Monitoring Cross Border Capital Flows in Ghana – 2009 Survey Findings and Policy Issues

ISSUES

This policy brief highlights the findings of the 2009 Cross Border Capital Flows Survey, the third to be conducted by the Bank of Ghana since 2000.

In sub-Saharan Africa, private capital flows constitutes a major source of capital to meet financing requirements aimed at economic expansion. Its multiplier effects on job creation, technology transfer, and higher growth prospects cannot be over emphasized. This notwithstanding, private capital flows are subject to volatilities. In this context, recently established codes and standards have been established within the global financial architecture to improve the stability of capital flows across countries. One of such is the monitoring of private capital flows for effective policymaking.

The Bank of Ghana's 2009 Survey aimed at monitoring the scale and nature of private capital flows between 2007 & 2008; and improving coverage of the private sector's foreign investment in Ghana for the compilation of Balance of Payments and International Investment Position (IIP).

Among others, the survey findings indicate that Ghana's net liability IIP was estimated at US$6 billion in 2008. One critical lesson drawn from the 2009 Survey is the need to improve the investment climate further by providing good infrastructure across the country. By so doing, private capital flows will be evenly spread across various sectors and regions to ensure a broad-based national economic development agenda.

Background

Following the adverse effects of the global financial crisis on international capital flows in 2008, foreign direct investments slowed down but not proportionate across regions. For instance, annual global FDI flows was estimated at US$1.69 trillion in 2008, about 10% lower than flows in 2007, but FDI flows to Africa remained resilient, increasing by 16.8% to US$61.9 billion in 2008. According to the 2008 World Investment Report (WIR), projected FDIs from developed countries may decline in the near future due to the dampening effects of the financial crisis coupled with weaker economic growth prospects.

Ghana continues to attract significant foreign direct investment flows within the West African sub-region, especially in project financing. This is underscored by political stability, improved investment climate and increasing investment opportunities. In 2008, economic performance was severely challenged by the global food and fuel shocks as well as fiscal expansion to meet the country's infrastructural and growth needs. Also, the general elections adversely affected business sentiments as some investors adopted a 'wait and see' attitude on key investment decisions until after the elections. But, the economy has since regained macroeconomic stability through prudent management and fiscal consolidation measures.

Foreign capital flows are generally cyclical in nature, increasing when economic conditions and the regulatory environment are favourable and declining otherwise with adverse effects on economic management. Therefore capital flows needs to be closely monitored to safeguard macroeconomic stability. Against this backdrop, the Bank of Ghana has since 2000 undertaken a series of surveys to monitor inflows and outflows of private capital to Ghana for effective policy formulation.

Survey Findings

1. Cross Border Capital Liabilities of the Private Sector

The survey estimates on private cross border liabilities in addition to data obtained from monetary and financial statistics on loans, currency and deposits, and other capital components, showed that in 2008, foreign direct investment (FDI) flows as a share of private capital flows was 65.6% (representing about 11% of GDP).

By the end of 2008, Ghana had total external liabilities of GH¢10,866.54 million (about US$9.0 billion). This reflects an accumulated inflow liability position of cross border capital of GH¢2,929.85 million (about US$2.4 billion) during 2008. The survey results showed that all the components of external liabilities covered registered positive growth.

Of the total external liabilities, the stock of direct investment liability constituted about 50.5% amounting to GH¢5,495.59 million in 2008 and GH¢3,574.80 million in 2007 reflecting an increase of GH¢1,920.79 million during 2008.

Equity capital and reinvested earnings by corporate entities also formed an important source of financing foreign direct investment during 2008. It accounted for about 43.7% of total stock of foreign direct investment. Another component of direct investment in Ghana that contributed significantly to the stock of liability was 'other' capital (liabilities to direct investors). It increased from a stock level of GH¢1,736.19 million in 2007 to GH¢3,096.19 million in 2008, representing a significant inflow of GH¢1,360.00 million during 2008.

The survey results indicated that portfolio investment (equity stake less than 10%) covering financial instruments in the form of equity and debt securities that are usually traded in Ghana's financial markets were relatively lower. The stock of portfolio investments increased by GH¢233.67 million to about GH¢1,006.21 million in 2008 from a stock position of GH¢772.54 million in 2007.

