 2000). However, private savings have fallen (ISSER, 2000).

### 3.2.3 Increase in Net Domestic Credit for the Private Sector

The consensus among interviewees is that access to long-term credit has not improved over the last three to five years. As noted above, private sector credit as a share of total domestic credit has declined. The new government has agreed to a "cash-budgeting" system, aiming for 0% financing by the end of this year (2001), according to a public sector representative. This should increase the amount of domestic credit available for the private sector. The previous government's excessive use of credit to finance campaign expenditures in 1999 was a severe setback to the economy, and has rendered any results of the new government's policies virtually imperceptible at this time.

### 3.2.4 Decrease in Self-Financed Business Expansions

The consensus among interviewees is that self-finance is still the principal source of funds for expansion. The ISSER 2000 report shows that one additional company was listed on the GSE, but another was delisted, leaving the net number unchanged at 22 companies. Some companies and business enterprises obtain funds informally (via "sou-sou" systems in rural areas) or via international lenders in Europe or the US. The latter source is usually limited to multinational companies. Indicators of the degree of financial system formality in the economy (M2/GNP, currency as a share of M1, and quasi-money as a share of GDP) have been virtually unchanged over the past ten years.

A small and underdeveloped GSE also increases reliance on self-financing. Sigma One, with the help of SEM International, has addressed the issue of developing the GSE with little success. Reasons cited for lack of success include: GSE's ineffectiveness in self-promotion; the prohibitive administrative costs of going public; the lack of demand for publicly traded stocks; and the lack of technical expertise of efficient administration of a stock exchange. GSE is the wrong target organization to promote private stock issues since GSE has no power to attract companies to join it, only to facilitate their trading once they join. The more appropriate focus would be on the companies themselves who make the decision to go public or not. More companies might be induced to go public if the high administrative costs of doing so could be



reduced. Demand for stocks might be increased by facilitating new investors' GSE involvement, such as insurance companies, by reducing restrictions on the types of investments they can make. Finally, much technical expertise with respect to scriptless, electronic management of stock trading is needed before the GSE will be popular and successful. According to this observer, once all these needs have been met, GSE will reach a critical mass and begin to create a joining fervor among privately held companies.

Another observer noted that many Ghanaians are still not used to transparency, especially in business dealings, and are just not comfortable with the idea of other people knowing how and what business decisions are being made, nor relinquishing control of those decisions.

### 3.2.5 Increased Linkages Between Ghanaian and Global Financial Systems

Sigma One's "Monitoring Plan for Measuring Progress on Reform Agenda" (1998) laid out in the indicators for this result. The first indicator, foreign direct investment, shows declining investment project numbers from a peak in 1997 of 234 projects to 180 in 2000. This differed from what most interviewees perceived, which was that foreign project interest had been increasing. The second indicator, a stable and realistic exchange rate, has been observed, as the cedi has been stable for the last six months, with no intervention by BOG. The third indicator, a strategy for improved monetary management, was completed in March of 2000 (Deliverables Milestone chart, 2001). The final indicator, the rate of inflation, showed mixed results: from an average of 19.3% in 1998, it declined to 12.4% in 1999, then increased to 25.2% in 2000.

## 4.0 Conclusions

Sigma One Corporation's areas of success in the Trade and Investment Reform Program include:

- Labor code draft process
- Implementation of a participatory policymaking process
- Broad budget presentation
- Reduction of exemptions and liberalization of tariffs
- Exchange rate policy: Non-intervention in the Foreign Exchange market
- Bonded warehousing
- Transparency of interest rate setting
- Domestic debt reduction
- Government spending reduction
- Cash budgeting
- Adherence to monetary targets

Sigma One is on target toward satisfying the USAID Intermediate Results, with a few areas to work on. Looking toward the final years/future of TIRP, the following areas have been suggested for improvements:

**Follow through.** Various interviewees noted the ambitious agenda of Sigma One. Many of them felt that the goals were too broad to be accomplished within the resources provided. The

perception of many Ghanaians at the implementation level is that many of the resources supplied by TIRP have gone to consultants to produce numerous reports, leaving nothing to cover follow-up and further technical assistance to implement the reports' suggestions. This has failed to motivate middle-level employees. If Sigma One could narrow its focus to some choice niche projects, it would be able to see them through from inception to implementation (creation of a credit reporting service was given as an example).

**Implementer attention.** A focus on working with the implementers to accomplish smaller projects would likely be more successful than a Sigma One representative sitting in with policymakers as a counterpart.

**Use of local talent.** It was recommended that Sigma One use local people more extensively on a full-time basis. The proposed Senior Monetary Economist is a Ghanaian. Ghanaians prepared 20 papers for the recent National Economic Dialogues. Sigma One intends to use local consultants when it is appropriate, subject to their availability.

**Publicity.** Sigma One has completed various activities (communications, town hall meetings, mailing list development, etc.) to improve the public's knowledge of reforms. It was recommended that the reforms be publicized even further, along with highlighting the research that Sigma One has done. However, the release of information to the public from reports done by Sigma One Corporation for the government is inappropriate, and therefore discouraged. Sigma One releases the information that it can legitimately, but otherwise much of what it produces for the GOG is subject to GOG's discretion.

