STATE OF THE FINANCIAL SECTOR IN GHANA

Introduction

1. Ladies and Gentlemen, as you will all recall, I assumed the position of Governor in April, 2017. At the time the financial sector had been in a considerable state of turmoil with the DKM crisis in 2016 and nine banks already identified as undercapitalized after the Asset Quality Review (AQR) exercise undertaken by the Bank of Ghana. We immediately began work and tasked the undercapitalized banks to submit recapitalization plans and worked to implement same. In the process we also resolved two Banks through a Purchase and Assumption transaction with GCB Bank. This was a necessary action taken to ring-fence the troubled banks, and also to prevent spillovers to the rest of the banks and the economy as a whole. Following these undertakings, we have conducted a comprehensive assessment of developments in the financial sector including the conclusion of an investigative report that sought to outline the underlying causes of the failure of the two banks. These developments have paved the way for us to outline a comprehensive set of measures which when implemented will address the legacy problems in the sector and ensure sustainable reforms needed to solidly position the financial sector as a major growth driver to support the country's inclusive broad-based and inclusive growth agenda.

2. Before I proceed further, let me first recount a series of events and policies that has brought us where we are now. The background is important as it should help us understand what got us here and how we move forward. Ladies and Gentlemen, Ghana's financial sector liberalization policies sought to deepen intermediation to support economic growth and integrate the domestic economy with global financial markets. As a result, a number of key reforms were introduced in the early 2000s which resulted in the entry of several new banks with the expectation of stimulating competition and innovation, especially in financial products and services and drive financial inclusion to promote economic growth.

3. While these set of reforms promoted growth in the banking sector and some level of competition and production and innovation, the Ghanaian economy was faced with a confluence of shocks and severe macro headwinds from both domestic and external sources.

Starting from 2012 in particular, the economy was characterized by large fiscal and current account deficits, high and volatile exchange rate developments, and high inflation but low real GDP growth, all of which exerted significant pressures on the banking system. At the same time, the governance challenges in the banking system spilled over and significantly weakened financial sector supervision and regulation, while corporate governance structures were completely disregarded —a situation which exerted undue influence on risk systems and credit delivery in most banks. It is therefore not surprising that most banks' balance sheets deteriorated with large non-performing loans and significant capital erosion.

4. A comprehensive Asset Quality Review (AQR) conducted by the Bank of Ghana in 2016 showed severe deterioration in asset quality in the banking sector. The AQR results also showed substantial provisioning shortfalls in a subset of banks (with a combined capital needs of around 1.6% of GDP). These toxic balance sheets of banks contributed to a decline in credit to the private sector and higher lending rates and spreads, undermining the transmission of monetary policy rate to the economy through market rates. In addition, there was unusual forbearance by the Bank of Ghana, which resulted in the extension of significant amounts of Emergency Liquidity Assistance (ELA) to these ailing banks, some of which were uncollateralized with accompanying risks to both the Bank of Ghana, in terms resources to conduct monetary policy operations and reputation risks, and also to the banks themselves. This official liquidity injection, together with banks' reluctance to extend new credit, further increased excess liquidity in the economy, which became extremely expensive for the Bank of Ghana to mop in order to support the disinflation process.

5. It was also clear from BOG's banking supervisory reports that some banks and deposit taking institutions lacked good corporate governance structures and more worryingly, was the co-mingling of board and management responsibilities which significantly undermined credit and risk management policies. In fact, there were several owner/management conflicts in a number of banks, in addition to connected lending practices without due processes laid down to guide such practices. These owner/CEOs and related Executive and Non-Executive Directors were largely responsible for credit extension and consistently breached related party transaction limits by extending credits to themselves and relations, and in some cases approved fictitious placements with related and connected companies. Unfortunately, these activities were usually rubber-stamped and sanctioned by the boards and board chairs.

6. The problems in the financial sector were also reflected in the Microfinance or MFI sub-sector comprising MFCs, MLCs and FNGOs, and RCBs and the extent of distress in this sub-sector was characterized by severely impaired capital; inability to meet regulatory capital adequacy requirement; generally low asset quality; and liquidity crises. These have culminated in threats to depositors' funds thus eroding public confidence and undermining efforts to promote financial inclusion. Of the total number of 566 licensed MFIs in 2018, 211 are active but distressed or folded up. Also, out of the total number of 141 RCBs, 37 are active but distressed or folded up. In total, it is estimated that 272 out of the 707 institutions in the sub-sector, representing 38.5% are at risk. This indicates that approximately GH¢740.5 million is owed to an estimated 705,396 depositors of the distressed or folded up MFIs and RCBs. In terms of significance, the deposits under distress form 8.81% and 52.49% of industry total deposits of RCBs and MFIs respectively.

BOG Roadmap to Streamline the Banking Sector

7. Ladies and Gentlemen, as you would realize by now, poor banking practices, coupled with weak supervision and regulation by the Bank of Ghana has significantly undermined the stability of the banking and other non-bank financial institutions and we all know some of the consequences by now—revocation of licenses of two banks while other banks were placed under comprehensive capital restoration plans.