The final component of cross border capital liabilities represented by 'other' investments consists of trade credit, loans, currency and deposits and other liabilities. In this category, the stock of outstanding trade credit was GH¢92.03 million as at end 2008, down from stock level of GH¢336.53 million in 2007. All trade credit was acquired by government institutions as well as non-bank financial institutions. Loans constituted the largest component of the stock of 'other' investment, estimated at GH¢3,945.18 million. The bulk (about GH¢3,732.50 million) of the loans had long-term maturities. The overall position shows that Ghana attracted substantial private cross border capital in 2008 to supplement domestic investment requirements.

2. Foreign Liabilities (FL)

A total of 224 entities reported Foreign Liabilities in the 2008 survey. We analyze the findings on FL components represented by equity, Private Sector External Debt (PSED) and other claims.

The survey results indicated that total foreign liability stock levels expressed in book value terms recorded a 57.7% growth from GH¢4,029.75 million in 2007 to GH¢6,354.83 million in 2008. All components of FL covered in the survey recorded positive growth. In 2008,

Fig. 1: Composition of Private Cross Border Liabilities (GH¢ m)

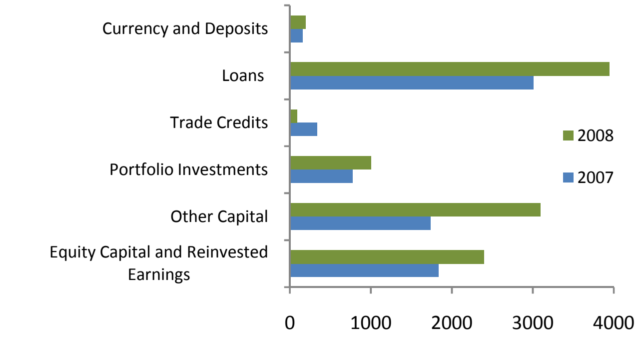


Fig. 2: FDEI Stock by Sector (GH¢ m)

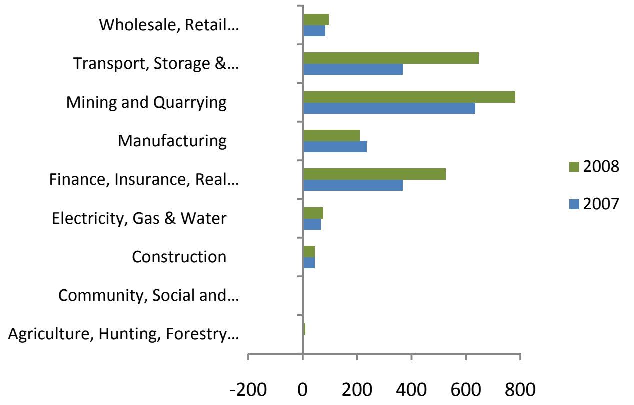
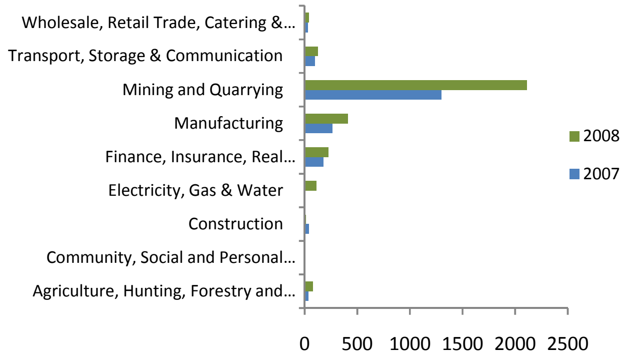


Fig. 3: Private Sector External Debt Stock (PSED) by Sector (GH¢ m)



FDI constituted 86.5% of the total stock of foreign liabilities most of which were equity or long term loans from related entities/shareholders. Non-FDI increased by 92.6% with long-term loans from related entities/shareholders forming the bulk of investments. Other Claims increased by 7.1% largely on account of an increase in currency and deposits, custody accounts and management fees.