Sigma One Corporation appears to be meeting the majority of the Task 1 Expected Results, and none of the Task 2 Results. The only Task 1 result not satisfied is that of "Streamlined importation procedures". This policy reform has been officially changed, but not fully implemented. Key challenges include getting the government to repay VAT and duty drawbacks in a timely manner and continued problems with CEPS. With respect to the former challenge, Sigma One Corporation has written a request for technical assistance to address this.

Sigma One has encountered more challenges in meeting the Task 2 results. The key setback here has been the lag time between the new fiscal and monetary policies of the current government and their resultant effect on the economy. This lag has challenged the viability of new financial instruments, an aggressive and competitive financial sector, availability of net domestic credit, externally financed expansions, and linkages between the Ghanaian and global financial systems. The current government appears to be sticking to the a sensible set of policies, many of them suggested or supported by the international financial institutions and Sigma One Corporation, and it is expected that this will pay off for them in the near future.

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## **Appendix A. List of Interviewees**

Dr. Sam Mensah, Private Consultant, SEM International

Mr. Gary Kilmer, AMEX

Mr. Emmanuel Addison, Ghana Export Promotion Council

Mr. Girma Birgashaw, Country Representative, International Monetary Fund

Mr. Matthew Armah, AMEX

Mr. Nicholas Railston-Brown, Country Director, Technoserve

Dr. Yahaya, Bank of Ghana

Dr. Bawumia, Bank of Ghana

Dr. Fenton Sands, Head of the Office of Trade, Agric. & Private Sector, USAID

Mr. Louise Amoo, Ministry of Finance

Mr. Steve Mintah, General Manager, SPEG

Mr. Henry Wientjes, Owner, WIENCO

Mr. Augustine Adongo, Executive Director, FAGE

Dr. Tony Mensah, President, Athena Foods

Mrs. Esi Nyadodui, Shareholder, Golden Harvest (TEXPO)

Mr. Augustine Gyamfi, Executive Director, Vegetable Producers Exporters Association

Mr. John Addaquay, Farma Pine, TechnoServe

Mr. Samuel Ayison, Scanstyle

Mr. Adu-Amankwah, Secretary General, Trades Union Congress

Mr. Harry Owusu and associates, Private Enterprise Foundation

Mr. Kingsly Ameyaw, Air Ghana

Mr. Ernest Adzim, Quality Assurance, Oké Bananas (VREL)

Dr. Tony Osei, Ministry of Finance

Henry Panlibuton, TechnoServe

Esther Osofsuapea, Office Manager, Sigma One Corporation-Ghana

Emmanuel Ahwireng, Office Support, Sigma One Corporation-Ghana

Emmanuel Owusu, Field Coordinator, Sigma One Corporation-Ghana

Abrar Sattar, Technical Director, Sigma One Corporation-RTP

Ralph Franklin, Senior Labor Policy Analyst, Sigma One Corporation-RTP

Robert Conrad, Tax Consultant, Sigma One Corporation-RTP

Dr. Joe Goodwin, Chief of Party, Sigma One Corporation-Ghana

## Appendix B. Stakeholder Interview Summaries

Discussions were held with Sigma One personnel in RTP and Ghana, USAID officials in Ghana, and both Ghanaian public and private sector representatives who have either helped implement the program or been in a position to witness its effects. Questions centered around either key policy issues, key firm-level effect issues, or implementation issues depending on the nature of the interviewee.

The Sigma One personnel in RTP and Ghana overall are pleased with the program's progress. However, each noted challenges that the project currently faces. One noted the challenge of putting the final touches on the labor code and helping the new government feel comfortable enough with it, to pass it into law. Another stated that, while pleased with the strides that Sigma One has made in the area of the trade regime, difficulties still remained with respect to slow VAT and duty drawback reimbursements. Another staffer remarked on the high level of ambition of TIRP, and the ensuing resource allocation questions of how to best spend time and energy to get the most effective changes made. A USAID representative is keenly aware of this challenge, and notes that it is hard to be able to identify so many problems, and yet not have the resources to deal with each and every one. He sees his role at AID-Ghana as one of reining in both the GOG and Sigma One Corporation when they attempt to do too much. Overall, though, he believes Sigma One's policy participation work has been very effective.

Ghanaian public sector individuals commented mostly on the policy-related issues. They were more closely led through the "Improved Policy Reform and Financial Intermediation: Expected Improvements and Resulting Effects" (**Table 1**) than the private sector interviewees. Most agreed with the indications of the chart. The most frequent issues of controversy with the chart were the recommendation that the SSNIT should reduce its presence in the GSE, the suggestion that the requiring banks to hold 35% secondary reserves "forces" them to lend to the public sector, and the recommendation of very specific financial instruments such as an inflation-indexed bond.

Finally, Ghanaian private sector interviewees addressed their perception of the prevalence of the firm-level effects identified as indicators by Sigma One at the start of the program. Strong consensus issues were access to long-term credit (still bad), streamlined exporting procedures (very good), and VAT and duty drawback reimbursements (very slow).