8. The financial sector cleanup has started but not completed and we have managed to keep a few weak banks in operation since August 2017. Today, we announce the continuation of the cleanup of the sector with the appointment of an administrator for uniBank by the Bank of Ghana. The Bank of Ghana has put uniBank under Official Administration to protect the stability of the financial sector. The official administrator will assume the responsibility of management and direction of the bank in a manner that contributes to the stability of the bank and the safety of depositors' funds. Broadly, the role of the Official Administrator will include the following:

- take management control over the institution, with powers that replace those of the shareholders, board of directors, and senior management.
- be responsible for preserving the assets and liabilities of the bank, preparing a final resolution plan, and restructuring the bank under the oversight of Bank of Ghana.

- granted a specific time frame (six months as prescribed by the BSDI Act) in which to thoroughly analyze the bank's condition and prepare a feasible rehabilitation plan.
- handle all contacts with the media after the intervention period
- ensure that the bank remains open to maintain confidence in the banking system by allowing depositors access to their funds and other banking services.

9. In taking this decision, we wish to note that UniBank Ghana Limited has been faced with severe insolvency and liquidity challenges over the past two years, with persistent clearing deficits resulting in extensive reliance on the Bank of Ghana's Emergency Liquidity Assistance (ELA) instrument since 2015. As a result, BOG is heavily exposed to UniBank to the tune of GH¢2.2 billion, of which GH¢1.6 billion is unsecured.

The bank also faces a significant capital shortfall. On March 20th, 2017, BOG's directed uniBank, per a letter, to submit a capital plan and resolve its significant undercapitalization within one hundred and eighty (180) days from the date of the letter in accordance with Section 106(1) of the Banks and SDIs Act, 2016 (Act 930). Since then, uniBank's Capital Adequacy Ratio (CAR)has rather deteriorated into the negatives from September 2017, and in a much more distressed condition with CAR of negative 24.02% and capital deficit of GH¢1.18 billion as of December 2017.

This notwithstanding, the bank has continued to increase its asset base (granting new loans to clients) to GH¢6.1 billion in December 2017 from GH¢4.9 billion in September — amidst increasingly poor loan asset quality. The bank's gross loans increased by GH¢760.67 million within the same period. As a result, its non-performing loans (NPLs) have remained high, further eroding the capital base of the bank and presenting liquidity challenges.

The reserve ratio (a measure of liquidity) has remained consistently below 1.0 percent since October 2017 compared to the regulatory minimum of 10 percent, resulting in a constant liquidity shortfall, and continued reliance on the BOG's Emergency Liquidity Assistance facility.

In line with these developments, BOG's Banking Supervision Department has reached the conclusion that uniBank is currently insolvent under Section 123 (4) of the Banks and SDIs Act, 2016 (Act 930), and in breach of all its key prudential regulatory requirements. Despite persistent pleas for extension over the past year, the shareholders have failed to restore the bank to regulatory capital and liquidity levels. The bank's current situation reflects its poor corporate governance and risk management practices that rendered the bank vulnerable to macroeconomic shocks.

2018 and Beyond – Improving the Supervisory and Regulatory Environment

10. While several important steps have been taken thus far, a lot remains to be done to restore safety, soundness and stability in the financial sector. Going forward, the BOG will continue to strengthen its regulatory and supervisory framework, and promote confidence in the financial system through the:

- Introduction of the Basel Regulatory Capital Requirement Directive.
- Review of guidelines, directives and regulations to the industry in line with the new Banks and Specialized Deposit-taking Institutions Act, 2016 (Act 930).
- Roll-out of the Basel II/III supervisory framework, and ensure implementation of IFRS 9 by banks;
- Full implementation of the new minimum capital requirements for banks by end-December 2018 deadline. To this end, the BOG will issue guidelines to the industry on compliance with the capital increase directive of 2017 and strictly monitor compliance;
- Address specific risks from high NPLs, poor corporate governance and poor risk management systems. To this end, we will issue directives on corporate governance, risk management (including cyber and information security-related risks);
- Strictly enforce Fit and Proper Guidelines for Shareholders, Directors and Key Management Personnel of Banks and SDIs as well as other supervised Non-Bank Financial Institutions to ensure bad behavior is not recycled within the financial sector;
- Strengthen the capacity and resources of the Banking and Supervision Department, undertake a comprehensive review and improvement of all supervisory processes, and ensure strong enforcement of prudential and conduct regulatory requirements;
- Strengthen overall financial stability risk assessments and establish adequate measures to promote stability of the financial system;

- Roll out implementation of the deposit insurance scheme established under the Ghana Deposit Protection Act, 2016 (Act 931),
- Introduce Banking Sector Cyber and Information Security Guidelines to protect consumers and create a safer environment for online and e-payments products in line with the government's interoperability objective, and finally
- Improve collaboration with other regulatory bodies to prevent regulatory arbitrage;

Conclusion

11. The outlook for the financial sector is positive and BOG remains committed to promoting strong, viable and stable banks, SDIs, RCBs, and MFIs to support the country's growth and development process. In the months ahead, we will engage with stakeholders as we design specific measures to strengthen systems and processes that would improve the industry.