3. Type and Sector Distribution of Cross Border Liabilities

❖ **Foreign Direct Equity Investment (FDEI)**

FDEI stocks analyzed in book value terms revealed that Mining and Quarrying accounted 34.5% share of the total FDEI stock in 2008; followed by the Transport, Storage and Communication and Finance sectors with respective 22.5% and 20.2% shares. During the period, there were net inflows of GH¢252.26 million, GH¢160.30 million and GH¢146.09 million in the Transport, Storage and Communication; Finance and Business Services; and Mining and Quarrying sectors respectively.

The Mining and Quarrying Sector also recorded the highest amount of equity capital (paid up share capital) of GH¢894.64 million equivalent 57.8% of the total equity capital in 2008. The Finance sector had the second largest share amounting to GH¢200.99 million (representing 13% of the total equity capital).

For the second consecutive year, Europe emerged as the leading source of FDEI accounting for a relative share of 50.78% in 2008, followed by the Middle East (29.12%) and the Rest of Africa (16.83%). By country of origin, United Kingdom remained the leading source of FDEI in 2008 with 31.94% share followed by Lebanon (27.0%), South Africa (14.5%) and France with 8.5%. Most of these countries invested in the top three sectors.

❖ **Foreign Portfolio Equity Investment (FPEI)**

Few sectors attracted foreign portfolio investments during 2008. In book value terms, the majority of FPEI stock in 2008 went to the Finance Sector (57.2%), followed by the Transport, Storage and Communication Sector (42.4%) with the Wholesale; Manufacturing and Agricultural Sectors accounting for 0.1% each.

In 2008, Oman and Lebanon accounted for respective FPEIs of GH¢15.32 million and GH¢0.65 million. These investments were channeled into the Transport, Storage and Communication sectors. Countries from Europe, that is, United Kingdom and Cyprus contributed respective FPEIs of GH¢9.31million and GH¢1.27million which were channeled to the Finance, Insurance, Real Estate, Tourism and Business Services sector. The United States contributed GH¢8.81 million directed mainly at the Finance sector.

❖ **Private Sector External Debt (PSED)**

The stock of Private Sector External Debt (PSED) grew by 82.1% from GH¢2,076.59 million (about US$2.1 billion) in 2007 to GH¢3,781.97 million (about US$3.1 billion) in 2008. The growth in stock was explained by net inflows of GH¢1,292.97 million (about US$1 billion) and other changes (largely as result of exchange rate changes) of GH¢412.42 million. The results revealed that 89.1% of the total debt had long-term maturities, with short-term debt accounting for the remaining 10.9% in 2008.

By sector classification, entities in the Mining and Quarrying sector registered the highest portion of PSED outstanding balance of GH¢1,301.91 million (about US$1.34 billion) and GH¢2,111.91 million (about US$1.76 billion) in 2007. The Manufacturing sector followed with GH¢262.51 million in 2007, increasing to GH¢409.25 million in 2008. The Transport, Storage and Communications sector and Finance, Insurance, Real Estate, Tourism and Business Services sectors recorded an outstanding balance share averaging 12.7% and 10.4% of the total debt for the two consecutive years.

Across the sectors, changes in PSED stock by respective net flows and other changes indicated that the Mining and Quarrying sector recorded the largest change of GH¢810.01 million, followed by Transport, Storage and Communication; Manufacturing; and Electricity, Gas and Water sectors with GH¢521.39 million, GH¢146.75 million and GH¢105.81 million respectively. Entities in Construction, however, recorded a decline in debt by GH¢29.41 million as the sector repaid most of its debt during 2008.

The PSED stock by source country revealed that the United States, Canada, United Kingdom and South Africa were the major sources of external borrowings, with each recording respective average shares of 45%, 16%, 13.5% and 4.6% of the total debt for the two year period. In terms of net inflows and other changes, GH¢822.10 million was contributed by the United States, GH¢409.64 million by United Kingdom, GH¢152.54 million by Canada; as well as GH¢113.17 million and GH¢55.04 million by China and South Africa respectively.

