

SECURITIES LITERACY WEEK CELEBRATION

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Mr. Chairman,

Hon. Minister of Finance and Economic Planning, Honourable

Ministers of State,

Distinguished Guests,

Ladies and Gentlemen,

1. It is a pleasure to be present at this event, which is launching the **Securities Literacy Week**. First of all, let me congratulate the Securities and Exchange Commission for organizing this week's program of activities. And certainly, the "Capital Market" offers an appropriate theme for public discussion and policy discourse at this stage of implementation of the Growth and Poverty Reduction Strategy (GPRS).

2. The issue is whether the Capital Market is the "missing link" in this strategy or an integral component that has to be developed because the conditions are now right, and if so

what are the challenges and the opportunities presented by a capital market development policy.

3. Mr. Chairman, to begin with, for an economy emerging from a high inflation environment, successful stabilization is fundamental to the quest for growth and poverty reduction; and it provides the foundation for capital market development; for efficient financial intermediation, i.e. mobilization of savings and transforming such savings into productive investment.

4. High and variable inflation and currency instability stymies the growth of the financial sector; it creates incentives for misallocation of resources and uncertainty that makes it extremely difficult for firms to plan, consumers and savers to make forward-looking decisions, It leads to an arbitrary and inequitable distribution of incomes; inflation, worst of all serves as a tax that hits hardest the most vulnerable groups and the poor.

5. Surprise inflation creates financial distress for banks as it erodes their capital as well as those of their corporate and other customers. Persistent instability shortens the horizon of corporates and financial structures, cuts short the maturity of debt, including government debt, and stifles the development of the financial system and the market for capital more generally. Stability stretches business horizons, lengthens the maturities of debt, and long term savings, risk taking and investment.

6. Emerging from historically high and volatile inflation environment, I believe, as a country we have come to appreciate the costs of instability. For much of its legacy still remains the concern of policies in the current regime of macroeconomic stability.

7. To illustrate this point:

- Government has been reliant predominantly upon concessional resources (and debt relief) from Bilateral donors and Multilateral financial institutions, for external revenue, and principally on short-dated Treasury Activities (91-day and 182-day Bills) for financing. Although just over the past year, we have seen a significant lengthening of the maturities, with the voluntary public uptake of the 2year and 3-year notes, as inflation expectations have grown increasingly mute. Thus, the primary domestic financial market activity remains driven and dominated by government debt, with very little secondary market activity.
- Private sector savings are mostly concentrated in short term Treasury Notes,
- Commercial Banks have locked considerable liquidity invested in such gilt-edged instruments, with the appetite for risk-taking still constrained by the history of nonperforming loans and difficulty in recovery of collateral.
- More generally, the economy overall depends on bank financing, while banking system intermediation is weak, measured by the amount of total credit to GDP which stands at 23.2 percent as at end September 2006.

- To a large extent, companies still rely on internally generated funds, or bank credit to finance ongoing and new investment projects. Small and medium sized enterprises rely on family and friends, where possible, with little access to credit.
- The stock market has seen market capitalization increasing to 99.2 percent of GDP in 2006, from 10.3 percent in 2001, but it still shows relatively limited liquidity and turnover.
- Public enterprises in key sectors of the economy depend mostly on government externally borrowed resources and budget transfers for investment.

8. A well-functioning stock exchange can be a source of efficiency, and key in providing funding for the corporate sector and liquidity for investors. It helps when risks inherent in the market are mitigated through transparency that improves price discovery, through prevention of market abuse, including reporting insider trading. Equally important are adequate disclosure requirements and enforcement, and better still when regulatory burden is minimized and the regulator has strong reputation and credibility.

9. Mr. Chairman, this is a setting in which economic growth and resource allocation tends to hinge on public sector investment, shifts in factors of production, and the growth in productivity of a few sectors, (eg. Cocoa sector); and re-investments from internally generated funds is characteristic of the present state of the economy. Resource allocation and growth depends less on the financial sector.

10. Domestic financial markets are vital pillars of a growing economy. Efficient mobilization of capital and allocation of financial resources is integral part of economic development. And it also has been documented that capital markets play an essential role in improving corporate governance, disclosure, and accounting standards, and transparency in the market place. As such they contribute to more stable investment financing, high economic growth and lower macroeconomic volatility and greater financial stability.