4. Cross Border Capital Assets by Resident Enterprises

Ghana's total stock cross–border capital assets of the private sector was estimated at GH¢4,874.25 million (about US$4 billion) in 2008, up by 7.12% from GH¢4,550.35 million in 2007. The low level of the asset position relative to the liability position indicates that on a net basis, Ghana was a recipient of financial flows.

Direct investment abroad in the form of equity capital, reinvested earnings and other capital amounted to GH¢582.86 million in 2008 an increase of GH¢428.43

million, adding to the stock of GH¢154.42 million estimated for 2007. Other capital in the form of claims on the affiliated enterprises accounted for 7.6% of the total outflow of GH¢428.43 million; the difference of 92.4% was contributed by equity capital and reinvested earnings. The stock of portfolio equity investment stood at GH¢13.57 million in 2008 an increase of GH¢2.39 million from the stock of GH¢11.18 million estimated for 2007.

The stock of 'other' investments comprising trade credits, currency and deposits and other assets recorded 8.4% growth from GH¢1,690.37 million in 2007 to an estimated GH¢1,832.32 million in 2008. Trade credit extended to non-residents increased from the 2007 stock level of GH¢10.04 million to GH¢101.89 million in 2008. The total stock of currency and deposit fell by 7.35% from GH¢1,511.00 million in 2007 to GH¢1,400 million in 2008.

The total reserve assets comprising monetary gold, holdings of Special Drawing Rights (SDR), reserve position with the IMF, foreign exchange and other claims was estimated at GH¢2,445.50 million in 2008, a decrease of GH¢248.87 million. Foreign exchange earnings fell by GH¢321.07 million to GH¢2,139.50 million in 2008. Monetary gold, on the other hand, increased by GH¢65.33 million from GH¢228.74 million in 2007 to GH¢294.08 million in 2008. Comparing the assets position to the liability position shows that on a net basis Ghana has been a recipient of financial flows.

5. Ghana's International Investment Position

Results from the survey in addition to other data sources such as Bank for International Settlement (BIS), estimates of currency and deposits assets of other sectors, monetary and financial statistics, and balance sheet statement of Ghana International Bank (GIB) London showed a net liability International Investment Position (IIP) of about GH¢5,992.29 million in 2008 having increased from a net liability position of GH¢3,386.34 million. This comprised total asset stocks of GH¢4,550.35 million and GH¢4,874.25 million and total liabilities of GH¢7,936.69 and GH¢10,866.54 for 2007 and 2008 respectively. Developments in the IIP showed that Ghana attracted and retained a considerable amount of cross border capital in 2008.

6. Comparison of Survey-based and Current Balance of Payments (BOP) Estimates

Following the survey findings, Ghana's BOP account was reconstituted to incorporate the survey estimates for comparison purposes with the initial BOP statement for 2008. To allow for a comprehensive assessment of the impact of the survey results on the BOP, supplementary data from the monetary and financial statistics and the Bank for International Settlements (BIS) were incorporated with the survey results.

Comparison of Survey Based and Current BOP Estimates

	2008 without survey results US$ Million	2008 with survey results US$ Million
A.CURRENT ACCOUNT BALANCE (A1+A2+A3)	**-3,543.11**	**-3,599.23**
A1. Goods Account (Trade Balance)	-4,998.77	-4,998.77
a) Total Exports (fob)	5,269.73	5,269.73
b) Total Imports (fob)	10,268.50	10,268.50
A2. Services and Income	-755.84	-811.96
A3. Current Transfer (net)	2,211.50	2,211.50
B. CAPITAL AND FINANCIAL ACCOUNT		
BALANCE (B1+B2)	**3,126.88**	**3,727.43**
B1. Capital Account	**463.31**	**463.31**
a) Capital Transfers inflows (credit)	463.31	463.31
B2. Financial Account (excl. financing items)	**2,663.57**	**3,264.17**
a) Direct Investment	**2,102.78**	**1,967.52**
i) Direct investment abroad	-8.82	358.82
ii) Direct investment in Ghana	2,111.60	1,608.70
b) Portfolio investment	**-49.01**	**200.88**
Assets	0	5.18
Liabilities	-49.01	195.7
Equity Securities	0	2.11
Debt Securities	-49.01	193.59
c) Financial Derivatives, net	**0**	**0**
d) Other Investment	**609.8**	**1,095.77**
Assets	692	212.28
Trade credits	0	76.93
Loans	692	0
Currency and deposits		
Other Assets	0	135.35
Liabilities	-82.2	883.49
Trade credits	-39.79	29.31
Loans	409.62	785.02
Currency and deposits	-130.89	25.09
Other Liabilities	-321.14	44.07
C.OVERALL BALANCE (A+B)	**-416.23**	**128.25**
D. RESERVES AND RELATED ITEMS	**416.23**	**-128.25**
a) Reserve assets	757.16	757.16
b) Use of fund credit and loans		
c) Exceptional financing		
d) Errors and Omissions	-340.93	-885.41

- **The Current Account**

Comparing the BOP with and BOP without survey results showed a deterioration of US$56.12 million in the current account arising from an increase in the deficit on the income account. The current account deteriorated from a deficit of US$3,543.11 million to a deficit of US$3,599.23 million. The increased deficit on the income account was due to the inclusion of estimates of US$181.93 million reinvested earnings debits provided by the survey and estimated interest payments on the stock of private debt of US$43.09 million, as well as US$90.70 million of payments in compensation to non-resident employees engaged in the private sector. These estimates worsened the services and income balance from a deficit of US$755.84 million to a deficit of US$811.96 million.

- **Capital and Financial Account**

The capital and the financial account reflected the observed effects of using the survey results on the BOP estimates. Overall, the financial account improved when the survey estimates were incorporated from a surplus of US$3,126.88 million to a surplus of US$3,727.48 million in 2008. The increase in the surplus on the financial account was equivalent to an additional inflow to the BOP of US$600.60 million. The additional inflow was sufficient to more than offset the deterioration of US$56.12 million on the current account. Much of the additional inflows in the financial account were due to higher estimates of portfolio investments in Ghana in a form of debt securities and other investment liabilities in a form of loans and trade credits.

- **Overall balance**

The comparison showed a higher overall BOP surplus of US$128.25 million compared to initial BOP deficit of US$416.23 million suggesting additional inflows of US$544.48 million. Net errors and omissions increased because of the increase in the net inflows to the BOP without corresponding increases in the use of funds.

7. Economic and Social Contribution of Foreign Investments

- **Turnover in Book Value Terms**

Analysis of entities surveyed data indicated that total turnover improved to GH¢8,466.67 million (about US$10.2 billion) in 2008 from GH¢5,802.99 million (US$5.6 billion). Within sectors, the highest proportion of total turnover of 25.4% in 2008 was registered by the Mining and Quarrying sector. This was followed by Finance, Insurance, Real Estate, Tourism and Business Services with 19.3%; Manufacturing (18.9%), and Transport, Storage and Communication sector (17.5%).

- **Actual Investments**

The survey results showed that actual investments by the surveyed entities grew by 51.9% to GH¢5,513.68 million (US$6.6 billion) from GH¢3,629.40 million (US$3.5 billion). This is consistent with the 45.9% growth in total turnover by all the sectors in 2008. The highest investments were recorded in the Mining and Quarrying; Transport, Storage and Communication and Manufacturing sectors with relative shares of 57.3%, 19.6% and 9.9% in 2008 compared with 50.7%, 20.9% and 12.3% in 2007 respectively.

- **Employment Levels**

The findings indicated that during the review period, employment levels within surveyed entities grew by 7.43% to 63,874 in 2008. Although male employees dominated the workforce of entities, their share in total employment fell slightly from 82.1% in 2007 to 81.8% in favour of female employees. The proportion of female employees in the total employment went up to 18.1% in 2008 from 17.9% in 2007.

Disaggregation of the employment survey data showed a general increase of 7.3% in jobs occupied by Ghanaians. On decomposition into skilled, unskilled and casual categories, there was a marked increase of 12.6% in the level of employment for skilled local employees, 0.64% increase in jobs for local unskilled persons and local casual labour force increased by 5.47% between 2007 and 2008.