11. The challenge therefore is to develop and expand the domestic capital market as a part of the financial system to allocate savings and investment. It should be an essential part of the development paradigm.

12. A well developed and efficient capital market would certainly offer an alternative but complementary source of funding to bank-debt financing and international capital markets for corporates as well as the public sector. At the same time it would encourage domestic savings through financial instruments that broaden the set of investment products, and allows better portfolio diversification, other than concentrating on deposits and domestic equities. And, it would serve as a vehicle for allocating foreign capital. As such the

development of the domestic financial market reduces the risks associated with excessive reliance on foreign capital including currency and maturity mismatches, the risks associated with committing the "original sin"-borrowing in foreign currency instead of local currency.

13. The policy issue is how to develop and strengthen this capital market pillar in the growth strategy. Even though the fundamentals are well placed to facilitate the development of the capital market, there are still formidable obstacles. This is because the prerequisites for a vibrant capital market are the very prerequisites for economic development, namely a strong macro economy, including robust growth, low inflation, long-run fiscal and monetary policy discipline. They include transparency, good governance, protection of property rights, and sanctity of contracts, and effective payments and settlement systems, These are the very conditions that underline the capacity of the economy to mobilize efficiently and transform savings into productive assets and income and job creation.

14. Some of the pre-conditions, some of the hard and soft infrastructure are already there to build upon.

- The domestic money market for government debt paper provides an anchor, on which to extend the yield curves that are critical for the pricing of income securities and derivatives. In this regard the listing of the 2-year and 3-year notes by the Government on the Ghana Stock

Exchange is a significant first step.

- The Bank of Ghana has introduced a Real Time Gross Settlement System (RTGS), this has made clearing instantaneous and eliminated settlement risks, introduced safety and security for high value inter-bank transactions .
- A central securities system has been in operation and efficiently for over a year now, and it is to be extended to cover equities and securities listed on the Ghana Stock Exchange. The system restores security of title. brings efficiency to the system of documentation and facilitates trading including on the secondary market.

16. The question is what can be done to foster the development of a vibrant money market? To begin with, stable macroeconomic conditions are fundamental. On this, we can say that the African economic landscape has been changing for the better, as the economic reforms are yielding benefits in the form of rising GDP growth rates, low inflation reduced fiscal and current account deficits and improved external debt indicators. The trade and payments system is liberalized with restriction on current account transactions removed. And there is the national commitment to good governance making the rule of law and protection of property rights and enforceability of contractual

obligations and accountability. These are positive developments in the outlook that have to earn reasonably good sovereign credit ratings, positioning the economy to attract capital flows to bolster the capital market.

17. It is important to build a formidable club of players for our domestic capital markets. The pension and mutual funds, insurance companies and social security, which have been placed largely under public administration, could release a significant pool of captive resources to be channelled into the capital markets. This potential source of liquidity must be tapped. It would enable enterprises to have access to longer-term capital to grow businesses, with the potential for creating jobs and contribute to sustainable reduction in income poverty levels.

18. One critical question is what can be done to increase the risk appetite of global investors, the suppliers of capital, the managers of large fund portfolios, to dispel their hesitancy to commit funds into the equity and bond markets, and bolster the growth of our domestic capital markets as we develop them. External investors' presence in the market

would provide strong signal of confidence in the economy. And if they do commit, their resources, what should be done to reduce the risk or avert "sudden stops" and the types of reversals that magnify financial crisis. We would need to pursue policies that reduce vulnerabilities to this free flow of capital. All these have implications for the quality of policies and institutions, and regulatory and supervisory systems that should be put in place. These will determine the creditworthiness ratings, quality of the debt of the sovereign and private and public sector borrowers seeking to tap the market, for resources.

19. Mr. Chairman, Ladies and Gentlemen, to close, let me note that, a capital market is basically efficient and productive only when fundamentals are right. This underscores the importance of sustaining the stability we have achieved without which both the soft and hard structures would not be effective.

20. Mr. Chairman, Ladies and Gentlemen, on this note, let me congratulate the SEC for instituting this week and let us all join them to create the necessary awareness.

Thank you for your attention.