By economic sectors, about 29.83% share of the total jobs in surveyed entities were found in the manufacturing sector, followed by financing and insurance (24.35%), mining (20.21%) and agriculture (13.04%). To a large extent, the trends reflect the employment generating potential of these sectors as increased investments in plant and machinery requires the employment of operationally skilled personnel. The increased use of computers in the financial sector as well as increased branch networking has also created space for absorption of employees with the requisite skills especially in the banking sector.

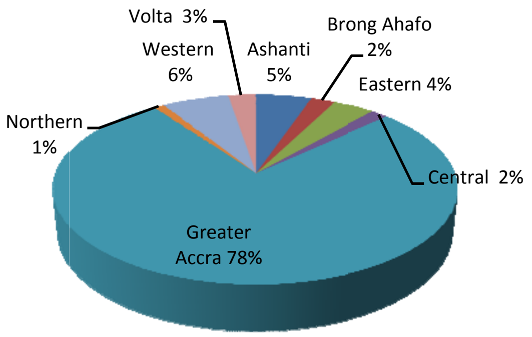
- **Corporate Social Responsibility**

All the surveyed enterprises contributed significantly towards the socio-economic development of the country through their Corporate Social Responsibilities (CSRs). In 2008, the overall contribution of CSRs almost doubled to GH¢66.06 million from GH¢34.28 million in 2007, indicating a 92.7% growth. Broadly, CSRs were directed at health and Welfare, Environment, and Security and General Social activities during 2008.

8. Survey Coverage

To achieve good coverage of cross-border activity, the Bank collated a list of enterprises with Foreign Assets and Liabilities (FAL) from the Ghana Investment Promotion Centre (GIPC), Registrar General's Department, Ghana Free Zones Board and the Internal Revenue Service (list of top 100 large tax payers). In all, questionnaires were administered to 318 enterprises with FALs spread across the regions (except Upper East and West). Of the distributed questionnaires, 274 were duly completed and returned, indicating a high response rate of 86.2%. Survey responses indicated that 247 out of the administered questionnaires, representing 77.7%, were received from enterprises in the Greater Accra Region, reflecting the dominance of head offices of most of the entities in the capital.

Fig. 4: Survey Responses by Region



9. Conclusion and Policy Recommendations

The 2009 survey of cross border capital flows has underscored Ghana's attractiveness as a foreign investment destination. The momentum of increased private capital flows between 2007 and 2008 needs to be sustained with sound economic frameworks and more openness towards better integration into the world economy.

In sum, the survey findings established that:

- Majority of the entities with Foreign Assets and Liabilities (FALs) were located in the Accra–Tema Metropolis and operated in the three top sectors of Manufacturing; Finance, Insurance, Real Estate, Tourism & Business Services; and Transport, Storage and Communication.

- Foreign Liabilities increased in 2008 with significant portions in the form of FDI inflows while equity and long-term loans from related entities/shareholders also constituted a greater portion.

- There was a significant growth in equity (FDEI) due to new equity inflows and increased retained earnings. FDEI was mainly concentrated in the Mining and Quarrying; Transport, Storage and Communication; and Finance, Insurance, Real Estate, Tourism and Business Services sectors.

- The stock of Private Sector External Debt (PSED) increased significantly in 2008 on the back of the long-term debt acquired by the Mining and Quarrying sector.

- Based on data from the survey and estimates from other sources, the overall International Investment Position (IIP) showed an increased net liability IIP of GH¢5.99 billion in 2008 having increased from a net liability position of GH¢3.38 billion. This indicates Ghana's attraction of a significant amount of cross border capital during 2008.

Notwithstanding the increased private capital flows, for Ghana to attain cross-country development and lower the incidence of rural-urban migration, there may be the need to minimize the potential adverse effects of FDI concentration in particular regions and sectors. To achieve this,

- Policies aimed at improving the investment climate must be strengthened further to boost investor confidence;
- The provision of good infrastructure (roads, electricity and water) across the country must be intensified to spread the potential benefits of foreign direct investments especially in terms of employment generation; and finally
- The continuous monitoring of private capital flows in conformity with international best practices and standards needs to be encouraged for effective policy formulation.

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